



INDIVIDUAL

Rights of directors

The rights of company directors focus on enabling a director to effectively perform their duties whilst a director of a particular company and allowing a director to defend themselves in legal proceedings after ceasing to be a director of that company. Rights are often set out in either a company's constitution or in the *Corporations Act 2001* (Cth) (the Act) replaceable rules if the company has no constitution.

A key right for directors is to have adequate information to allow them properly to meet their obligations to the company. Protocols for obtaining information should be included as part of a corporate governance charter and in a director's terms of engagement.

What rights do directors have?

The right to receive documents in the company's possession

A director has a general right of access to documents in the company's possession in a timely manner to enable him or her to carry out their director functions. In practice, boards are frequently provided a broad right of access to enable the director to do their job properly.

The *Centro* case (*ASIC v Healey* (2011) FCA 717) has shown that managing the flow of information for directors is critical – a director needs to ensure the volume of board papers is appropriate, that key matters are highlighted, and the information is comprehensible to all directors. In this regard, directors should always exercise independent judgement and make proper inquiries about the information presented by management. As stated in the *Final Report Royal Commission in to Misconduct in the Banking, Superannuation and Financial Services Industry Volume 1*, "boards cannot operate properly without having the right information. And boards do not operate effectively if they do not challenge management".¹

1. K M Hayne, 2019, *Final Report Royal Commission in to Misconduct in the Banking, Superannuation and Financial Services Industry Volume 1*, February, Commonwealth of Australia, pp 396, <https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf>, (accessed 4 June 2019).

There may be circumstances where external information is not given to directors for a limited period of time. For example, at certain points during a takeover.

For listed entities, Recommendation 5.2 of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* (ASX Principles) proposes that, directors of an entity should receive copies of all published market announcements of the entity in a timely manner.²

The right to inspect documents and financial records

At law, a director has the right to inspect, and to take copies of, the books and accounts of the company for a proper purpose. A director may exercise that right personally or employ a proper agent to make the examination on their behalf.

Currently serving directors (but not their agents) have the right to inspect books, other than financial records, at all reasonable times for the purposes of a legal proceeding to which they are party or wish to bring against others or believes may be brought against them (s 198F(1)). They also have the right of access for a currently serving director to 'financial records' (which are defined in a relatively limited way in s 9) at all reasonable times (s 290).

A director may apply for a court order to allow another person to inspect and make copies of the records on their behalf. The court must be satisfied that the applicant is acting in good faith and that the inspection is to be made for a proper purpose. Before resorting to legal action to access documents, it is suggested that a director should approach the chair, company secretary and/or CEO. In some instances, the company cannot refuse access to the information.

Former directors have the right to inspect books, including financial records, for up to seven years after ceasing to be a director (s 198F). Again, this only applies for the purpose of a legal proceeding. This period of access may be extended by the company and its directors entering into appropriate deeds of access (often called a Deed of Access and Indemnity). *Boulos v Carter; Re Tarbs World TV Australia Pty Ltd* (2006) 24 ACLC 46 established that a former director may request access to bring an action on behalf of the company provided they have standing under s 236, are acting in good faith and obtain the leave of the court (s 237) to do so.

The Explanatory Memorandum relevant to s 198F states that information can only be used by the director for the purposes of the company. This suggests that if an ex-director and the company are in litigation with each other it may be difficult for the ex-director to establish that access to documents are for the purposes of the company. If a director holds shares in the company, they will also have the rights of a shareholder. Shareholders have the right to access the minutes of general meetings of members only (s 251B). Members also may apply to the courts for access to company books under s 247A or may apply to their board for the purpose of inspecting books of the company by passing a resolution at a general meeting under s 247D.

The right to delegate

Unless the company's constitution provides otherwise, the directors of a company may delegate any of their powers to anyone (s 198D). The delegation must be recorded in the company's minute book. Good governance practice suggests boards establish a formal written list detailing the delegation of authority and attached the list within their governance or board charter.

If the directors delegate a power, s 190 makes the directors responsible for the exercise of that power by the delegate as if the power had been exercised by the directors themselves.

However, a director will not be responsible for the exercise of power under the delegation if:

- the director believed on reasonable grounds at all times that the delegate would exercise the power in conformity with the duties imposed on directors of the company by the Act and the company's constitution (if any); and
- the director believed on reasonable grounds and in good faith, *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.

2. ASX Corporate Governance Council, 2019, *Corporate Governance Principles and Recommendations*, 4th edition, February, p 21, <https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf>, (accessed 4 June 2019).

Delegation does not excuse a director from their duty of care and diligence. Directors should establish clear oversight of the delegate individual(s) by making proper inquiries and holding them to account. As explained in the final report of Prudential Inquiry into the Commonwealth Bank of Australia, a board's effectiveness in monitoring and overseeing may be weakened if they are over-confident in the board committees and executive management.³ It is therefore suggested that directors remain vigilant in relation to delegations and ensure sufficiently robust checks and balances avoiding over-confidence and over-collaboration are in place and effective.

Reliance on information or advice

In legal proceedings alleging breach of a director's duty, a director may raise, as a defence, reasonable reliance on information or professional or expert advice provided by others (s 189). Unless it is proven otherwise, the director's reliance on the information or advice is taken to be reasonable.

Essentially, the director must prove:

- (a) the director relied on information, or professional or expert advice, given or prepared by:
 - (i) an *employee* of the corporation whom the director believed on reasonable grounds to be reliable and competent in relation to the matters concerned; or
 - (ii) a *professional adviser* or expert in relation to matters that the director believed on reasonable grounds to be within the person's professional or expert competence; or
 - (iii) another *director or officer* in relation to matters within the director's or officer's authority; or
 - (iv) a *committee of directors* on which the director did not serve in relation to matters within the committee's authority; and
- (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.

However, the courts have been firm that directors cannot substitute reliance upon the advice of management or others for their own attention and examination of an important matter that falls specifically within the board's responsibilities – matters such financial reporting obligations (*Centro* case) or statements to the markets (*James Hardie* cases).

The final report of Prudential Inquiry into the Commonwealth Bank of Australia also illustrated that reliance on key individuals hinders full utilisation of the collective expertise of board members and management, leads to individual preferences and biases, and limits robust discussion in meetings.⁴ For example, the CBA board and their board risk committee (BRC) had heavily relied on the discretion of the BRC chair and the Chief Risk Officer, who were both recognised as industry experts with 'scholarly gravitas'. Other less-experienced committee members felt less confident in challenging them and this eventually undermined group collaboration.

The right to obtain insurance against liability for breaches of duty in certain circumstances

This is a complex area. Directors can obtain insurance against liability in certain circumstances but they cannot obtain insurance for certain breaches of the Act (or indeed some other breaches of legislation). It is important to have appropriate directors and officers insurance (often referred to D&O insurance), not the least because an indemnity will be of little assistance if the company has insufficient funds to meet a claim by a director for indemnity.

What are some other rights?

In *Ford, Austin and Ramsay's Principles of Corporations Law* (I M Ramsay and R P Austen, 2018, 17th edition, LexisNexis Australia), Ramsay and Austen identify other director rights:

- Lawful administration of the affairs of the company
- The right to enforce statutory provisions
- The right to enforce the corporate constitution
- Remuneration (if in a director's terms of engagement)
- Participation in board decisions
- Indemnity
- The right to remain in office until validly removed

3. J Laker, J Broadbent and G Samuel, 2018, *Prudential Inquiry into the Commonwealth Bank of Australia*, Australian Prudential Regulation Authority, April, s 2.2.6 (p 20) and s 9.2.6 (pp 89-90), https://www.apra.gov.au/sites/default/files/CBA-Prudential-Inquiry_Final-Report_30042018.pdf, (accessed 3 June 2019).

4. *Ibid*, pp 17-18.

What rights do officers have?

Officers are defined as a director or secretary of the organisation, a person who makes or helps to make decisions that affect the whole or a substantial part of the business or who may significantly affect the company's financial standing, or receivers, administrators, liquidators and trustees (s 9). However, the specific rights of directors referred to above do not always extend to other officers. Therefore, officers would need to have rights provided in a specific agreement such as a deed of access and indemnity, as discussed below.

Because company secretaries are defined as officers under the Act, the board should consider indemnifying them in appropriate circumstances.

What are deeds of access and indemnity?

In addition to the statutory requirements of the Act regarding access to information, organisations will normally offer directors deeds of access and indemnity. The deed will ordinarily give directors access to company documents and records should a legal claim ever be made against them relating to their office. When reviewing these types of deeds, directors should consider the following potential limitations:

- The right of access does not apply to any documents over which the entity claims legal professional privilege.
- Whether the right of access should be limited to a particular period after the director has ceased service (for example, seven years).
- An undertaking by the director to keep the contents confidential, except where they must be disclosed in court proceedings or as required by law.

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