Personal liability of directors: Regulatory overkill?

1 Introduction

This article reviews the literature that considers the arguments for and against holding directors personally liable for criminal wrongs committed by the companies they represent. The literature refers to the liability of representatives of corporations other than directors; however, as this research is limited to directors, these views are, where necessary, adapted to limit the discussion to directors only. Section 2 discusses what is meant by deemed liability and the issues that may arise as a consequence. Section 3 considers various official reviews on this topic. Section 4 is a general literature review. Section 5 sets out the conclusions of the author.

The author concludes that it is only where there has been personal involvement in a wrong or there are no corporate processes in place to deter and detect wrongdoing that resort could be had to imposing some form of liability on directors. This arises either because the director was an active participant in the offending or there was a breach of a director’s statutory duties. In neither case is there a need for deemed liability.¹

The article first considers what is meant by and what issues arise if a director is held criminally liable simply by virtue of the office held.

2 What is deemed liability? What issues does it raise?

An Australian Law Reform Commission (ALRC) review entitled *Principled Regulation: Federal Civil and Administrative Penalties in Australia*² noted that there were three ways in which liability could be imposed on directors; concurrent (direct) where both the company and director are separately liable as principals; accessorial where the individual

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¹ The situation where either a civil or other monetary penalty may be imposed on a director is beyond the scope of this research.
² *Principled Regulation: Federal Civil & Administrative Penalties in Australia* (ALRC 95, 2002) <http://www.austlii.edu.au/au/other/alrc/publications/reports/95/> . This is referred to as the ALRC report.
is liable as accessory and the corporation as principal; and managerial (deemed)\(^3\) where liability is imposed because of that entities role in the company. \(^4\) This is also sometimes referred to as a derivative liability.

There can be no issue where both the corporation and directors are liable as principal or where there is accessorial liability on the part of directors. In each of these situations liability is directed to those committing the wrong. This is not the case where liability is imposed simply by virtue of the office held. It is this latter situation that the article considers.

Imposing deemed liability conflicts with the view of the House of Lords in *Salomon v Salomon & Co, Ltd; Salomon & Co, Ltd v Salomon* \(^5\) that a company and its members, including its directors, are each separate entities in law. \(^6\) It amounts to a statutory piercing of the corporate veil. \(^7\) Where the corporate veil is pierced the court no longer distinguishes between the corporation and its shareholders or directors. \(^8\) At common law liability is only ascribed to directors in one of two situations. First where there is some positive wrongdoing on the part of the director or second if there is a breach of some statutory obligation imposed on directors. \(^9\)

\(^3\) The report noted at paragraph 28 that there has been an increasing trend towards provisions that deem directors and other senior corporate officers personally liable for a contravention.

\(^4\) ALRC report at paragraph 8.13


\(^6\) Problems and issues arising from the relationship between the company, its directors and shareholders are beyond the scope of this research.

\(^7\) Consideration when a court will pierce the corporate veil in outside the scope of this research. For a paper considering the Australian, Hong Kong and Singaporean principles behind this doctrine see Angelo Capuano, The realist’s guide to piercing the corporate veil: Lessons from Hong Kong and Singapore; (2009) 23 Australian Journal of Corporate Law 56.

\(^8\) See for example *FC of T v Whitford's Beach Pty Ltd* 82 ATC 4031 at p 4039, per Mason J Another tax case, albeit not in Australia, where the veil was pierced was *Littlewoods Mail Order Stores Ltd v McGregor* [1969] 3 All ER 855.

Deemed liability is analogous to strict liability where the Crown does not have to prove the mental element of an offence. This latter type of liability raises the problem that:

The application of strict liability does not allow differentiation between persons that intentionally flout the law and those that make their best efforts to comply. This can lead to resentment on the part of a person who is found guilty of a criminal offence without any element of moral culpability.

The above criticism applies to deemed liability. Support for this view can be found for example in submissions made by Fisse to a Senate Committee on Legal and Constitutional Affairs on Company Directors’ Duties where he is recorded as stating (at paragraph 12.29) that to extend strict liability for company acts inter alia to directors violated the traditional precept that criminal liability required blameworthiness. The Senate Committee recommended at paragraph 12.31 that directors only be held liable where there that director intentionally or recklessly assists in or encourages an act which constitutes an offence by the company. This is an approach which accords with the rule of law and gives proper weight to the presumption of innocence.

There is now only one example left (assuming the Personal Liability for Corporate Fault Reform Bill 2012 bill is enacted in its current form) where deemed liability will still be imposed in a tax context. This is section 8Y Taxation Administration Act 1953 (TAA). Section 8Y (1) provides:

Where a corporation does or omits to do an act or thing the doing or omission of which constitutes a taxation offence, a person (by whatever name called and

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10 The Criminal Code Act 1995 provides for four types of fault: intention, knowledge, recklessness and negligence. The Act also provides that strict liability is an alternative to fault. Some examples of the application of strict liability in the Corporations Act 2001 are sections 448C, 448D and 471A.


13 Considered in section three below.
whether or not the person is an officer of the corporation) who is concerned in, or takes part in, the management of the corporation shall be deemed to have committed the taxation offence and is punishable accordingly.

Section 8Y (2) affords a defence to the offender if he can show that he did not aid, abet, counsel or procure the act or omission of the corporation concerned; and (my emphasis) was not, whether directly or indirectly, knowingly concerned in or a party in the offending. The effect of this subsection is to shift the onus from the regulator to prove the offending to the director to prove a negative. This latter onus can often be a difficult one to discharge.

With aiding, abetting, counseling and procuring the intention of the secondary participant is a necessary element of the offence even if mens rea is not required for the primary offence. There must be knowledge of all the essential facts constituting the offence. Knowledge can be established if the defendant has deliberately shut his eyes to a relevant fact or has deliberately abstained from obtaining knowledge by making an inquiry for fear that he may learn the truth. A person who aids and abets is present at the commission of the offence and took some part whilst one who counsels or procures is not present at the commission of the offence. One can be convicted of aiding, abetting, counseling or procuring even though the offence only refers to the principal offender. It is a prerequisite to liability that the offence actually takes place.\textsuperscript{14} The director must prove none of these elements are present.

As to the second leg of section 8Y (2) a director must prove inter alia that he did not have actual or constructive knowledge of the offence. In deciding this issue a court is ‘involved in the task of examining the applicant's actions and behaviour and in gauging the genuineness and weight of his assertions and claims.’\textsuperscript{15} Again if a director deliberately abstains from acquiring knowledge because he suspected the existence of a fact which would have been ascertained on inquiry, or that the defendant has acted recklessly in the sense that he did not care whether the facts existed or not knowledge

\textsuperscript{14} Giorgianni v R [1985] HCA 29.

\textsuperscript{15} Per Macrossan J in Buist v. Federal Commissioner of Taxation; Ex parte Buist 88ATC 4376, 4381.
will be shown to exist.\textsuperscript{16} Derrington J (who concurred in the judgments of both Kelly SPJ and Macrossan J in \textit{Buist}) said at 4381):

Knowledge of the omission is not necessary to the applicant's being a party to it. If the circumstances require positive action on his part, his failure to perform that duty is an alternative to knowledge as an element to his being party to the omission.

Even if a director is successful the result, in context, may be unjust. This person would have had to incur significant legal and possibly other expenses to prove that he played no part in the offending. This reinforces the view that imposing liability by virtue of the office held impinges to a large degree of basic rules of criminal law and natural justice. This conclusion, it is suggested, is almost irresistible if all the other criticisms of deemed liability referred to in this article are taken into account.

There is a possibility of another defence being available to a director. A majority of the full bench of the New South Wales Court of Appeal found that a breach of Divisions 8 and 9 \textit{Income Tax Assessment Act} 1936 (now Division 269 of Schedule One of the \textit{Taxation Administration Act} 1953) could possibly be defeated by reliance on section 1318 Corporations Act.\textsuperscript{17} Santow JA (Basten JA delivered a separate concurring judgment) said (at paragraph 108-110)\textsuperscript{18}:

\begin{quote}
\textbf{Power to grant relief}

\begin{enumerate}
\item If, in any civil proceeding against a person to whom this section applies for negligence, default, breach of trust or breach of duty in a capacity as such a person, it appears to the court before which the proceedings are taken that the person is or may be liable in respect of the negligence, default or breach but that the person has acted honestly and that, having regard to all the circumstances of the case, including those connected with the person's appointment, the person ought fairly to be excused for the negligence, default or breach, the court may relieve the person either wholly or partly from liability on such terms as the court thinks fit.
\end{enumerate}
\end{quote}


\textsuperscript{17} The operative part of section 1318 reads as follows:

\begin{quote}
\textbf{Power to grant relief}

\begin{enumerate}
\item If, in any civil proceeding against a person to whom this section applies for negligence, default, breach of trust or breach of duty in a capacity as such a person, it appears to the court before which the proceedings are taken that the person is or may be liable in respect of the negligence, default or breach but that the person has acted honestly and that, having regard to all the circumstances of the case, including those connected with the person's appointment, the person ought fairly to be excused for the negligence, default or breach, the court may relieve the person either wholly or partly from liability on such terms as the court thinks fit.
\end{enumerate}
\end{quote}

\textsuperscript{18} \textit{DCT v Dick} [2007] NSWCA 190.
A breach of the tax obligation is capable of giving rise to a parallel breach of the core duty of care and diligence if directors expose their company carelessly to liquidation or administration by reason of their permitting neglect of the company’s PAYG obligations... What this illustrates is that there is a danger of error in identifying duties centrally concerned with corporations, based on the narrow view of whether or not they are imposed by the corporations statute itself. The expansive constitutional interpretation of the Commonwealth’s corporations power to support the validity of legislation directed at constitutional corporations favours a wider view than this… Accordingly to base the test for application of s1318 on whether the statutory obligation is in the Corporations Act itself is at odds with that contemporary reality.¹⁹

As section 8Y operates in conjunction with sections 19B and 21B Crimes Act 1914 (Crimes Act) a brief discussion of these two provisions is apposite. Section 19B²⁰ allows a court to discharge a person charged with a federal offence²¹ without proceeding to conviction or to dismiss the charge under certain circumstances even though the offence is proved. These orders can be made conditional on the accused giving inter alia reparation or restitution or paying compensation in respect of the offence. Thus where an offence is proved but in the exercise of its discretion under section 19B a court could discharge an accused but make the discharge conditional on the outstanding tax of the company being paid if non payment were part of the offence. This section complements section 21B.

Section 21B provides that if a person is convicted of a federal offence or an order is made under section 19B that person can be ordered to make reparation to the Commonwealth

¹⁹ Whether such a defence exists in cases of deemed liability is beyond the scope of this research.

²⁰ See for example Commissioner of Taxation v Baffsky [2001] NSWCCA 332 when an order under section 19B was made in relation to charges of failing to submit income tax returns in time.

²¹ A federal offence is defined in section 16 CA as an offence against the law of the Commonwealth.
or to a public authority under the Commonwealth,\textsuperscript{22} by way of money payment or otherwise, in respect of any loss suffered, or any expense incurred, by the Commonwealth or public authority by reason of the offence.\textsuperscript{23} If a reparation order is made it has the effect of a civil judgment in favour of the Commonwealth, or that public authority and is enforceable in all respects as a final judgment of the court in which it is filed. This section enables a court to order a director to pay to the Commonwealth any tax shortfall occasioned by the offence.

In \textit{Vlahov v FCT}\textsuperscript{24} the Full Court of the Supreme Court of Western Australia explained the operation of section 21B CA as follows:

Section 21B of the \textit{Crimes Act} operates where a person is convicted of an offence against the law of the Commonwealth, whether or not any penalty is imposed upon the person so convicted. Once an officer of a company is convicted by virtue of the provisions of s 8Y(1) of the \textit{Taxation Administration Act}, he fulfils the condition prescribed in s 21B of the \textit{Crimes Act} and the court may order him to make \textit{reparation} in respect of any loss or expense referred to in that section.

A reparation order is discretionary and forms part of the sentencing process. The judicial officer must exercise the discretion as part of the overall disposition of the case and bearing in mind all of the relevant circumstances.\textsuperscript{25} There has to be a nexus between the offence and the loss in respect of which reparation is claimed. This loss may not be difficult to prove. As was stated by Deane, Dawson and Gaudron JJ in \textit{Hookham v R}\textsuperscript{26}(at paragraph 7):

\begin{quote}
22 A public authority under the Commonwealth is defined in section 3 CA as any authority or body constituted by or under a law of the Commonwealth or of a Territory. This would include the ATO.

23 The court can also make an award in favour of any person, by way of money payment or otherwise, in respect of any loss suffered by the person as a direct result of the offence. This article does not deal with the case where shareholders or creditors of the company could look to directors for reparation due to loss suffered as a result of the offence.

24 \textit{Vlahov v FCT} 93 ATC 4501.

25 Per Owen J in delivering the judgment of the Full Court of the Supreme Court of Western Australia in \textit{Gould v FCT} 98 ATC 4946 at 4951.

26 \textit{Hookham v R} 94 ATC 4789.
\end{quote}
But a loss need not involve the transfer from the Commonwealth to someone else of a proprietary interest. The Commonwealth suffered a loss by being deprived of money which it would have been paid had it not been for the commission of the offences in question. There is no reason why that should not be regarded as being a reparable loss.

A loss would include any interest which accrues on a tax obligation and any penalty imposed by the Commissioner. Penalties (and interest) are entitlements of the Commonwealth granted to it by statute, as is the case with the original tax obligation. The quantum of a claim for reparation can be significant. Amendments to assessments, as a result of an audit, can take place many years after the income year for which a return is filed. With compound interest and penalties the total claim can sometimes be more than double the actual tax. One should, however, bear in mind the comments of Priestly JA delivering the judgment of the Court of Criminal Appeal New South Wales in R v Hookham when considering quantum of a section 21B claim that:

> Because the Commissioner has possibilities of recovery from other sources (for example, other company officers and in some cases the company or its liquidator) the amount of the loss suffered will depend on the facts of each case.

It is not a defence to proceeding under section 21B that the claim denies the defendant the right to defend a civil action.

The use of section 21B in conjunction with section 8Y TAA is an important and powerful tool in the hands of the Commissioner.

The article now returns to section 8Y.

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27 In Commissioner of Taxation v Dixon (Trustee) [2007] FCA 1079 Justice Collier held that penalties were imposed by operation of law and not the Commissioner. This statement was found to be obiter (but not dissented from) by the Federal Court of Appeal in Archibald Dixon as Trustee for the Dixon Holdsworth Superannuation Fund v Commissioner of Taxation [2008] FCAFC 54.


29 Gould v FCT 98 ATC 4946 at 4952.
In *Hookham v R*\(^{30}\) the High Court (per Deane, Dawson and Gaudron JJ) stated section 8Y operates in the following way (at paragraphs 5 and 6):

That function is to reverse the onus of proof which would otherwise rest upon the prosecution of proving that a defendant who is concerned in, or takes part in, the management of a corporation is a participant in a taxation offence by reason that he or she aided, abetted, counselled, procured or was knowingly concerned in, or party to, its commission...Section 8Y, in providing that the person is "punishable accordingly", is not providing for punishment for an offence which was really committed by the corporation and is only "deemed" to have been committed by that person; it is providing for punishment for an offence to which that person is deemed to be a party because of his or her complicity in it.

Professor Baxt\(^{31}\) is of the opinion (at page 7) legislation should not require a director to prove his innocence; rather the law should follow the principle that you are innocent until proven guilty.

As will be shown below provisions such as this can lead to convictions, where, if the criminal standard were applied with the onus on the prosecution, a conviction would not follow.

### 3. Government reviews.\(^ {32}\)

\(^{30}\) *Hookham v R* [1994] HCA 52; (1994) 181 CLR 450.


\(^{32}\) There are a number of governmental reports not reviewed, as they were superseded by those considered in this research. There reports are:

- Senate Standing Committee on Legal and Constitutional Affairs, *Company Directors’ Duties, Report on the Social and Fiduciary Obligations of Company Directors* (Cooney, Chair), Canberra, AGPS, 1989, 188, 16–17;
- Joint Select Committee on Corporations Legislation, *Report* (Edwards, Chair), Canberra, AGPS, 1989; and
The first report considered is that issued by the ALRC\textsuperscript{33} and mentioned in section two above.

The ALRC in its report referred to a number of factors that it considered problematic in cases of deemed liability. These factors were: is it sufficient for liability simply to hold office or is some consideration or weight to be given to seniority; the reversal of the onus of proof raised issues of fairness; should fault play a part when imposing liability; and what differential, if any, should there be between penalties imposed on corporations and those on individuals.\textsuperscript{34} Invariably legislation imposing liability on directors makes no reference to seniority. The issues of the reverse onus and fault are discussed in detail below. The final point on different penalties for corporations and individuals is beyond the scope of this article.

The ALRC referred to a number of situations where, in its opinion, deemed liability was considered to be appropriate. These include preventing directors from hiding behind the corporation for their own acts;\textsuperscript{35} or fines against corporations are often inadequate;\textsuperscript{36} or penalties on corporations are often assumed by innocent parties such as shareholders;\textsuperscript{37} or penalties on individuals may be a more credible and effective deterrent.\textsuperscript{38}

The reasons for accepting deemed liability as suggested by the ALRC is subject to a number of criticisms.

First it offends against principles of criminal law and the rule of law that a person is innocent until proven guilty. Lacey refers to the requirement of proof of individual

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House of Representatives Standing Committee on Legal and Constitutional Affairs, \textit{Fair Shares for All – Insider Trading in Australia} (Griffiths, Chair), Canberra, AGPS, 1989, 41.

These reports were cited by R Tomasic, ‘Sanctioning Corporate Crime and Misconduct: Beyond Draconian and Decriminalization Solutions’ (1992) 2(1) \textit{Australian Journal of Corporate Law} 82.
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\textsuperscript{33} See n 2 above.
\textsuperscript{34} See n 2 above ALRC report at paragraph 8.5.
\textsuperscript{35} ALRC report at paragraph 8.6
\textsuperscript{36} ALRC report at paragraph 8.8.
\textsuperscript{37} ALRC report at paragraph 8.9.
\textsuperscript{38} ALRC report at paragraph 8.10.
responsibility or fault as the jewel in the crown of criminal law doctrine. To impose criminal liability evidence should be led to show the offending and necessary state of mind of the accused rather than assuming guilt and placing an onus on the accused to show there was no involvement in the commission of the offence. The presumption of innocence is almost universally recognized and deemed liability is in direct conflict with this doctrine. As Sayre stated:

Acts alone are frequently colorless; it is the state of mind which makes all the difference between innocence and criminality... To inflict substantial punishment upon one who is morally entirely innocent, who caused injury through reasonable mistake or pure accident, would so outrage the feelings of the community as to nullify its own enforcement.

Second even if liability is imposed in this way it should only occur when the accused person has a duty or responsibility for that area of activity and is able to influence outcomes and fails to do so. In some larger corporations even this may not be sufficient. If a director was an active participant in the offending deemed liability is not necessary. The usual means for proving liability should be adopted. As will be demonstrated below reversing the onus can lead to a miscarriage of justice.

Third if the legislature believes a fine against a corporation is inadequate it has the power to amend the legislation to provide for larger fines or other penalties against the corporation. Even if fines against corporations are assumed (usually indirectly) by innocent third parties this cannot be a sustainable basis to impose liability on a director. This seems to substitute one innocent party for a potentially another innocent party. Penalties that have a direct impact on a company such as the equity fine suggested by

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40 Sayre, Francis Bowes, Public Welfare Offenses; 33 Colum. L. Rev. 55 (1933) at 56.
41 Honore’s views on outcome responsibility are beyond the scope of this research. Honore was of the view that people are responsible for their actions including any unintended consequences of such action: Honore T, Responsibility and Fault; Oxford, Hart publishing, 1999.
Coffee can be imposed. Finally to suggest that penalties on individuals are a more credible deterrent ignores research by people such as Kraakman that dual penalties are the most effective form of penalty. If taken to its logical conclusion, the last proposition suggests that corporations should never be indicted criminally or have civil or other monetary penalties imposed as for all practical purposes it can only operate through individuals.

Some suggest executives (and employees) invariably act in their own self-interest, and their pursuit of individual goals is the primary reason for corporate crime. Even accepting this proposition it is not a basis for deemed liability of directors. In these circumstances the individual is an active participant in the wrongdoing.

It is accepted there may possibly be a justification in circumstances where the corporations is a small family controlled entity but even here it is submitted that the arguments against deemed liability suggest this should not occur. Other more direct remedies are always available as invariably the director is a direct participant in the wrongdoing.

The ALRC considered the problem raised by reversing the onus of proof and suggested (at paragraph 8.57) this could be justified because either some contraventions may be considered very serious; or there may be aspects of a case that would be too difficult for the regulator or prosecutor to prove; for example, because confidentiality obligations or privileges prevent them gaining access to critical documents or information; or the contravention may be one that only affects a particular segment of the community and it may be that that segment is considered to be capable of safeguarding its own interests; or deeming an individual to be responsible for the conduct of the corporation (unless that person can prove a defence) is one method of ensuring that ‘someone pays’ for the misconduct.

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The ALRC qualified the above stating (at paragraph 8.61) that legislators must always balance efficacy arguments for reversing the onus of proof against fairness issues such as the harshness of the penalty and the impact on the segment of the regulated community that is likely to be subject to the deeming provision.

The arguments for reversing the onus of proof do not withstand scrutiny.

First the fact a contravention may only affect a particular segment of the community and that segment is considered to be capable of safeguarding its own interests is not a proper basis for deemed liability. The fact that a director of a company is capable of looking after his/her own interest is not to the point. The true issues are twofold. First if the director is unable to discharge a reverse onus but in criminal proceedings would not have been found guilty as there would have been some doubt in the court’s mind is there a miscarriage of justice? Second should Parliament do away with a basic principle of criminal law that a person is innocent until proven guilty? There is a possibility of a third issue: Should the fact that a person has monetary and other resources available to him be a basis for imposing a reverse onus? The answer to this last question should be an emphatic no.

The next aspect in support of deemed liability raised by the ALRC is that someone should pay for the wrong and/or the contravention is regarded as being serious. This is analogous to saying one or a number of persons committed an offence in conjunction with a company, I do not know who they are, or even if I do know I cannot obtain a conviction against them. As you are associated with the company that committed the offence you will be convicted of the crime unless you can show you played no direct or indirect part in it. The problems with this argument are illustrated by extracts from two judgments mentioned below. The first is that of Justice Sachs sitting in the South African Constitutional Court in *State v Coetzee*\(^{43}\) where he said:

> There is a paradox at the heart of all criminal procedure, in that the more serious

\(^{43}\) *State v Coetzee*\(^{43}\)[1997] 2 LRC 593 at 677-678.
the crime and the greater the public interest in securing convictions of the guilty, the more important do constitutional protections of the accused become. The starting point of any balancing inquiry where constitutional rights are concerned must be that the public interest in ensuring that innocent people are not convicted and subjected to ignominy and heavy sentences, massively outweighs the public interest in ensuring that a particular criminal is brought to book ...

Reference to the prevalence and severity of a certain crime therefore does not add anything new or special to the balancing exercise. The perniciousness of the offence is one of the givens, against which the presumption of innocence is pitted from the beginning, not a new element to be put into the scales as part of a justificatory balancing exercise.

_Coetzee_ considered the constitutional validity in South Africa of legislation imposing personal liability on directors. 44 A major factor against personal liability in the context of the _Coetzee_ case was the reluctance to impose criminal sanctions in the absence of blameworthiness.

The second is the judgment of Dickson CJC sitting in the Canadian Supreme Court in _R v Whyte_ where in delivering the judgment of the court he said (at paragraphs 30, 31): 45

The real concern is not whether the accused must disprove an element or prove an excuse, but that an accused may be convicted while a reasonable doubt exists. When that possibility exists, there is a breach of the presumption of innocence… It is the final effect of a provision on the verdict that is decisive. If an accused is required to prove some fact on the balance of probabilities to avoid conviction, the provision violates the presumption of innocence because it permits a conviction in spite of a reasonable doubt in the mind of the trier of fact as to the

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44 See Van Der Linde K, The Personal Liability of Directors for Corporate Fault – An Exploration, (2008) 20 SA Merc LJ 439–461 at 454. Van Der Linde commenting on this case noted that the court identified the policy considerations favouring the imposition of personal liability which included the fact that individual were more likely to be deterred by imprisonment and that wrongful conduct by individuals albeit in the name of a company should not be insulated from liability.

guilt of the accused…Section 237(1)(a) requires the accused to prove lack of intent on a balance of probabilities. If an accused does not meet this requirement, the trier of fact is required by law to accept that the accused had care or control and to convict. But of course it does not follow that the trier of fact is convinced beyond a reasonable doubt that the accused had care or control of the vehicle. Indeed, in this case, as in Appleby, the trier of fact stated that he convicted the accused despite the existence of a reasonable doubt as to care or control, an element of the offence.46

The dicta in both Coetzee and Whyte are compelling arguments against a reverse onus provision. Hookham suggests section 8Y merely seeks to convict one who participated in the crime but submissions such as those raised in Coetzee and particularly Whyte do not appear to have been raised before the High Court.

Notwithstanding the possible justifications put up by the ALRC for a reverse onus provision it concludes that penalties should only be imposed on individuals who have control or influence over the body corporate and particularly in relation to the wrong committed.47 This suggests some direct involvement in the act. At the very least the director should have been put on enquiry and then failed to do anything.

None of the grounds referred to above are, on a proper analysis, a basis for deemed liability.

The second government review considered is a report from CAMAC entitled Personal liability for corporate fault (September 2006),48 identifies (at page 1) two principal areas

46 It is accepted that the South African courts are bound by the terms of a written Constitution whereas in Canada the courts are bound by a Bill of Rights. Notwithstanding this the comments in both Coetzee and Whyte are apposite to Australia.
47 ALRC report at paragraph 8.67 and 8.89 to 8.92
of concern with deemed liability. First the tendency to impose personal criminal sanctions on individuals for corporate wrongs by virtue of the office held. Second the undue complexity about requirements for compliance. The report notes the purpose of deemed liability was to ensure that effective risk management arrangements were put into place. It goes on to identify two areas in which it considered deemed liability to be contentious. These included (at pages 8–9): the discrimination against directors compared with other entities subject to civil or criminal penalties; and the encouragement of corporate compliance does not justify an abrogation of rights on the part of persons targeted.

The report continued (at pages 29–33) that with deemed liability: the imposition of personal liability without proof of personal fault is based on an unjust assumption that directors are at fault merely because a corporate breach has occurred; and there is often no reasonable causal nexus between the offence and the person who is subject to personal liability. The reasons for imposing personal liability on directors were either prosecutorial expediency (reversing the onus of proof) or political expediency, whereby governments are seen to be taking a tough stand against areas of conduct where there are strong community feelings. These do not constitute a proper foundation for deemed liability. The preferred approach of CAMAC (at pages 9 and 33) is that ‘individuals should not be penalised for misconduct by a company except where it can be shown that they have personally assisted or been privy to that misconduct, that is, where they were accessories’.

The report continued (at page 34–6) that personal liability should be limited to responsibility for ensuring that a company complies with a specific operational or administrative requirements, such as the filing of a return by a particular date, and that

These differences in legislative approach, even in the same areas of regulation, and the consequential lack of harmony result in complexity and lack of clarity for individuals in considering their responsibilities. Directors and other individuals may be subject to differing standards of responsibility with divergent defences available to them under various statutes that affect the operations of their company in different jurisdictions. This very lack of harmony can impair ready communication of statutory requirements and effective compliance efforts.

With tax, the complexity is even greater.
liability should not extend to areas where compliance requires the exercise of significant judgment or discretion. This view may reflect a misunderstanding of the role director’s play. Their role is to determine policy and strategic goals, not to deal with the day-to-day administration of a company, other than possibly in small family-owned companies. Even in the smaller companies the tasks of submitting returns and the like are invariably delegated to subordinates. A director’s duties, even in a small company, generally do not extend to overseeing day to day administrative tasks. In all companies there should be systems and processes in place, commensurate with its size and complexity, to deter and where possible discover any wrongful acts by employees. This is considered in more detail below.

Corporations are vehicles for creating wealth; obligations imposed on directors should not seriously compromise their goal of maximising shareholder wealth. Too much regulation could be counterproductive to the wealth creating function of corporations but (at page 11): ‘decisions must be taken in the interests of the company and be challengeable if they are not bona fides and well informed’. The report recommended the statutory formulation of a business judgment rule that ‘should not insulate directors from liability for negligent, ill-informed or fraudulent decisions. Rather, the rule should encourage a company to adopt risk-management structures and thereby significantly reduce director uncertainty.’

CAMAC notes (at page 53) that there was a growing trend for legislatures to impose strict personal liability upon directors of corporations for breaches of statutory obligations by the corporation. The rationale for this, it was said, was to ensure that directors (at page 53) put in place ‘effective risk-management arrangements to ensure the corporation complies with its obligations’.

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50 CAMAC report, 7–8.
It is the managerial risk management function that seems to be overlooked when the legislature deems liability to occur by virtue of an office held. The principle should be the following: has the company a well-developed corporate governance framework to detect, prevent and deter wrongdoing, which is regularly reviewed and does it take steps to ensure it is operating effectively? If this is the case, there would be appear to be no basis for deemed liability simply by virtue of the office held. If the director has been an active participant in the wrongdoing, there is no need for deemed liability. If there are no processes that are regularly monitored and updated to prevent the wrong occurring there has not been the necessary implementation of corporate governance processes coupled with a lack of risk management. This is breach of a director’s duty of care and good faith to the company and gives rise to remedies under the Corporations Act. There is no need for deemed liability.

Indeed CAMAC stressed (at pages 43 and 44) that directors should not be assumed to be aware of every aspect of the day-to-day functioning of their corporations; and any defences provided for needed to be realistic. If not, there would be little incentive to implement corporate compliance systems or practices. It was suggested that the evidential burden on the regulator should not be so onerous to create an undue and inappropriate disincentive for regulators to prosecute apparent breaches. This view ignores the basic principle that accused should have the right to the presumption of innocence and that persons who have not participated in a wrong should not be held liable even if they may avoid liability by discharging a positive onus in showing they took no part in the wrongdoing.

CAMAC, in a later report entitled Guidance for Directors, states that regulators should realise that risk management is not about the limitation of risk but that risk should be understood and managed. Good practice requires boards to be involved in establishing

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52 When reference is made in this article to active wrongdoing, it includes cases in which the director or the board is put on enquiry but does nothing.

53 Sections 180 to 183 Corporations Act prescribe civil penalties for a breach of their provisions and section 184 provides for criminal sanctions if the person acted dishonestly.
This latter report concludes that directors cannot and should not be held liable for all wrongs committed by a company. For liability to exist, there must be active participation in the offence or a failure to impose proper governance processes with a view to properly managing (not eliminating) any risk of wrongdoing by employees. Welsh et al., writing in response to this report, were also of the opinion that liability should depend on fault. This, it is submitted, is the correct approach to directorial liability.

As was said by French J (as he then was) sitting in the Federal Court in *ASIC, Re Chemeq Ltd (ACN 009 135 264) v Chemeq Ltd (ACN 009 135 264).* In considering the appropriate penalty for the contravention by a corporation... it is relevant to consider whether the corporation has in place policies and procedures designed to achieve compliance with such requirements.

The Court will consider the form and content of the policies and procedures and also the measures adopted by the corporation to ensure that they are understood and applied. A well drafted set of policies and procedures will mean little if there is no follow up in terms of training of company officers (including directors) and, where appropriate, refresher training ... Compliance policies and procedures will not be effective unless there is, within the corporation, a degree of awareness and sensitivity to the need to consider regulatory obligations as a routine incident of corporate decision-making. This kind of general sensitivity to the issues underpins what is sometimes called a ‘culture of compliance’. It does not require a risk averse mentality in

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56 *ASIC, Re Chemeq Ltd (ACN 009 135 264) v Chemeq Ltd (ACN 009 135 264)* (2006) 24 ACLC 806 [84]–[85]. See also the judgment of J Heerey in *Australian Competition and Consumer Commission v Visy Industries Holdings Pty Ltd (No 3)* [2007] FCA 1617 [319] where the learned judge said: The Visy Trade Practices Compliance Manual might have been written in Sanskrit for all the notice anybody took of it.
the conduct of the company’s business, but rather a kind of inbuilt mental check list as a background to decision-making.

Although Justice French refers to matters to be taken into account in sentencing, it is suggested the absence of the same factors may be a basis for liability but not because the director has participated in the offence but because there has been a breach of the director’s duty of care and good faith towards the company.

CAMAC felt (at pages 34–6)\(^\text{57}\) that it was only in exceptional circumstances that the public interest, in achieving compliance by a company, may be seen as requiring officers to assume a more positive role within their sphere of influence and to risk personal liability where they have acted with reckless or negligent disregard of the company’s relevant conduct. This failure, it is submitted, by directors is not a basis for deemed liability but rather lays the foundation for liability for a breach by a director of their statutory obligations.

The next report briefly considered is one by Treasury on *Sanctions for Breaches in Corporate law*.

The Treasury report noted that penalties for breaches of directors’ duties must ensure that they strike an appropriate balance between promoting good behaviour and ensuring business is willing to take sensible commercial risks.\(^\text{58}\) The review (at pages 29–30) also refers to the need for a business judgment rule\(^\text{59}\) to give directors a safe harbour where decisions are taken in relation to matters relevant to the operations of the business. It noted (at page 10) that the Taskforce on Reducing Regulatory Burden on Business\(^\text{60}\) cautioned that:


\(^{59}\) Corporations Act, subsection 180(3).

\(^{60}\) *Rethinking Regulation: Report of the Taskforce on Reducing Regulatory Burdens on Business* (January 2006).
A risk-averse approach by business may limit their willingness to adopt innovative approaches in developing products and meeting new challenges. It would also be reflected in an overly cautious approach to compliance such as in product disclosure statements. This would undermine the overall efficiency and dynamism of the economy.\textsuperscript{61}

The remainder of this report refers to civil penalties and as such is not germane to this article.

The final report discussed is one issued by the Ministerial Council for Corporations for Reform of Directors’ Liability Provisions (MINCO).

On 6 November 2009, the then Minister for Financial Services, Superannuation and Corporate Law, Chris Bowen, referred to an agreement reached by by the Ministerial Council for Corporations for Reform of Directors’ Liability Provisions (MINCO). MINCO had agreed on a set of principles by which all jurisdictions would audit their legislative provisions that deal with personal liability on company directors.\textsuperscript{62} Broadly these principles\textsuperscript{63} provide that the imposition of criminal liability on a director for wrongs

\begin{flushleft}
\textsuperscript{61}Rethinking Regulation: Report of the Taskforce on Reducing Regulatory Burdens on Business (January 2006) 90. \textsuperscript{62}Press release on 6 November 2009 by Chris Bowen, Minister for Financial Services, Superannuation and Corporate Law on Principles agreed to by the Ministerial Council for Corporations for Reform of Directors' Liability Provisions. \textsuperscript{63}The full text of these principles is transcribed below. \\
1. Where a corporation contravenes a statutory requirement, the corporation should be held liable in the first instance.
2. Directors should not be liable for corporate fault as a matter of course or by blanket imposition of liability across an entire Act.
3. A ‘designated officer’ approach to liability is not suitable for general application.
4. The imposition of personal criminal liability on a director for the misconduct of a corporation should be confined to situations where:
   a. there are compelling public policy reasons for doing so (for example, in terms of the potential for significant public harm that might be caused by the particular corporate offending);
   b. liability of the corporation is not likely on its own to sufficiently promote compliance; and
\end{flushleft}
committed by a corporation should occur only in very limited circumstances. These are public policy; or punishing the corporation alone will not promote compliance; or it is reasonable having regard to things such as the director having capacity to influence the conduct of the corporation in the offending or that there are steps that a reasonable director might take to ensure the corporation’s compliance with the obligation.

In a paper presented in the University of New South Wales Thought Leadership Series, Professor Baxt noted that both he and the Australian Institute of Directors were of the opinion that although the MINCO principles were a good start, more needed to be done.64

As a result of the MINCO principles Government acknowledges that deemed liability should only be imposed in the limited circumstances identified by MINCO.

The above principles were reiterated in the Explanatory Memorandum65 (EM) to the Personal Liability for Corporate Fault Reform Bill 2012 which was introduced so as to give effect to the MINCO principles over a range of laws including the tax laws. The EM66 stated the purpose of the legislation was to:

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5. Where principle 4 is satisfied and directors’ liability is appropriate, directors could be liable where they:
   a. have encouraged or assisted in the commission of the offence; or
   b. have been negligent or reckless in relation to the corporation’s offending.
6. In addition, in some instances, it may be appropriate to put directors to proof that they have taken reasonable steps to prevent the corporation’s offending if they are not to be personally liable.

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64 Professor Baxt, ‘Is the Time Right to Reform the Law Governing the Duties of Public Company Directors and Non-executive Directors in Particular?’ (Paper presented at the University of New South Wales Thought Leadership Series).
• remove personal criminal liability for corporate fault where such liability is not justified;
• remove the burden of proof on defendants to establish a defence to a charge;
• replace personal criminal liability for corporate fault with civil liability where a non-criminal penalty is appropriate; and
• where personal criminal liability is justified, to make clear the circumstances where such liability would apply.

The methodology adopted is either to repeal the provision, or impose a civil penalty instead; or to clarify the level of fault required before becoming liable to criminal sanctions. This legislation was introduced in three tranches during 2012. The first two considered legislation which does not impact on the tax function of corporations.

The third tranche of the *Personal Liability for Corporate Fault Reform Bill 2012,* deals with four specific provisions imposing personal liability in relation to tax:

• Section 8Y of the *Taxation Administration Act 1953*;
• Section 444-15 of Schedule 1 to the *Taxation Administration Act 1953*;
• Paragraph 252(1)(j) of the *Income Tax Assessment Act 1936*; and

67 This can be accessed at:


68 Section 444-15 provides as follows:

Liability of directors and officers of a company

(1) Any notice, process or proceeding that may be given to, served on or taken against a company or its public officer under an * indirect tax law* may, if the Commissioner considers it appropriate, be given to, served on, or taken against an entity (the *representative*) who is:

(a) a director, secretary or other officer of the company; or
(b) an attorney or agent of the company.

(2) The representative has the same liability in respect of the notice, process or proceeding as the company or public officer would have had if it had been given to, served on or taken against the company or public officer.

(3) This section does not, by implication, reduce any of the obligations or liabilities of the company or public officer.

69 Section 252 deals with the appointment of a public officer to a company and the liability of that officer. Section 252 (1) (f) provides:
• Subsection 57(7)\textsuperscript{70} of the \textit{Superannuation Guarantee (Administration) Act} 1992.

The last three provisions are being repealed. Section 252(1)(j) was the subject matter of a full Federal Court decision\textsuperscript{71} which held that before the provision could apply notice had to be given to the director to perform the obligation in question before liability could attach to a director. The other two provisions which are being repealed were drafted on similar terms to section 252 (1)(j). The situation may be different here than where, such as with section 8Y, liability is imposed without any notice to do any acts before liability accrues.

Section 8Y \textit{Taxation Administration Act} 1953 is not being repealed. It was in fact enacted after the Crown was unsuccessful in \textit{Reynolds}.\textsuperscript{72}

The reasons given for refusing to repeal section 8Y are that first it provides directors various defences, the effect of which is that directors can show, on the balance of probabilities, that they were not involved in the company’s offending. As such, section

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\textit{The public officer shall be answerable for the doing of all such things as are required to be done by the company under this Act or the regulations, and in case of default shall be liable to the same penalties.}

\textbf{Section 252 (1)(j) reads:}

(j) Notwithstanding anything contained in this section, and without in any way limiting, altering or transferring the liability of the public officer of a company, every notice, process or proceeding which under this Act or the regulations thereunder may be given to, served upon or taken against the company or public officer may, if the Commissioner thinks fit, be given to, served upon or taken against any director, secretary or other officer of the company or any attorney or agent of the company and that director, secretary, officer, attorney or agent shall have the same liability in respect of that notice, process or proceeding as the company or public officer would have had if it had been given to, served upon, or taken against the company or public officer.

\textsuperscript{70} This reads as follows:

(7) Despite subsections (1) to (6) (inclusive) and without affecting any of the public officer's obligations and liabilities, a notice, process or proceeding that under this Act may be given to, served on or brought against the company or public officer may, if the Commissioner thinks fit, be given to, served on or brought against any director, secretary or other officer of the company or any attorney or agent of the company, and the director, secretary, officer, attorney or agent has the same liability in relation to the notice, process or proceeding as the company or public officer would have had if it had been given to, served on or brought against the company or public officer.

\textsuperscript{71} \textit{Reynolds v. Deputy Federal Commissioner of Taxation}. 84 ATC 4689

\textsuperscript{72} See n 71 above.
8Y operates, in substance, as an accessorial liability provision. The problem with this type of reasoning was considered in section two above.

The second reason is that ‘it would not be feasible to shift the burden and require the prosecution to prove a director’s involvement in the company’s offence; especially as such information could be peculiarly within the knowledge of the director’. It is submitted this latter reason has no substance. Any problems the prosecution might face are no different to those faced by a prosecution in any criminal trial. It is cause for concern that directors should be singled out for this special treatment. It seems to be an attempt to rationalise a policy of ensuring someone pays for a wrong, irrespective of the identity of the wrongdoer. If one has proper regard to the role of a director in a company, the reality is that, other than where the director is a participant in the wrong, he or she may not have any knowledge of the conduct giving rise to the charges and may have sought to prevent such wrongs by introducing systems and policies to prevent it. To be charged in these circumstances ignores any suggestions that the rule of law or the presumption of innocence has any place in the regulation of directors or at worst lip service is given to demands for proper corporate governance processes.

The EM continues that it took into account the MINCO principles in reaching this decision (at page 3) including ‘the magnitude of harm that the offending conduct would likely cause, the effectiveness of corporate penalties in preventing this conduct and the availability of evidence to the prosecution and the director’. No explanation is given as to how this evaluation process was carried out. Section two above illustrates just how difficult it could be for a director to discharge the onus imposed by section 8Y TAA. On a proper construction of section 8Y TAA it is suggested that it is not a defence if steps were taken to prevent the conduct but notwithstanding such steps, the act occurred, particularly as the accused has to show no aiding, abetting, counselling or procurement, and that he or she was not knowingly by act or omission, directly or indirectly, concerned in, or party to, the act or omission. Further, the problems set out in Coetzee and Whyte above are clearly problematic for the director in these circumstances. The EM continues, in any event, section 8Y is used sparingly, as the Commissioner only resorts to it in cases
of serious and repeated neglect of company tax obligations. This is of little comfort to
directors. The pyramidal system of regulation followed by the ATO specifically relies on
what is referred to as the benign big gun.\textsuperscript{73} The use of this provision is solely within the
discretion of the Commissioner.

This article now turns to the views of academics on whether deemed liability should be
imposed.

4 The literature

Fisse and John Braithwaite\textsuperscript{74}, writing in 1988, were of the opinion that personal liability
would facilitate accountability on the part of directors. They said such liability should
‘provide a strong incentive for him to monitor the corporation’s activities and implement
preventative programs to avoid future breaches’. The problem with this view is that even
if processes are in place to prevent the wrong this would not be a defence under section
8Y Taxation Administration Act 1953.

A report by Andrew Kitching (at pages 2–4), on 16 October 2008 prepared for the
Library of the Canadian Parliament, considered director liability provisions under the
Canada Business Corporations Act R.S.C 1985 and noted that the traditional motivation
of corporations was to enhance shareholder value. Kitching was of the opinion that if
directors are subject to excessive personal liability they could resign or refuse to act on
boards and potentially make companies less competitive due to increased compliance
costs. As Justice Kirby (as he then was) stated: ‘when it (the company) loses entirely the
spark of adventure and risk-taking entrepreneurship, it has lost its raison d’etre’.\textsuperscript{75}
Notwithstanding this, Kitching is of the view that without personal liability, a moral

\textsuperscript{73} John Braithwaite, ‘Mortgage Origination Fraud Diagnostics of White-collar Crime Prevention’ (2010)
9(3) Criminology & Public Policy 621.

\textsuperscript{74} Fisse and Braithwaite, ‘The Allocation of Responsibility for Corporate Crime: Individualism,

\textsuperscript{75} The Hon. Justice Michael Kirby AC CMG, Australian Corporations Law and Global Forces, 2; J Flinders
hazard exists, as accountability rested on this premise. It is suggested that this premise is flawed, as is demonstrated by that set out above.

Slemrod\textsuperscript{76} notes enforcement strategies directed at a director and at the corporation may have different effects on corporate behaviour and as such, it is important to know whether there is a reason to prefer one over the other. With evasion, Slemrod states penalties imposed on the manager (director) directly are more effective than those imposed on shareholders because the latter are diluted.\textsuperscript{77} This view does not take into account the problems with making directors liable without a direct connection between the director and the offence.

Young (at page 229),\textsuperscript{78} discussing sections 180-184 of the Corporations Act which do not deem liability, is of the view that the imposition of civil penalties on directors is justified for two reasons. First, the company board has a central role in corporate management and directors may be the most appropriate and culpable party against whom to seek damages or enforce penalties. Second, the spectre of liability has an important regulatory impact in setting strong norms for behaviour. Young continued (at page 231) that in his view, the imposition of liability on directors can be a useful deterrent against irresponsible risk taking as well as dishonest and careless behaviour by directors. This view possibly negates the business judgment rule contained in section 180(3) Corporations Act. Provided directors come within the terms of the business judgment rule and have otherwise acted properly, they should be entitled to rely on this as a safe harbour. If a director breaches any of the provisions discussed by Young there is no need for deemed liability as the director is a direct participant in the wrong.


\textsuperscript{77} See also \textit{Review of Sanctions for Breaches of Corporate Law} (The Treasury, 2007) [2.41].

\textsuperscript{78} Neil Young QC, ‘Has Directors’ Liability Gone Too Far or Not Far Enough? A Review of the Standard of Conduct Required of Directors under Sections 180-184 of the Corporations Act’ (2008) 26 \textit{C&SLJ} 216. Young’s article referred only to sections 180–184 Corporations Act but the sentiments expressed by Young presumably mirror those of the legislature when imposing obligations and liability on directors in relation to tax.
Gerding\textsuperscript{79} refers to the responsible officer doctrine in the US, which was based on the judgment in \textit{United States v Dotterweich},\textsuperscript{80} which is a form of strict liability \textit{inter alia} for directors. This doctrine provides for liability where in criminal proceedings:

The Government establishes a \textit{prima facie} case when it introduces evidence sufficient to warrant a finding by the trier of the facts that the defendant had, by reason of his position in the corporation, responsibility and authority either to prevent in the first instance, or promptly to correct, the violation complained of, and that he failed to do so.\textsuperscript{81}

This principle has also been applied in tax cases.\textsuperscript{82} This doctrine may found a basis for liability if it could be shown that irrespective of the conduct of the director, no processes were put into place to prevent the wrong.

According to Gerding, the courts in the US no longer apply a liberal view of the doctrine. They now require an explicit reference to the doctrine in legislation and that a corporations’ organisational documents task a director with more direct oversight of the particular area of a corporation’s operations involved in legal misconduct for it to be applied. This is an implicit recognition that companies do not act in a vacuum. Directors control the policy and direction of companies. Acts by employees are not the act of the directors. Tom Bostock is reported to have said that the imposition of personal liability on directors shows a lack of understanding of the role of directors in relation to the

\textsuperscript{79} Erik Gerding, \textit{Directors’ Personal Liability for Corporate Fault in the United States} (January 2008)\texttt{<http://works.bepress.com/cgi/viewcontent.cgi?article=1005&context=erik_gerding.>}

\textsuperscript{80} \textit{United States v Dotterweich} 320 U.S. 277; 64 S. Ct. 134; 88 L. Ed. 48; 1943 U.S. LEXIS 1100.

\textsuperscript{81} \textit{United States v Park}, 421 US 658 (1975) 673–4, as cited in above n 64.

\textsuperscript{82} See for example \textit{Thomsen v United States} 887 F.2d 12; 1989 U.S. App. LEXIS 15104; 89-2 U.S. Tax Cas. (CCH) P9575; 64 A.F.T.R.2d (RIA) 5752. In this case, the judgment of the court was delivered by Chief Judge Campbell. The learned Judge noted that the doctrine encompassed a number of principles. Included are the following:

\begin{itemize}
  \item Responsibility is a matter of status, duty and authority, not knowledge; and
  \item Indicia of responsibility include the holding of corporate office, control over financial affairs, the authority to disburse corporate funds, stock ownership, and the ability to hire and fire employees; and
  \item delegation will not relieve one of responsibility.
\end{itemize}

business operations of their companies.\textsuperscript{83} As far as can be determined, the Australian courts have not developed a similar doctrine either in the limited form in which it is now applied in the US or at all.

The views of Slemrod and Young seem to suggest that the reason for imposing criminal penalties on a director is based on a view that the director (or directors) was directly involved in a decision not to comply or had the means of preventing, detecting or correcting the non-compliance. A director who implements systems that are reasonable, effective and have regard to the nature and extent of the risk involved and which processes are regularly monitored and updated where necessary should not have any penalties imposed, even if the company is later found guilty of some wrongdoing provided always the director was not a participant in that conduct. In such a case, any penalty imposed should be for the account of the company only or the company and those employees who brought about the conduct in respect of which the complaint is made. Kaplan and Harrison\textsuperscript{84} note that increasing the exposure of directors to liability could result in a governance crisis, as it would affect the willingness of suitably qualified people to become and act as directors of corporations. By placing the director’s personal assets at risk, it increases the cost of acting as a director, which may be greater than its benefits and becomes (at416):

‘a threat to the corporation as well as to directors, since it jeopardizes the corporation's supply of an important resource and enhances the criticality of its dependence on this resource’.

Daniels\textsuperscript{85} suggests at (page 243) that on the surface, a case can be made for directorial liability based on the assumption that directors are involved in the day-to-day


management of a corporation but believes this assumption is fallacious. Directors are not bound to participate in or approve every decision made by the company. Directors’ functions are oversight, direction and control. It is because of directors’ power to gather and disseminate information, coupled with an ability to shift risk, that legislatures believe directors are the natural target for attention. This ability to shift risk is dependent on the state being prepared to accept such a transfer. This is often not the case.

Daniels (at pages 245–6) believes that directors may be targeted because of the role of the independent director. These persons are not dependent on the company for their livelihood, generally holding senior positions in other companies. Any wrongdoing by the corporation would affect their reputations, which they value highly and will always act to protect. If this is the rationale to ensure the necessary processes are put in place it is unnecessary. If processes are not in place all directors would be liable not because of some deemed liability but because they breached their duties to the corporation.

Daniels (at pages 251–3) refers to the due diligence defence (such as that contained in section 8Y (2) Taxation Administration Act 1953) and states that directors have significant problems in identifying durable and effective safe harbours. If there is no ability to shift risk, liability falls squarely on the shoulders of the director. As a result,

‘the board will rationally constrain socially desirable risk-taking in an effort to limit directors' liability. Alternatively, as in the cases surveyed at the outset of this article, directors will resign from boards at the first sign of crisis’.

The fact that the board of directors is usually dominated by insiders compounds the problems. Such insiders include management of large corporations and controlling shareholders in closely held companies.

The final problem is what Daniels refers to as sub-goal pursuit, which is the prospect that lower level employees, whose cooperation is essential for the implementation of an effective corporate compliance regime, will fail to take proper care in performing activities that entail risks of directors’ liability. He says (at pages 254–5) that:
By withholding or, even more aggressively, distorting front-line information, employees may be able to bias board decision-making in directions that would be deemed perverse were accurate information available. Thus, the conclusion of sub-goal pursuit into the analysis of supplementary liability raises legitimate concern over whether a board, even one that is committed to full realization of the corporation's legal and social obligations, will be able to ensure responsible corporate conduct. Obviously, the severity of these problems is greatest in those companies with complex and multi-tiered internal organizational structures.

He concludes (at page 255) that the issue as to whether to impose directorial liability is a very complex problem. He states:

In some cases, liability chill will deter talented individuals from accepting a nomination for board service. Alternatively, individuals may agree to serve on boards, but then insist as a precondition of service that management sedulously avoid any activities entailing the prospect, however remote, of directors’ liability. In either case, the costs, to the corporation and to society, of foregone wealth production are clear and unequivocal.

The issue of what Daniels refers to as sub-goal pursuit has significant implications for any regulatory authority that seeks to impose liability on directors for wrongs committed by the companies they represent. Assume a company has good corporate governance processes, seeks to comply with all its tax obligations and has processes available to detect and deter wrongdoing. If employees have sent distorted information to a board of directors who have done everything they could to prevent wrongdoing but nevertheless the company commits a wrong, these directors should not be held liable for these actions.86 Directors set policy and strategic goals for a company. They rely on employees to carry out these directions properly but subject to safeguards. If employees go on frolic of their own then it seems there is nothing that the directors could have done to prevent the wrong. Liability in such circumstances would not be justified on any basis.

Writing on the UK experience Baldwin noted that: ‘many feared that the Government, had decided to “go after individuals” as a matter of considered policy’. Baldwin noted that many regulators believe that personal liability encourages compliant behaviour but the results of the survey conducted by him suggested the reality is otherwise. Various possible reasons for this were given. These are that: corporate responses are lagging behind government strategies; senior corporate personnel do not see regulatory risk negatively in terms of liability; or there was confusion about the nature and extent of possible liability. Baldwin states ‘he prospect of sanctions may lead such companies and their staff to behave in ways other than straight compliance-seeking even on rational deterrence assumptions.’

Compliance is one way of reducing the risk of sanctions. Examples of other ways include shifting the blame onto others or creative compliance and as such bringing pressure on the regulator not to prosecute. The risk of sanctions may even induce corporations to act by taking out insurance or risk sharing or enhancing the ability of the company to withstand any sanction imposed.

He continues:

On rational deterrence assumptions a company will balance the costs and benefits of compliance with the expected costs and benefits of non-compliance—to be calculated by *inter alia* multiplying the probability of having to pay a penalty and the quantum of any penalty (as ameliorated by any damage-limiting measures taken). Overall it will choose the combination of risk-reducing responses that maximises benefits over costs.

Baldwin concludes his analysis by referring to Christine Parker who states there are two main ways to use liability to increase a company's commitment to self-regulation.

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88 Above n 87, 368–70.
89 Above n 87, 370–1.
90 Above n 87, 375–6.
First, liabilities can be adjusted by reference to the company’s self-regulation programme and second uses the coercive powers of courts or regulators to require or encourage a company to implement a self-regulatory system when a breach has been alleged or has occurred.

The forgoing sets out the same views suggested by the author in this research, albeit phrased in meta-regulation terminology.

5 Conclusions

The forgoing review for the various bases described by government bodies to justify deemed liability are subject to serious criticism. These critiques are reinforced when regard is had to dicta such as those cited above in cases such as Coetzee and Whyte.

In the author’s opinion there is no need for provisions which impose liability simply by virtue of the office held. Direct remedies are available which are better suited to the wrongs in respect of which complaint is made. Either the director is a direct participant in the wrong where normal criminal law criteria should be used to obtain a conviction or there has been a breach by the director if his corporation law obligations which give rise to remedies under the Corporations Act.