



## INDIVIDUAL

# Directors' right to seek external professional advice

Generally, boards make decisions on behalf of organisations by resolutions passed at duly convened meetings of the board or by circular resolutions in writing of all directors.

Also, generally, individual non-executive directors do not have legislative or constitutional authority on their own initiative to commit the organisation to a contract, including one to provide professional advice to the director on matters relating to their board service.

Organisations, whether on the initiative of management or by board resolution, often take external professional or consultancy advice on matters under consideration by the organisation and/or its board. That advice may be for the benefit of the organisation generally, or even only for the benefit of the board discretely from management; for example, in the performance of its oversight role of management, the board may need advice independent of any affiliation with management.

In terms of seeking external professional advice, the following good governance practice is recognised:

- On occasions, the entire board may wish to obtain external professional advice separately from the organisation on matters relating to their duties and responsibilities as a director(s);
- On other occasions, an individual director or a subset of directors may wish to obtain external professional advice separately from the organisation and the board on matters relating to their duties and responsibilities as a director(s);
- Provided they are acting in good faith, it is reasonable for them to do so at the expense of the organisation and accordingly;
  - They should be entitled to reimbursement of expenses for the external professional advice taken
  - They should not risk breaching confidentiality obligations owed to the organisation by taking that advice.
- In such a case, an authority to do so should be given in accordance with applicable policies and procedures;
- Commonly, such an authority is found in one or more of the following instruments which have contractual status between the organisation and the director:
  - Organisation's constitution;
  - Organisation's governance or board charter;
  - Letter of appointment by which the director was appointed to office;
  - Deed of access, indemnity and insurance between the organisation and the director.

As board members act in a collective capacity where trust and confidence is valued and consensus decision making is favoured, directors should exercise any right to take individual expert professional advice sparingly and only in circumstances where the director has a legitimate and significant reservation concerning the matter upon which the advice is sought, and which reservation the board and its professional advisers (as appropriate) are not able or are not willing to address to the reasonable satisfaction of the director.

It is considered good practice to have policies and procedures in place to allow for this. Such policies and procedures on seeking external professional advice at the organisation's expense are often documented in the organisation's board or governance charter. This is further discussed below.

### What legislative provisions are relevant?

Although *replaceable rule 202A (2) (c)* of the *Corporations Act 2001* (the Act) states that a company may pay the directors' travelling and other expenses that are properly incurred in connection with the company's business, even if the section did apply, without further authorisation it is unlikely to extend to a director obtaining external professional advice for themselves.

No other section of the Act expressly addresses a director's right to assistance from external advisers,<sup>1</sup> nor is this a matter commonly covered in other legislation under which an incorporated entity may be registered.

Importantly, individual directors do not have the authority to bind the company in a contract.

Case law is also yet to recognise any general right for individuals to seek external advice.

### What is good corporate governance practice?

Guidance has been provided by the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations (ASX Principles)*<sup>2</sup> The commentary to Recommendation 1.1 states the following with respect to access to external professional advice:

*The board charter should state the entity's policy on when and how directors may seek independent professional advice at the expense of the entity. This generally should be whenever directors, especially non-executive directors, judge such advice necessary for them to discharge their responsibilities as directors.*

The commentary to Recommendation 1.3 states that a director's agreement or letter of appointment should contain:

*... the entity's policy on when directors may seek independent professional advice at the expense of the entity (which generally should be whenever directors, especially non-executive directors, judge such advice necessary for them to discharge their responsibilities as directors).*

As board members act in a collective capacity where trust and confidence is valued and consensus decision making is favoured, directors should exercise any right to take individual expert professional advice sparingly.



1. R P Austin and I M Ramsay, 2018, *Ford, Austin and Ramsay's Principles of Corporations Law*, 17th edition, LexisNexis Australia.

2. ASX Corporate Governance Council, 2019, *Corporate Governance Principles and Recommendations*, 4th Edition, February, <https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf>, (accessed 10 September 2019).

Organisations often include a statement of policy in their board or governance charter as to the right of a director to seek external professional advice. A sample of such a statement follows:

#### STATEMENT OF POLICY

##### Independent Professional Advice

A board member is entitled to seek independent professional advice (including but not limited to legal, accounting and financial advice) at the company's expense on any matter connected with the discharge of his or her responsibilities, in accordance with the procedures and subject to the conditions set out below:

- the board member must seek the prior approval of the chair (or deputy chair/senior independent director as appropriate having regard to the relevant circumstances);
- in seeking such prior approval, the board member must provide details of:
  - the nature of and reasons for the independent professional advice to be sought;
  - the likely cost of obtaining the independent professional advice; and
  - details of the independent adviser the board member proposes to instruct.
- the approval of the chair (or deputy chair/senior independent director as appropriate) must not be unreasonably withheld.



The presence of independent advice, particularly in related party transactions, may assist directors in marshalling arguments to counter assertions that may be made that the director has failed in his/her duties and responsibilities.

This is designed to maintain a level of managed control over the process and to guard against directors taking excessive, and perhaps unnecessary, costly advantage of the policy.

Some boards may decide to have a recommended panel of expert advisers from which to choose when independent advice is sought.

Where advice is received individually by a director at the company's expense, provided that any privilege attaching to the advice is not comprised and the other directors request the advice, the advice might also be shared with other board members for information purposes.

##### When is advice independent?

Generally speaking, directors should consider whether they ought to have the advantage of independent advice from advisers not otherwise employed by the organisation or the board as a whole).

For clarity of advice and possible future evidentiary purposes, it is preferable that advisers provide the director with written advice.

In the US, the Security Exchange Commission's view is that the use of truly independent counsel is also a factor looked upon favourably by the courts and may help to shield directors from assertions of breach of duty in certain circumstances. The presence of independent advice, particularly in related party transactions, may assist directors in marshalling arguments to counter assertions that may be made that the director has failed in his/her duties and responsibilities. Independent counsel will also assist the directors to evaluate issues with an independent and critical eye.

## To what extent can the advice be relied on as a defence?

Section 189 of the Act provides that a director's reliance on information or advice is taken to be reasonable (unless the contrary is proved) if:

- (a) *The director relies on information, or professional or expert advice, given or prepared by ... 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;*
- (b) *The reliance was made in good faith and after making an independent assessment of the information or advice, having regard to the director's knowledge of the corporation and the complexity of the structure and operations of the corporation; and*
- (c) *The reasonableness of the director's reliance on the information or advice arises in proceedings brought to determine whether a director has performed a duty under this Part or an equivalent general law duty.*

However, there are a number of cases which suggest that, in relation to directors' core duties, there will be limitations on the extent to which reliance can be placed on information or advice from experts or professional advisers. For example, in the Healey case (*ASIC v Healey* (2011) FCA 717) the court accepted that errors in relation to financial reporting had been made by the company's auditors and management. The directors argued that they had not breached their duty in signing off on the financial reports because they had relied on the advice of the auditors and management. However, the Federal Court rejected this argument, saying:

*Directors cannot substitute reliance upon the advice of management for their own attention and examination of an important matter that falls specifically within the Board's responsibilities as with the reporting obligations. The Act places upon the Board and each director the specific task of approving the financial statements. Consequently, each member of the board was charged with the responsibility of attending to and focusing on these accounts and, under these circumstances, could not delegate or 'abdicate' that responsibility to others.*

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