



# Directors of Commonwealth Authorities and Companies – Legal Duties & Liabilities

A guide

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## Introduction

Minter Ellison has prepared this Guide for persons serving on, or considering serving on, the boards of Commonwealth companies or authorities. It covers their legal duties and obligations, focusing in particular on the *Corporations Act 2001* (Cth) (**Corporations Act**) and the *Commonwealth Authorities and Companies Act 1997* (Cth) (**CAC Act**).

It is prudent for appointees and prospective appointees to boards of Commonwealth companies and authorities to raise questions about the legal duties and obligations imposed on directors and to consider the extent of the potential personal liability associated with holding such positions.

The Guide is in three parts. Part One outlines the key statutory duties of directors, the sources of those duties and the possible liabilities for breach. Part Two looks at key measures for directors to manage their potential exposure to personal liability. Part Three is comprised of checklists focusing on issues that commonly arise that are relevant, in particular, to directors of Commonwealth companies.

## Definitions

### Companies

In the CAC Act, 'Commonwealth company' is defined to mean a Corporations Act company that the Commonwealth controls (other than a subsidiary of a Commonwealth authority or Commonwealth company) (section 34(1)). The Commonwealth will be taken to control a company if it:

- a) controls the composition of the company's board (the Commonwealth will be taken to do so under section 34(1B) if it can appoint or remove all, or the majority, of the directors of the company); or
- b) is in a position to cast, or control the casting of, more than one-half of the maximum number of votes that might be cast at a general meeting of the company; or
- c) holds more than one-half of the issued share capital of the company (excluding any part of that capital carrying no right to participate beyond a specified amount in a distribution of either profits or capital).

'Wholly owned Commonwealth company' is defined in the CAC Act to mean any Commonwealth company other than one whose shares are beneficially owned by a person other than the Commonwealth (section 34(2)).

Although the provisions of the Corporations Act (where relevant) apply to Commonwealth companies, the CAC Act sets out additional restrictions or obligations on Commonwealth companies and wholly owned Commonwealth companies (several of which are mentioned in this Guide).

In this Guide:

- a) 'company' means any company incorporated under the Corporations Act, including Commonwealth companies; and
- b) 'Commonwealth company' has the meaning given in the CAC Act.

### Authorities

'Commonwealth authority' is defined in section 7(1) of the CAC Act to mean either of the following kinds of body that holds money on its own account:

- a) a body corporate that is incorporated for a public purpose by an Act;
- b) a body corporate that is incorporated for a public purpose by:
  - (i) regulations under an Act; or
  - (ii) an Ordinance of an external Territory (other than Norfolk Island) or regulations under such an Ordinance,
 and is prescribed as such by regulations under the CAC Act.

The CAC Act specifies that companies incorporated under the Corporations Act are not Commonwealth authorities (section 7(2)). Accordingly, a Commonwealth company cannot be a Commonwealth authority and vice versa.

The Corporations Act does not apply to Commonwealth authorities, although the CAC Act contains a number of provisions equivalent to provisions of the Corporations Act, including certain directors' duties provisions described in this Guide.

In this Guide, 'Commonwealth authority' and 'authority' are used interchangeably to mean a 'Commonwealth authority' as defined in the CAC Act.

## Officers

The expression 'officer' is broadly (and differently) defined in the Corporations Act and the CAC Act (see below) to include not only directors, but also a range of other persons of importance to the entity. Many of the legislative provisions discussed in this Guide apply to officers generally, while other provisions are applicable to directors only – we have identified which is the case in each instance.

## Officers of companies

In section 9 of the Corporations Act, 'officer' of a corporation (which includes a company) is defined to mean:

- a) a director or secretary of the corporation;
- b) a person:
  - (i) who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation;
  - (ii) who has the capacity to affect significantly the corporation's financial standing;
  - (iii) in accordance with whose instructions or wishes the directors of the corporation are accustomed to act (excluding advice given by the person in the proper performance of functions attaching to the person's professional capacity or their business relationship with the directors or the corporation);
- c) a receiver, or a receiver and manager of the property of the corporation;
- d) an administrator of the corporation;
- e) an administrator of a deed of company arrangement executed by the corporation;
- f) a liquidator of the corporation; or
- g) a trustee or other person administering a compromise or arrangement made between the corporation and someone else.

In the context of discussing companies, references to 'officers' in this Guide will mean all persons meeting the definition above from the Corporations Act.

## Officers of authorities

In section 5 of the CAC Act, 'officer', in relation to a Commonwealth authority, is defined to mean:

- a) a director of the authority; or
- b) a senior manager of the authority.

The definition of 'senior manager' of an authority is similar to paragraph (b) of the definition of 'officer' under the Corporations Act. 'Senior manager' is defined in section 5 of the CAC Act to mean a person (other than a director of the authority, a Minister, or an APS employee engaged as an employee for the purposes of an Agency other than the authority) who:

- a) makes, or participates in making, decisions that affect the whole, or a substantial part, of the operations of the authority; or
- b) has the capacity to affect significantly the authority's financial standing.

In the context of discussing authorities, references to 'officers' in this Guide will mean all persons meeting the definition above from the CAC Act.

## 1 Key duties

Part 1 of this Guide sets out the key general duties of:

- a) directors of companies incorporated under the Corporations Act, including the directors of Commonwealth companies incorporated under that Act; and
- b) directors of Commonwealth authorities under the CAC Act, such duties being comparable to those of company directors.

Several other legislative provisions clarifying the scope of the duties of directors are also considered.

### Duty of care and diligence

#### Companies

Directors and other officers 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 or officer of a company in the company's circumstances, and occupied the office held by, and had the same responsibilities within the company as, the director or officer (section 180(1) of the Corporations Act).

It is clear that the standard of care and diligence required must be assessed by reference to the particular circumstances of the director or officer concerned.

#### Authorities

The CAC Act mirrors this duty for directors and other officers of Commonwealth authorities (section 22(1)).

### Business judgment rule

#### Companies

The 'business judgment rule' is contained in section 180(2) of the Corporations Act. The essence of the rule is that a director or officer of a company will be taken to have met the requirements of the duty of care and diligence, both under the legislation and at general law, in making a business judgment (defined as any decision to take or not take action in respect of a matter relevant to the business operations of the company) if the director or officer:

- made the judgment in good faith for a proper purpose;
- did not have a material personal interest in the subject matter of the judgment;

- informed themselves about the subject matter of the judgment to the extent they reasonably believed to be appropriate; and
- rationally believed that the judgment was in the best interests of the company.

It is presumed that the director's or officer's belief that a business judgment is in the best interests of the company is a rational one unless the belief is one that no reasonable person in the director's or officer's position would hold.

The protection provided by the business judgment rule only applies in relation to the duty of care and diligence, not to any other duty.

#### Authorities

The CAC Act contains an equivalent business judgment rule for directors and other officers of Commonwealth authorities (section 22(2)).

### Liability for breach

There are potential civil penalties (rather than criminal liability) under the Corporations Act or CAC Act (as the case may be) for a breach of the duty of care and diligence. Civil penalties include fines, orders to pay compensation for damage suffered by the company/authority, and disqualification from managing any bodies corporate.

The director is also exposed to a possible action by the company/authority for breach of the general law fiduciary duty corresponding with the legislative duty. Possible liability for such breach includes payment of compensation to the company/authority.

### Duty of good faith

#### Companies

Directors and other officers must exercise their powers and discharge their duties in good faith in the best interests of the company and for a proper purpose (section 181(1) of the Corporations Act).

## Authorities

The CAC Act mirrors this duty for directors and other officers of Commonwealth authorities (section 23(1)), subject to the effect of section 27A of the CAC Act discussed below.

## Best interests

There have been many cases on the meaning of the term 'in the best interests of the company' but it is clear that, subject to special duties owed to creditors prior to insolvency, the duty to act in good faith is owed to the company itself.

This duty presents unique problems in company groups where directors may feel that they must act in the interests of their appointors or in the interests of a particular shareholder. The problem is more profound where the company is owned by both government and industry.

Nonetheless, regardless of whether the company is wholly owned by government or jointly owned by both government and industry, a company director is bound to act in good faith in the best interests of the company and is not entitled to put the perceived interests of government or of any other third party ahead of the company's interests.

The constitution or enabling legislation (as the case may be) of the company or authority may contain provisions enabling the relevant Minister to issue directions to the Board. For example, section 143 of the *Primary Industries and Energy Research and Development Act* provides that the Minister may give an R & D corporation written directions about the performance of its functions and the exercise of its powers. In many cases, the constitution or enabling legislation deems a Ministerial direction to be 'in the best interests' of the company or authority.

## Liability for breach

There are potential civil penalties for a breach of the duty to act in good faith in the best interests of the company and for a proper purpose. There is potential criminal liability if the director or officer has been reckless or intentionally dishonest (section 184(1) of the Corporations Act, section 26(1) of the CAC Act).

The director is also exposed to a possible action for breach of the corresponding general law fiduciary duty.

## Use of position

### Companies

Directors, officers and employees of a company must not improperly use their position to gain an advantage for themselves or for another person, or to cause detriment to the company (section 182(1) of the Corporations Act).

### Authorities

The CAC Act mirrors this duty for directors, officers and employees of Commonwealth authorities (section 24(1)), subject to the effect of section 27A of the CAC Act discussed below.

### Liability for breach

There are potential civil penalties for a breach of this duty, as well as potential criminal liability if directors, officers or employees use their position dishonestly or recklessly (section 184(2) of the Corporations Act, section 26(2) of the CAC Act).

The director is also exposed to a possible action for breach of the corresponding general law fiduciary duty.

## Use of information

### Companies

Directors, officers and employees of a company must not improperly use information obtained by virtue of their position to gain an advantage for themselves or for another person, or to cause detriment to the company (section 183(1) of the Corporations Act).

### Authorities

The CAC Act mirrors this duty for directors, officers and employees of Commonwealth authorities (section 25(1)), subject to the effect of section 27A of the CAC Act discussed below.

### Liability for breach

There are potential civil penalties for a breach of this duty, as well as potential criminal liability if the director, officer or employee had used the information dishonestly or recklessly (section 184(3) of the Corporations Act, section 26(3) of the CAC Act).

The director is also exposed to a possible action for breach of the corresponding general law fiduciary duty.

## Limitation of duties of directors of Commonwealth authorities

### No breach for doing an act required by CAC Act

Section 27A(1)(a) of the CAC Act provides that an officer (including a director) does not contravene sections 23, 24 or 25 (obligations relating to good faith, use of position and use of information), or their equivalent duties at common law and in equity, by doing an act that another provision of the CAC Act requires the officer to do.

### APS employee or Agency Head acting in the course of their duties

Section 27A(1)(b) provides that an officer of a Commonwealth authority does not contravene sections 23, 24 or 25, or their equivalent duties at common law and in equity, by doing an act in the course of the performance of their duties as an APS employee or Agency Head.

Section 27A(2) clarifies that the public services exemption does not apply if the enabling legislation for the Commonwealth authority establishes a Statutory Agency in relation to the Commonwealth authority and the officer is the Agency Head or an APS employee in the Statutory Agency. That is, the exemption is to apply only where officers are APS employees or Agency Heads not employed within the same Commonwealth authority, to provide protection against conflict between a person's duty as an APS employee and as an officer of the authority.

As the provision has yet to be tested in the courts, the precise extent of the protection afforded by section 27A(1) has not yet been determined.

There is no corresponding provision applicable to directors and officers of Commonwealth companies.

## Reliance on expert advice

### Companies

In determining whether a director has performed one of the duties under the Corporations Act listed above in this Guide or an equivalent general law duty, section 189 of the Corporations Act contains a rebuttable presumption that a director's reliance on information or professional or expert advice is reasonable in certain circumstances.

Section 189 provides that the director's reliance on information or advice is taken to be reasonable, unless the contrary is proved, if it was given or prepared by:

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

and the reliance on it was made in good faith after making 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.

### Authorities

The CAC Act contains an equivalent presumption with regard to directors of Commonwealth authorities (section 27D).

## Delegation by directors

### Companies

The Corporations Act authorises the directors of a company to delegate any of their powers not only to a committee of directors, but to a single director, an employee of the company or any other person, subject to any restrictions in the constitution of the company (section 198D).

However, section 190 of the Corporations Act provides that a director will continue to be responsible for the exercise of the power by the delegate unless:

- the director believed on reasonable grounds at all times 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
- the director believed on reasonable grounds, in good faith and after making proper inquiry if the circumstances indicated the need for inquiry, that the delegate was reliable and competent in relation to the power delegated.

### Authorities

The CAC Act contains an equivalent provision to section 190 of the Corporations Act, applying to delegations by authority directors of powers under the authority's enabling legislation (section 27E).

## Specific CAC Act obligations on directors

In addition to the general duties of directors, the CAC Act and Regulations place a series of specific obligations on directors; these include:

	Section	Directors' Obligation
<b>Authority</b>	Annual report 9(1)	Prepare an annual report in accordance with Schedule 1 for each financial year and give it to the responsible Minister in accordance with section 9(2). Not cause the reporting rule in section 9 to be contravened, and not fail to take reasonable steps to secure compliance (civil penalty). Dishonest contravention or failure is a criminal offence. (Note the availability of a defence if omission of information was immaterial and did not affect the giving of a true and fair version if contravention is an omission from financial statements.)
	Audit of subsidiaries 12(1)	Do whatever is necessary to ensure all relevant subsidiaries' financial statements are audited by Auditor-General.
	Auditor-General's report 12(3)	Give Auditor-General's report under section 12(2) to the responsible Minister together with a copy of subsidiaries' financial statements.
	Interim reports 13(3)	Give the interim report required by section 13(3) to the responsible Minister.
	Budget estimates 14	If not a Government Business Enterprise (GBE), prepare budget estimates for each financial year and any other periods directed by the responsible Minister.
	Significant events 15	Give the responsible Minister written particulars of any proposal by the authority or any of its subsidiaries to: <ul style="list-style-type: none"> <li>a) form a company or participate in the formation of a company;</li> <li>b) participate in a significant partnership, trust, unincorporated joint venture or similar arrangement;</li> <li>c) acquire or dispose of a significant shareholding in a company;</li> <li>d) acquire or dispose of a significant business activity;</li> <li>e) commence or cease a significant business activity;</li> <li>f) make a significant change in the nature or extent of its interest in a significant partnership, trust, unincorporated joint venture or similar arrangement.</li> </ul> Exemptions may be granted and written guidelines given to the directors by the responsible Minister.
	Informing Minister 16	Within the time limits set by the relevant Minister: <ul style="list-style-type: none"> <li>a) keep the responsible Minister informed of the operations of the authority and its subsidiaries;</li> <li>b) give the responsible Minister such reports, documents and information as the Minister requires;</li> <li>c) give the Finance Minister such reports, documents and information as the Finance Minister requires.</li> </ul>
	Corporate Plan – GBE 17	If a GBE, prepare a corporate plan for the authority (including any subsidiaries) at least once a year and give it to the responsible Minister. In addition, keep the responsible Minister informed about significant changes to the plan and matters that arise that might significantly affect the achievement of the objectives. (The responsible Minister may give written guidelines to the directors that are to be used by the directors in deciding which matters are to be covered by the plan.)

	Section	Directors' Obligation
	Accounting Records 20	Not cause the authority to contravene obligation to keep, retain, and make available accounting records under sections 20(1), 20(2) and 20(3), and not fail to take reasonable steps to secure such compliance (civil penalty). Dishonest contravention or failure is a criminal offence. (Note that this obligation extends to senior manager of the authority.)
	General Policy Order 28	Ensure that the authority complies with a General Policy Order applying to the authority and that, as far as practicable, the subsidiaries of the authority comply with that General Policy Order.
	Aligning accounting periods of subsidiaries 30	Ensure, and do whatever is necessary to ensure, that the annual accounting period of any subsidiaries becomes, or remains, the same as the authority's financial year, and not fail to take reasonable steps to secure such compliance (civil penalty). Dishonest contravention or failure is a criminal offence. Exemptions from section 30 may be granted by the Finance Minister.
	Audit Committee 32	Establish and maintain an audit committee.
	Government Procurement Requirements 47A	If the Regulations specify that government procurement requirements apply to the authority, ensure that directions related to procurement are complied with by the authority and, as far as practicable, by its subsidiaries.
<b>Company</b>	Annual report 36(1B) and (1C)	Not cause the company to contravene the obligation to give the responsible Minister reports or information under sections 36(1) and 36(1A), and not fail to take reasonable steps to secure such compliance (civil penalty). Dishonest contravention or failure is a criminal offence.
	Audit of subsidiaries 37(1)	Do whatever is necessary to ensure all relevant subsidiaries' financial statements are audited by Auditor-General.
	Auditor-General's report 37(3)	Give Auditor-General's report under section 37(2) to the responsible Minister together with a copy of subsidiaries' financial statements.
	Interim reports 38(3)	Give the interim report required by section 38(1) to the responsible Minister.
	Budget estimates 39	If a wholly owned Commonwealth company (other than a GBE), prepare budget estimates for each financial year and any other periods directed by the Minister.
	Significant events 40	<p>If a wholly owned Commonwealth company, give the responsible Minister written particulars of any proposal by the company or any of its subsidiaries to:</p> <ul style="list-style-type: none"> <li>a) form a company or participate in the formation of a company;</li> <li>b) participate in a significant partnership, trust, unincorporated joint venture or similar arrangement;</li> <li>c) acquire or dispose of a significant shareholding in a company;</li> <li>d) acquire or dispose of a significant business;</li> <li>e) commence or cease a significant business activity;</li> <li>f) make a significant change in the nature or extent of its interest in a significant partnership, trust, unincorporated joint venture or similar arrangement.</li> </ul> <p>Exemptions may be granted and written guidelines given to the directors by the responsible Minister.</p>

	Section	Directors' Obligation
	Informing Minister 41	If a wholly owned Commonwealth company: a) keep the responsible Minister informed of the operations of the company and its subsidiaries; b) give the responsible Minister such reports, documents and information as the Minister requires; c) give the Finance Minister such reports, documents and information as the Finance Minister requires,  within the time limits set by the relevant Minister.
	Corporate Plan – GBE 42	If a wholly owned Commonwealth company that is a GBE, prepare a corporate plan for the company (including any subsidiaries) at least once a year and give it to the responsible Minister. In addition, keep the responsible Minister informed about significant changes to the plan and matters that arise which might significantly affect the achievement of the objectives. (The responsible Minister may give written guidelines to the directors that are to be used by the directors in deciding which matters are to be covered by the plan.)
	General Policy Order 43	If a wholly owned Commonwealth company, ensure that the company complies with a General Policy Order applying to the company and that, as far as practicable, the subsidiaries of the company comply with that General Policy Order.
	Audit Committee 44	If a wholly owned Commonwealth company, establish and maintain an audit committee (see also Regulation 68).
	Government Procurement Requirements 47A	If the Regulations specify that government procurement requirements apply to a wholly owned Commonwealth company, ensure that directions related to procurement are complied with by the company and, as far as practicable, by its subsidiaries.

## Conflicts of interest

### Companies

Extensive case law and statutory regulation have developed around conflicts of interest of company directors. The essential issue is whether a director can bring an independent mind to bear on a matter, or whether the conflicting interest or duty is so significant as to divide his or her loyalties. If a director has another interest or duty and there is a real possibility of conflict, that other interest must be disclosed and the director should consider declining to receive board papers and leaving the meeting when the issue is discussed.

The fundamental principle is that directors must act in the best interests of the company as a whole. In the context of a company wholly owned by the Commonwealth, the interests of the shareholder (the Commonwealth) will often (but not necessarily always) coincide with the interests of the company as a whole.

Sections 191 and 192 of the Corporations Act require directors to give notice to the other directors of material personal interests, subject to specified exceptions. The term 'material personal interest' is not defined in the legislation. The Corporations Act does not require that an interest be financial to be considered a 'material personal interest'.

Section 193 confirms that sections 191 and 192 have effect in addition to, and not in derogation of, any general law rule or provision in a company's constitution about conflicts of interest.

For proprietary companies, the issue of whether or not the director may vote on the matter is usually regulated by the company constitution, and this frequently allows a director to vote provided that notice of the interest has been given (as does the corresponding 'replaceable rule' in section 194 of the Corporations Act). The Corporations Act does not prohibit the director voting on the matter.

For public companies, which include companies limited by guarantee, a director with a material personal interest in a matter must not be present or vote, subject to specified exceptions (section 195). The Corporations Act does not allow the company to relax this restriction.

### Authorities

Sections 27F, 27G and 27H of the CAC Act are provisions with respect to directors of Commonwealth authorities equivalent to sections 191, 192 and 193 of the Corporations Act.

Under section 27J, an equivalent provision to section 195 of the Corporations Act, a director with a material personal interest in a matter must not be present or vote on that matter, subject to specified exceptions. Under section 27K, the responsible Minister may declare that a director may be present and vote on a matter in relation to which he or she has a material personal interest.

Additional provisions regarding conflicts of interest may be contained in the authority's enabling legislation.

### Liability for breach

A breach by a company director of their obligation under section 191 of the Corporations Act to disclose material personal interests is a criminal offence of strict liability, with a maximum penalty of \$1,100 and/or 3 months' imprisonment. A breach by a public company director of the section 195 restriction on being present or voting is a criminal offence of strict liability, with a maximum penalty of \$550.

A penalty of \$1,100 applies for a failure to disclose a material personal interest under section 27F of the CAC Act and a penalty of \$550 for being present or voting (section 27J of the CAC Act). An authority's enabling legislation may also provide for sanctions (for example, termination of the director's appointment).

### Other sources of potential liability

Breaches of any of the key duties listed above in this Guide are by no means the only sources of potential personal liability for directors of Commonwealth companies and authorities. Other sources of potential personal liability (which are not within the scope of this Guide) include the sources set out below.

### Liability for breach of general law fiduciary duties

The statutory duties are based on equivalent, but not identical, general law fiduciary duties, which continue to apply. Legal action can be taken against a director for both

breach of a statutory duty and breach of the corresponding general law fiduciary duty. An action for a breach of a general law fiduciary duty will be considered in certain circumstances as both the duty and the available remedies may be wider than for the equivalent statutory duty.

### Liability for breaches of other provisions of the Corporations Act/CAC Act

Directors can be personally liable for breaches of other provisions of the Corporations Act/CAC Act, including in some cases in relation to obligations of the company/authority as well as for breaches of obligations imposed directly on directors, for example in relation to:

- insolvent trading by the company; and
- statements in, or omissions from, a prospectus.

### Liability for breaches of other legislation

Directors can be personally liable for failing to ensure that the corporate vehicles they manage comply with statute law. Commonwealth legislation generally imposes secondary liability on a director where the corporation has contravened the legislation. As such, the liability is strict. If the corporation is liable, the director or officer is automatically deemed liable as well. The onus is then placed on the director to make out one of the statutory defences (if available) to avoid liability.

In many cases, the liability can attach to a broad range of persons, including chief executive officers, executive officers, directors, public officers, body corporate managers, secretaries and other officers. Examples of Commonwealth legislation imposing liability on directors by virtue of the corporation's breach include:

- the Trade Practices Act (eg offences relating to unfair practices and product safety and product information);
- Customs Act;
- environmental laws (eg offences relating to Commonwealth land, failing to comply with requirements for approvals or conditions on approval, National Greenhouse and Energy Reporting); and
- taxation laws.

### Liability in tort

Directors will be personally liable for torts committed by them when carrying out their responsibilities as director, for example their:

- negligent acts or omissions; and
- defamatory comments.

## 2 Managing exposure

This Part sets out a summary of the legal position regarding availability of indemnities and insurance for directors of Commonwealth companies and authorities, being 2 key measures for directors to manage their potential exposure to personal liability.

The scope of this Part does not include consideration of general risk management and compliance measures used to assist in limiting potential legal liability by reducing the likelihood of a liability arising in the first place. Nor does this Part specifically address personal liabilities that may arise under other legislation or specific legislative provisions, other than the Corporations Act or the CAC Act, which may void indemnities (eg section 77A of the Trade Practices Act).

### Indemnification of directors

#### Companies

##### Prohibition on exemption from liability to company

The Corporations Act prohibits a company (and a related body corporate) from exempting its directors and other officers (whether directly or through an interposed entity) from a liability to the company incurred as a director or officer of the company (section 199A(1)).

##### Indemnities against liabilities to company and third parties

A company (and a related body corporate) is also prohibited (under section 199A(2)) from indemnifying its directors and other officers (whether by agreement or by making a payment and whether directly or through an interposed entity) against any of the following liabilities (other than legal costs) incurred as a director or officer of the company:

- a liability owed to the company itself (or a related body corporate);
- a liability for a fine or a compensation order; or
- a liability owed to a third party (ie a party other than the company or a related body corporate) that did not arise out of conduct in good faith.

Accordingly, a company may indemnify its directors and officers against liabilities to third parties other than those falling within the last two points above.

##### Indemnity against legal costs

A company (and a related body corporate) is prohibited (under section 199A(3)) from indemnifying its directors and other officers (whether by agreement or by making a payment and whether directly or through an interposed entity) against legal costs incurred in defending an action for a liability incurred as a director or officer of the company if the costs are incurred:

- in defending or resisting proceedings where the director or officer is found to have a liability for which they could not be indemnified under section 199A(2);
- in defending or resisting criminal proceedings in which the director or officer is found guilty;
- in defending or resisting proceedings brought by ASIC or a liquidator for a court order if the grounds for making the order are found by the court to have been established; or
- in connection with proceedings for relief to the director or officer under the Corporations Act in which the court denies the relief.

Accordingly, a company may indemnify its directors and other officers against legal costs incurred in their capacity as director or officer other than those prohibited under section 199A(3) as described above. For example, a company may indemnify its directors against costs incurred in defending civil or criminal proceedings where the director or officer is found not liable or not guilty.

##### Company constitution

It is not uncommon for a company constitution to contain a form of indemnity for its directors and other officers, to the extent allowed by the Corporations Act.

##### Authorities

The CAC Act contains equivalent provisions with regard to indemnification of directors and other officers of Commonwealth authorities (section 27M).

### Void indemnities

Anything that purports to indemnify a director or other officer of a company/authority against a liability, or exempt them from a liability, is void to the extent that it contravenes section 199A of the Corporations Act or section 27M of the CAC Act (section 199C(2) of the Corporations Act, section 27P(2) of the CAC Act).

### Indemnities from the Commonwealth

See below for the position regarding Commonwealth indemnities.

### Deeds of indemnity

It is common practice for directors to enter a deed of indemnity with the company/authority, particularly if there is no indemnity contained in the constitution/enabling legislation. The advantage to directors in entering such a deed is to create a personal contractual right to indemnification, regardless of the company constitution or enabling legislation for an authority.

In the case of indemnities against legal costs, the legal ability of the company or authority to provide the indemnity cannot be determined until the conclusion of the proceedings. A benefit to a director of obtaining a deed of indemnity is that the deed may make provision for a form of contingent protection. For example, it may allow the company to fund the director's legal proceedings by making a loan, which is repayable in the event that the director is found liable or guilty.

## Insurance for directors

### Companies

Section 199B of the Corporations Act prohibits a company (and a related body corporate) from paying, or agreeing to pay (whether directly or through an interposed entity), the premiums for insurance policies taken out to cover liability of its directors and other officers (D&O insurance) arising out of:

- conduct involving a wilful breach of duty in relation to the company;
- improper use of company information; or
- obtaining improper advantage from their office.

Companies may pay the premiums for insurance to cover all other liabilities of directors and officers, although there are limitations regarding the liabilities for which insurers are willing to provide insurance.

The insurance policy can also cover the costs of defending legal proceedings, regardless of the outcome of the proceedings.

### Authorities

The CAC Act contains equivalent provisions with regard to insurance of directors and other officers of Commonwealth authorities (section 27N).

### Void insurance

Anything that purports to insure a director or other officer of a company/authority against a liability is void to the extent that it contravenes section 199B of the Corporations Act or section 27N of the CAC Act (section 199C(2) of the Corporations Act, section 27P(2) of the CAC Act).

### D&O insurance

Directors should ensure that D&O insurance is obtained for them and should carefully consider the scope of the cover. It is usual for companies and authorities to effect and maintain such insurance for their directors, subject to the restrictions described above. In the case of a company, a requirement that the company take out D&O insurance may be set out in its constitution.

Commonwealth companies and authorities that are within the Government General Sector are covered by Comcover for insurable risks.

D&O insurance usually only covers claims made during the term of the policy. Consequently, it is not unusual for directors of Commonwealth companies and authorities to enter into a deed with the company/authority obliging it to maintain, at its expense, D&O insurance for the benefit of the director for seven years after they cease to hold office as a director. Such deeds are sought by directors of companies even where such obligation is contained in the company constitution.

The benefit to directors of such a deed is that it imposes a contractual obligation on the company/authority to ensure that insurance is maintained for the former director to cover claims that may be made against them in relation to their term as a director during the statute of limitations period (which is usually six years – subject to certain limited exceptions). Former directors should ensure that the policy is, in fact, put in place. Such deeds usually require the company or authority to provide evidence of the required insurance if requested by the former director, and it is advisable for the director to exercise this right.

### Indemnities and assistance provided by the Commonwealth to directors of Commonwealth companies and authorities

The circumstances in which a director of a Commonwealth company or authority may be able to obtain an indemnity, or assistance in legal proceedings, from the Commonwealth, rather than from the company or authority itself, are limited.

### Assistance to Commonwealth employees for legal proceedings – Legal Services Directions

The Attorney-General's Department Legal Services Directions 2005 (as amended 1 July 2008) contain, at Appendix E, the Commonwealth's policy for handling requests for assistance in relation to legal proceedings by a Commonwealth employee or former employee.

In relation to Commonwealth employees who are directors of Commonwealth companies and authorities, the Directions specifically provide (at paragraph 3 of Appendix E) that:

'Expenditure to assist a Commonwealth employee in respect of activities the employee undertakes for a Commonwealth authority or company covered by the CAC Act (in particular, by being on the board) is to be approved only to the extent that the employee is not indemnified or insured by the authority or company. (See Department of Finance and Administration Finance Circular 1997/19.)'

However, Finance Circular 1997/19 is no longer current and has not been replaced.

## 3 Checklist for directors of Commonwealth companies

This Part contains checklists developed to assist directors identify issues that commonly arise or that are relevant to them as members of Boards of Commonwealth companies. Most of the issues listed are also applicable to directors of Commonwealth authorities, who will each also need to have regard to their authority's enabling legislation.

### Checklists for directors of Commonwealth companies

#### The director's role

- Who appoints you and removes you?
- Are the criteria for board appointments clearly stated?
- Is there a clearly defined division of responsibilities?
- Are you expected to report to your appointor? If so, what are your confidentiality obligations to the company? Is your reporting obligation consistent with your legal obligations to the company?
- What are the requirements for attendance at:
  - Board meetings?
  - Board committee meetings?
  - other company business?
- What special skills do you bring to the Board?
- Are new directors appropriately briefed on appointment regarding the company generally and their governance responsibilities?

### Conflicts of interest

- What are the possible areas of conflict of interest?
- Has the Board developed a Code of Conduct defining the standards of behaviour to which the directors and employees of the company are required to adhere? Is adherence to the Code of Conduct regularly reviewed?
- What does the constitution say about conflicts of interest, in particular regarding:
  - disclosure?
  - absenting yourself?
  - receipt of Board papers on an issue of conflict?
  - voting on issues where a conflict arises?
- Have you made a conflict disclosure? Have you kept it up to date?
- Does a matter under consideration by the Board involve a conflict for you? Have you disclosed that conflict?
- Should you decline to receive board papers on the matter?
- Should you leave the meeting while the matter is discussed/decided?
- Should you resign due to the conflict?

### The Board's role

- Is the role of the Board clearly defined and documented in a Board Charter?
- Is there a strategy in place approved by the Board?
- Are annual objectives set out in an annual plan approved by the Board?
- Have you read and understood the annual corporate plan/statement of corporate intent and business plan?
- Are you aware of the company's formal policies and procedures?
- Do you understand the role and powers of the audit committee and other committees of the Board?
- Are executive reports/recommendations to the Board adequate, eg:
  - sufficient background?
  - supported by fact?
  - clear recommendations?
  - confirmation of compliance with established company policy?
  - supported by financial and legal advice?
- Do you have sufficient familiarity with the key executives' experience, expertise and strengths?
- Has an Audit Committee been established?
- Have other Board committees been established?

### Director liability

- Do you have the benefit of an indemnity:
  - under the constitution of the company?
  - expressly by your appointor?
  - that is compliant with the Corporations Act requirements for indemnities?
- Do you have a contractual right of access to company records?
- Are you covered by directors' and officers' liability insurance? If so, who pays the premium? What are the exclusions from the policy? Is the policy a 'claims made' or 'claims proven' policy? Can you settle on counsel's advice? Are you covered for legal fees?

### Remuneration

- Will the Remuneration Tribunal need to be consulted?
- Has the Remuneration Tribunal already made a determination in relation to your office?
- What form does your remuneration take?
- How is your remuneration varied? Does the Remuneration Tribunal have to be consulted in relation to variations?
- Does your primary employer permit you to receive directors' fees?

### Insurance

- Is the company adequately insured against appropriate risks?
- What risk management and reporting procedures are in place?

### Corporate compliance

- Is the company a wholly owned Commonwealth company?
- Is there a senior executive responsible for ensuring compliance with the company's statutory obligations?
- Is there formal reporting of compliance for critical compliance obligations and exception reporting for other compliance obligations?
- Is there a process for identifying significant events and operations for the purposes of section 40 of the CAC Act?
- Are all applicable legislation, regulations and other instruments identified, readily available to relevant staff and included in staff training arrangements?
- Are there any General Policy Orders applicable to the entity?
- Does the company have effective arrangements to ensure compliance with all applicable legislation, regulations and other relevant instruments including:
  - Corporations Act compliance?

- Commonwealth Authorities and Companies Act compliance?
- environmental and heritage compliance?
- trade practices compliance?
- taxation (including GST) and stamp duty compliance?
- occupational health and safety compliance?
- anti-discrimination compliance?
- compliance with privacy legislation and Senate disclosure orders?
- compliance with any General Policy Orders?
- compliance with any community service obligations (CSOs)?
- compliance with Legal Services Directions?
- compliance with Codes or Guidelines (such as National Code of Practice for the Construction Industry)
- Have any guidelines in relation to 'significant events' or in relation to 'operations' been issued under section 40 or 41 of the CAC Act?
- What management procedures are in place to avoid legal proceedings and to record/handle legal claims?
- Is the company eligible for any tax exempt status?
- If the company has any tax exempt status, is the company's compliance with any special conditions associated with that tax exempt status constantly monitored?
- Are there any restrictions on borrowing or the giving of security?
- Is there a corporate plan and are there any Finance Minister requirements under section 42 of the CAC Act?
- Are there any subsidiaries?

## Roles of other players

### The Minister

- Is the role of the Minister clearly defined?
- Can the Minister:
  - overrule Board decisions or policy?
  - give directions to the Board and, if so, on what conditions?
  - direct the Company to perform non-commercial activities (eg CSOs)?

### The auditor

- Is the Auditor-General the auditor of the Company?
- Is the role of and/or interaction (where relevant) between the Auditor/Auditor-General appropriate and clear, including:
  - the contract terms?
  - reporting to the Audit Committee?
  - reporting to the Board?

- Is the Audit Committee established in accordance with the Regulations (only applicable to wholly owned Commonwealth companies)?

### Unions

- What unions (if any) have coverage?
- Are labor relations/consultative processes appropriate?
- What arrangements/agreements exist?

### Chief executive officer and senior executives

- Are the roles of the CEO and other senior executives clearly defined?

### Community

- Are community consultative committees involved and, if so, what is their role?
- Are there any community service obligations?

### Statutory duties

- Are there duties set out in any enabling legislation?
- Extent of duties under the Commonwealth Authorities and Companies Act?

## Reporting

- Are interim reports required?
- Are budget estimates required and, if so, are they prepared in accordance with the required form?
- Who requires reports:
  - Ministers (including reports on significant events)?
  - shareholders (annual reports)?
  - Parliament?
  - the Australian Stock Exchange?
  - quarterly reports
  - continuous disclosure
- Have the reporting requirements for subsidiaries been met?

### Guarantee/borrowings

- Does the company have a government guarantee?
- What are the major borrowings of the company and are they secured?

### Non-financial performance

#### Purchasing policies

- Do the Commonwealth Procurement Guidelines apply though the Finance Minister's (CAC Act) Procurement Directions ?
- Is there a Procurement Manual?

- Is there a process for determining whether or not to appoint a process advisor or auditor for a procurement process?
- Is the Minister's approval required for purchases above a threshold?
- What are the levels of delegation?
- Are all applicable Commonwealth policies (including General Policy Orders) addressed?
- Do the Fair Work Principles apply?
- Are there Australian Industry Participation Plan requirements?
- Are the applicable Commonwealth competitive neutrality policies observed when dealing with government and private businesses?

#### Pricing policy

- Are there Ministerial pricing directives?
- Does the Australian Competition & Consumer Commission have a role in relation to price surveillance?

#### Financial performance

- Is the budget process adequate?
- What assumptions underpin the budget?

- Is capital expenditure set by the Board?
- Is there a long-term capital expenditure program?
- Is there a requirement for Ministerial approval of capital expenditure?
- Are limits on expenditure defined?
- How does management report on financial matters:
  - regularity?
  - comparison against budget?
  - clarity?
  - accrual basis?
- Are financial indicators appropriate?
- Does the company publish on a timely basis an objective and readable annual report?
- What process applies for the disposal of assets?
- Is special legislation required for transfers of property?
- What is the process for approval of the acquisition of major assets or other businesses?
- Are there material contingent liabilities?
- Are there adequate reserves?
- Are all major assets adequately accounted for?
- What valuation principles apply and are valuations current?
- What dividends/shareholder levies must be paid? Who decides the level? How are they determined?

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