Directors' Duties and Liabilities – Where Are We Now and Where Are We Going in the UK, Broader Commonwealth, and Internationally?

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Overview

Boardroom regulation and practice is under pressure on a number of fronts in the 21st century global business environment. In Anglo-American corporate regulatory systems that broadly subscribe to market capitalism, shareholder value, and board oversight of management, the law of directors' duties and defences is increasingly becoming a domain in which some of these external pressures are brought to bear. Witness for example the transnational legal debate about corporate directors taking account of stakeholder interests and wider social responsibilities as part of a social licence to operate for business. At the same time, national corporate regulation increasingly has potential points of interaction with international economic law, transnational norms of finance and investment, and global frameworks affecting multinational business activity. It also is responsive to ongoing changes in the tension between the oversight and management responsibilities of boards as an essential component of corporate governance.

In light of these developments, this article focuses upon some key aspects of how national corporate regulatory regimes cope or engage with such developments, with special emphasis upon the similarities and differences in approach and test case issues that are emerging in two Anglo-American jurisdictions (ie the UK and Australia) in response to such developments. In particular, this article focuses upon comparative lessons for the development and reform of Anglo-Australian corporate law due to recent legislative reform and litigation in each jurisdiction affecting corporate directors and managers, the multiplicity of ways in which conventional corporate governance law and practice potentially engages with the corporate social responsibility (CSR) agenda, and the implications for such corporate regulatory regimes of the newly accepted framework and guiding principles on business and human rights from the UN Human Rights Council. Selective reference for illustrative purposes is made to recent developments internationally (eg UN) and in the EU, Anglo-American jurisdictions (ie the USA, Canada, UK, Australia, and New Zealand), and South Africa.

The Need for Transnational and Cross-Jurisdictional Perspectives

Corporate boards and those who regulate and advise them must increasingly have one eye on the business and regulatory environment in their own jurisdiction and another eye on comparative models, norms, and lessons from other jurisdictions. In particular, why might UK and Australian company directors and in-house counsel, corporate lawyers and other professional advisers, governmental regulators of business, and even members of a multinational company's supply and distribution chain need to take account of boardroom obligations under law and regulation outside their own country? Indeed, some of the multiple levels on which this comparative and global perspective is increasingly necessary apply equally beyond the UK and Australia to other Anglo-American jurisdictions and developed corporate regulatory regimes across the globe (eg the EU).

First, in terms of the 21st century realities of borderless corporate groups and activities, transnational corporations (TNCs) obviously need to comply with corporate law and regulation in each country in which they do business.

[1] Contacts: bryan.horrigan@monash.edu; work 61-3-99053359. This paper significantly revises and updates the presentation by the author to the invited clients of Four New Square at Lloyds in London on 15 November 2010, as part of Four New Square's seminar on *Directors' Duties and Liabilities: Where Are We Now and Where Are We Going?*'.

This covers dual-listed companies seeking to have their shares traded on national securities exchanges, companies seeking to relocate their corporate headquarters across jurisdictions, and foreign corporations and corporate actors who must comply with local laws wherever they do business.[2]

This is a matter for corporate boards, in-house counsel, and senior management of multinational corporate groups. Similarly, company directors who sit on the boards of parent, subsidiary, or other companies across more than one jurisdiction need to take heed of the law of directors' duties and other boardroom obligations in each country. For example, UK-based and other overseas directors were involved in some recent landmark Australian corporate law cases, including litigation over the finance and security arrangements of the Bell Group companies involved in a financial work-out, as well as the regulatory prosecution of directors of the James Hardie group for misleading public statements to the investment community about a compensation fund for asbestos victims.

Corporate conduct or decisions occurring in one country might still have legal relevance in another country, under local laws with extra-territorial effect. 'Some of the conduct and events that are the subject of this case occurred in the United Kingdom and Europe', noted the trial judge in one of Australia's recent leading cases on directors' duties and business judgment defences.[3] Similarly, overseas supply and distribution chain members might be contractually held to standards or become subject to reporting obligations that are grounded in the corporate law of a multinational company's country of origin. If that country of origin is the UK, such business value chain arrangements become reportable matters under business review requirements in the UK Companies Act, as detailed later in this article.

Secondly, corporate regulation and practice is responsive to the growing interactions between national, transnational, and global norms affecting business on multiple levels.[4] Cross-jurisdictional thinking and practice of good corporate governance informs the design and implementation of corporate governance law and regulation. For example, the UK Cadbury Report's landmark standard-setting on corporate governance has influenced the evolution of corporate governance in the UK and other anglophone countries. Similarly, the principle-based 'comply or explain' approach to recent corporate regulation in the EU, UK, and Australia contrasts with what is often described as a more prescriptive rule-based approach in other jurisdictions from time to time, as exemplified by the original US Sarbanes-Oxley Act, although such sweeping systemic characterisations have their own difficulties and limits.

More broadly, the acceptance in mid-2011 by the UN Human Rights Council of a new overarching framework and guiding principles on business and human rights now awaits national implementation and integration in business regulation and practice. At the same time, those standards are progressively being incorporated or otherwise aligned with important global standards such as the UN Global Compact, revised OECD Guidelines for Multinational Enterprises, and updated social and environmental standards from the World Bank's International Finance Corporation.

Thirdly, CSR's own progress in the 21st century from the periphery towards the mainstream of business regulation and practice is matched by the twin developments of at least some convergence between CSR and corporate governance, together with the emergence of an emerging body of comparative and transnational law and regulation in which CSR concerns can arise, directly or indirectly. Global business and regulatory conditions are pushing companies and their boards to be more economically, socially and environmentally responsible. The G8 and G20 countries list CSR-related concerns about responsible lending, sustainable development, and climate change as geopolitical priorities.

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[2] Eg Australian companies with UK operations complying with new 2010 UK foreign bribery laws (see Allens Arthur Robinson, 'Focus: UK Bribery Act Passed – Corporate Liability for Failing to Prevent Bribery', April 2010), and Australian and UK companies with US operations needing additional global insurance coverage after the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (see 'US Reforms Expose Directors to Claims', The Australian Financial Review, 2 August 2010, at p 13).

[3] *ASIC v Rich* [2009] NSWSC 1229 at [7183].

[4] On the general phenomenon of interaction between local, municipal, and international norms in the globalisation of legal orders, see, for example: P. C. Berman, 'From International Law to Law and Globalization' (2005) 43 *Columbia Journal of Transnational Law* 485.

The groundswell of global support for standards such as the UN Global Compact, Principles for Social Investment, and Principles for Responsible Investment swings the pendulum further towards CSR, as does the European Commission's renewed CSR focus through its Social Business Initiative and new Strategy for CSR announced in late 2011. In addition to the integration of human rights within corporate compliance, due diligence, and organisational risk management and reporting systems under the UN-based global standards discussed above, for example, even conventional regulation and practice of corporate governance and responsibility can confront CSR-related concerns in areas such as directors' duties and defences, annual corporate reporting, legal compliance and due diligence, shareholder proposals, stakeholder engagement mechanisms, investment decision-making, and corporate governance standards. These trends are tracked and illustrated from legal and other disciplinary perspectives by new scholarship that highlights the commonalities and contrasts of principles and other standard-setting across jurisdictions.[5]

Fourthly, the first decade of the 21st century is producing many challenges to the prevailing notion of shareholder primacy, value, and wealth-maximisation that arguably underlies much Anglo-American corporate law and regulation in general and the legal responsibilities and liabilities of corporate boards and managers in particular.[6] Considered from the academy's perspective, these challenges stem from sources as variable as cross-disciplinary opposition to shareholder-based normative theories of corporate governance, debates about the sustainability and limits of market capitalism, and new calls for 'shared value'[7] and other models of corporate engagement with society to replace business as usual. What still remains in doubt is the extent to which notions of 'shared value' and socially sustainable capitalism represent threats to shareholder-based norms of corporate governance and business success, or simply different ways of meeting or even reconceiving them. After all, even one of the most widely quoted opponents of CSR, Milton Friedman, once argued that his own famous statement that 'the social responsibility of business is to increase its profits' was equivalent to the argument of a CSR advocate that 'the enlightened corporation should try to create value for *all* of its constituencies'.[8]

Fifthly, good corporate legal and policy reform takes account for modelling purposes of the corporate problems and regulatory solutions adopted in comparable jurisdictions. This has a number of manifestations. Recent corporate law inquiries and reform initiatives in the UK, Australia, and elsewhere explicitly or implicitly include within their terms of reference the need to consider comparable lessons and experiences from other jurisdictions. The corporate constituency and anti-takeover statutes in numerous US states are models on some level for the emergence of laws in other countries that explicitly permit or even require reference by directors in their decision-making to a range of shareholder and broader stakeholder concerns, as in the new legislative statements of directors' duties and correlative business review requirements under the UK Companies Act. Corporate governance standard-setting draws upon good practice in corporate governance thinking and behaviour across jurisdictions. Hence, this area of concern is a matter for corporate law-makers, policy-makers, and regulators, including courts and the lawyers who appear before them.

Finally, lawyers and judges engaged in the art of making and assessing arguments about matters of corporate law can gain insight from what has been argued and decided elsewhere, especially when there are new laws, unresolved issues, or novel applications. In some developing economies, reference to the corporate legislation and case law of other countries is officially authorised for instructive purposes in interpreting and developing that country's own corporate law.[9]

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[5] Eg B. Horrigan, *Corporate Social Responsibility in the 21st Century: Debates, Models and Practices Across Government, Law and Business*, 2010, Edward Elgar Publishing, UK; and M. Kerr, R. Janda, and C. Pitts, *Corporate Social Responsibility: A Legal Analysis*, 2009, LexisNexis, Canada.

[6] For a landmark defence of the shareholder-based norm in mature corporate regulatory systems worldwide that has generated much scholarly debate, see: H. Hansmann and R. Kraakman, 'The End of History for Corporate Law', in J. Gordon and M. Roe (eds), *Convergence and Persistence in Corporate Governance*, 2004, Cambridge University Press, Cambridge.

[7] Eg M. Porter and M. Kramer, 'Creating Shared Value: How to Reinvent Capitalism – and Unleash a Wave of Innovation and Growth', *Harvard Business Review*, January-February 2011, HBR Reprint R1101C.

[8] See the sources and analysis in Horrigan, note 5, at pp 92-93.

[9] For example, section 5(2) of the current South African Companies Act says that '(t)o the extent appropriate, a court interpreting or applying this Act may consider foreign company law'. In addition, constitutional protection of human rights is also a relevant matter for South African corporate law, given that section 5(1) states that the Companies Act must be

Even in mature corporate regulatory systems that share a common transnational heritage and adjudicative methodology as common law systems, commonalities and contrasts in corporate legal problems, courtroom arguments, and judicial outcomes across jurisdictions can be instructive in testing and developing the boundaries of corporate law. This is a matter for judges, barristers, and solicitors seeking to explore the boundaries of corporate law's development and application.

For example, cases in the UK and Australia that have been decided both before and after the passage of the UK Companies Act in 2006 suggest that this practice will continue, whatever differences continue to emerge in the regulation and practice of corporations under each country's unique blend of political, economic, and legal conditions. Indeed, UK cases on corporate law since the enactment of that country's new Companies Act suggest that Australian corporate law might still have something to offer UK courts and those appearing before them on some of the more vexed questions of corporate law under that Act, especially concerning the interests of the company and its shareholders, directors' duties and defences, and the respective responsibilities and roles of boards and management under the law.

Comparative Lessons for UK and Australian Corporate Law

Similarities between UK and Australian Corporate Law

Despite emerging differences between UK and Australian law, there is still much for each corporate regulatory system to learn from the other, for the reasons that follow. UK and Australian corporate law and regulation have some similarities. In light of Australia's inheritance from English law and justice, as evidenced by the tendency of courts in each country to refer to decisions of courts in the other country on many critical matters of corporate law, both Australia and the UK share a common tradition of judge-made development of corporate law's fundamental doctrines, whatever different statutory and other inroads now apply in each corporate regulatory system.

Moreover, the progressive globalisation of law through appropriate judicial reference at the national and sub-national level to international and foreign law means that UK and Australian courts are also part of a broader enterprise in cross-fertilisation and modelling of approaches to corporate law and its outcomes and reform. This broader enterprise extends beyond the historical commonplace reference to one another's judgments by UK and Australian courts, and even beyond the shared heritage of corporate law doctrines and practices in the broader Commonwealth of Nations.[10] At the very least, it also includes the body of Anglo-American corporate law, an emerging body of comparative CSR-sensitive law both inside and outside corporate law, and a transnational set of policy and regulatory drivers (eg the facilitation of environmental, social, and governance (ESG) considerations in investment decision-making) that are penetrating business conduct and corporate law alike. Such developments raise questions under corporate law about the scope for directors' duties to permit or even require reference to human rights and other stakeholder interests, especially under human rights due diligence and other business reforms signalled by the UN Human Rights Council mandate of Harvard's Professor John Ruggie, as detailed later in this article.

Australia and the UK also both subscribe to shareholder primacy as the foundation of corporate law and governance, at least in comparison with alternative corporate regulatory models such as European-style co-determination or stakeholder pluralism, although shareholder primacy's recent UK manifestation in the legislated policy of 'enlightened shareholder value' (ESV) has some elements that Australian corporate law lacks. To that extent, the corporate laws of countries such as Australia, the UK, and the USA provide some evidence for what some leading comparative corporate law scholars call a wider transnational convergence on shareholder primacy as the ultimate model for corporate law and practice.[11]

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interpreted according to its designated purposes which, under section 7, include a purpose to 'promote compliance with the Bill of Rights as provided for in the Constitution, in the application of company law'.

[10] Eg A. Capuano, 'The Realist's Guide to Piercing the Corporate Veil: Lessons from Hong Kong and Singapore' (2009) 23 *Australian Journal of Corporate Law* 56.

[11] Eg H. Hansmann and R. Kraakman, 'The End of History for Corporate Law', in J. Gordon and M. Roe, eds, *Convergence and Persistence in Corporate Governance*, Cambridge University Press, Cambridge (Mass).

In contrast to the prescriptive rule-based approach to corporate governance that characterised the post-Enron approach in the USA, at least as enshrined initially in the Sarbanes-Oxley Act, both Australia and the UK subscribe to a more flexible principle-based approach to corporate governance regulation, although the distinction between the two regulatory approaches cannot be pushed too far.[12] Since the passage of the landmark UK Companies Act in 2006, Australia and the UK both have the law of directors' duties expressed in legislative form. Finally, in the wake of the recent global financial crisis (GFC), together with increased international coordination and harmonisation of approaches to key aspects of corporate and financial regulation, both Australia and the UK are experiencing post-GFC pressures and other developments that continue to put corporate law and its ongoing reform under the microscope.[13]

Differences between UK and Australian Corporate Law

At the same time, future cross-fertilisation of arguments and outcomes in Anglo-Australian corporate law must take account of the significant differences between the UK and Australian positions in the 21st century. UK corporate law is subject directly to the influence of EU directives and indirectly to ECHR/UK human rights jurisprudence (through horizontal integration of human rights norms in various fields of law) that remain foreign to Australian corporate law. This can be contrasted with the amenability to foreign, international, and human rights concerns under South African corporate law.

Indeed, despite many ongoing similarities in fundamental doctrines of corporate law, there are also key differences in the legislative wording of directors' duties and defences, directors' reporting obligations, shareholder derivative actions, and other key aspects of corporate governance law and regulation in each country. For example, Australia has a statutory business judgment defence for directors, whereas the UK has no such defence expressly encapsulated in its Companies Act, although there are elements of good faith that are relevant in different ways in each country's treatment of directors' duties and defences. This includes an Australian defence to a director's statutory duty of good faith for the directors of wholly-owned subsidiaries, as well as other business judgment considerations that condition judicial findings of a breach of a directorial duty of care. Nevertheless, the UK now mandates a set of considerations for directors under the duty of loyalty and business review in the UK that Australian corporate law and public inquiries on possible corporate law reform have resisted to this point in time.

Finally, the UK's legislative incorporation of shareholder ratification in the UK Companies Act 2006 overtakes Australian corporate law, where there is no legislative authorisation of shareholder ratification to cure breaches of directors' duties. In Australia, there is therefore residual concern about the capacity of shareholders to excuse what effectively amounts to a breach of statutory duty owed by directors. However, some High Court of Australia dicta also pave the way for shareholder ratification to influence the preconditions for characterising a breach of duty in particular circumstances, as discussed below.

Convergence and Divergence in Corporate Governance

The GFC and its ongoing fall-out in the courts in both countries place the spotlight once again on conceptions and practices of governance. 'Governance in the broad sense is open for debate – the role of the state, international cooperation, the scope of prudential regulation, the role of boards of directors and in particular risk management procedures and capital adequacy requirements are all being questioned', in the pithy assessment of one leading Anglo-Australian corporate law and governance scholar.[14]

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[12] The 'comply or explain' (or 'if not, why not') approach to corporate governance regulation in the EU and the UK is exemplified in Australia in the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*, last amended in 2010.

[13] In the UK, see eg S. Graham, 'Directors' Duties: Current Interpretation and Future Reforms', Wragge & Co, September 2009 ('The Companies Act 2006 (2006 Act) is not yet three years old. The statutory statement of directors' duties (the statutory statement) is younger still ... There is, nevertheless, already a significant body of 2006 Act-related case law ... There are, at the same time, a number of reform proposals now circulating in the arena of directors' duties that have been stimulated by the ongoing financial crisis. It cannot have escaped anyone's notice that we are, only a decade on from the Company Law Review, barely six years after the Higgs report, at another critical juncture in the regulation of company directors.').

[14] J. Farrar, 'The Global Financial Crisis and the Governance of Financial Institutions' (2010) 24 *Australian Journal of Corporate Law* 227.

As foreshadowed above, recent developments in the UK, Australia, and North America evidence the regulatory trend across jurisdictions towards a closer alignment between CSR and corporate governance. CSR-sensitive considerations are permeating at least some aspects of corporate law across jurisdictions, as well as other aspects of corporate regulation. The old paradigm kept CSR separate and marginalised form the core concerns of corporate law and its relationship to business success, legal standards, and market efficiency as means to the end of social equity, efficiency, and effectiveness.

In other words, CSR in limited forms was perceived and acted upon largely as a voluntary add-on extra, considered largely from a corporation's standpoint alone, disengaged from any real interdependence in wider aspects of societal governance and regulation, ad the first thing to be cut back or thrown overboard in tough financial times.The new paradigm witnesses the integration of CSR within standard business practice, organisational governance, and corporate law and regulation. The European Commission's October 2011 package of measures on responsible business includes an 'updated definition' of CSR as 'the responsibility of enterprises for their impacts on society'. Together with its 'new agenda for action' on CSR, this suggests an approach to CSR in the 21st century that entails responsibility and accountability for corporate action beyond the baseline of legal compliance.[15]

CSR considerations can be integrated with most or all aspects of corporate governance, regulation, and practice in the following ways:

(1) CSR preconditions for ongoing corporate existence or entitlements (eg (i) revocable corporate charters (USA); (ii) winding up on public interest grounds; and (iii) international ethical and human rights violations as grounds for investigation and de-listing (eg OMX Nordic Exchange);

(2) corporate objectives, capacity, and powers (eg (i) not-for-profit Community Investment Corporations (CICs) accommodated as a form of corporate structure in corporations legislation (UK); and (ii) legislated capacity for directors to engage in corporate philanthropy, corporate community investment, and corporate contributions to public affairs and free enterprise (USA));

(3) official sanctioning of standard-setting authority (eg (i) corporate law's reference to CSR-sensitive auditing, accounting, and other standards and listing rules; and (ii) sanctioning corporate regulatory control of ESG standard-setting);

(4) directors' and officers' duties/defences (eg explicit or implicit authorisation for directors to consider both shareholder and other stakeholder interests in the UK, Canada, USA, Australia, and elsewhere, notwithstanding other differences between ESV, corporate constituency and anti-takeover laws, and business judgment rules);

(5) corporate disclosure and reporting obligations (eg (i) employee, environmental, and community factors in UK business review requirements; and (ii) reporting of social, environmental, and related risks as 'material business risks' under Australian corporate governance reporting requirements for listed companies);

(6) standard-setting for good corporate governance (eg stakeholder engagement mechanisms, such as former UK Combined Code's cross-reference to investment industry guidelines on corporate dialogue with institutional investors on a company's CSR performance, and complementary watchdog and standard-setting roles for non-government organisations (NGOs));

(7) shareholder/stakeholder intervention and decision-making mechanisms (eg (i) stakeholder/regulator capacity to prevent breaches of corporate law; (ii) shareholder votes on executive remuneration; and (iii) shareholder proposals on environmental, social, and governance (ESG) issues);

(8) special treatment of key non-shareholder interests (eg (i) employee benefits in corporate liquidation; (ii) long-tail corporate liabilities; and (iii) creditor interests approaching insolvency (and otherwise: see *Bell Resources* litigation));

(9) creation of incentives and removal of disincentives at the policy and regulatory level for socially and environmentally responsible corporate behaviour (eg matching governmental procurement and public approval/licensing conditions to good business compliance and corporate citizenship track records);

(10) investment promotion and decision-making (eg requirements to accommodate CSR/ESG/SRI criteria in investment decision-making (Australia, UK, and some EU countries));

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[15] *A Renewed EU Strategy 2011-2014 for Corporate Social Responsibility*, European Commission, COM (2011) 681 final, 25 October 2011.

(11) complementary voluntary self-regulation (eg (i) voluntary corporate responsibility/sustainability reports; and (ii) corporate adoption of industry codes of conduct/practice);
(12) other key laws regulating corporations and CSR (eg (i) favourable taxation/regulatory treatment of socially and environmentally responsible corporations; (ii) unfair contract terms in standard consumer agreements (UK and Australia); (iii) 'licence to operate' issues in securing public approvals/licences for business development projects (eg socio-economic and environmental impact assessments); and (iv) corporate due diligence on legal compliance and risk management (eg human rights due diligence)); and
(13) prescription of the boundaries, conditions and limitations of liability for corporations in their home jurisdictions of operation for their harmful effects (eg complicity in state-facilitated human rights abuses) in host jurisdictions (eg corporate codes of conduct and foreign direct liability mechanisms for TNCs).

Directors' Duties Under UK and Australian Corporate Law

For the purpose of understanding what cases on directors' duties and defences might offer by way of comparative guidance for lawyers, judges, and corporate regulators in each jurisdiction, compare and contrast the legislative wording on the two fundamental directors' duties – the duty of loyalty and the duty of care – in each of Australia and the UK. Under long-standing general principles of Anglo-Australian corporate law, there is a distinction between a director's duty of loyalty to the company in serving the company's interests and not their own or someone else's interests, on one hand, and a director's duty to take proper care in exercising company powers, using company resources, and meeting company responsibilities.[16] Both Australian and UK corporate law broadly reflect this position in the different directors' duties now enshrined in legislation in each country, with Australia enshrining the duty of loyalty in its statutory duty of good faith and the UK doing likewise in the duty to promote the company's success, although not in identical terms in either content or applicable defences.

Corporate law experts and commentators in both Australia and the UK readily agree that the legislative statement of directors' duties reflects shareholder primacy and incorporates the pre-existing judge-made law on directors' duties, at least to a significant degree. However, there are lingering questions about how judges might yet interpret some of the new provisions and what difference they make to business practice. Here, the major point of note for a UK audience is that Australian corporate law cases are being referred to for guidance in cases on a range of different matters arising under the new UK Companies Act. For example, Australian cases were considered in the first UK decision to approve a statutory derivative action (*Wishart v Castlecroft Securities Ltd* [2009] CSIH 65) and in one of the first UK decisions to consider the meaning of the directors' duty of loyalty under section 172 and how it relates to notions of 'the interest of the company' (*Re Southern Counties Fresh Foods Limited* [2008] EWHC 2810). To that extent and more, keeping abreast of Australian arguments and developments is important for UK corporate lawyers, regulators, and judges. Similarly, the continuing reference to English authorities in recent ASIC test cases on directors' duties and defences evidences that this is a two-way street and of just as much significance for Australian law-makers, regulators, and lawyers too.

The GFC and its litigious aftermath for corporate regulators, business leaders, and professional advisers (including corporate lawyers) gives a sharper edge than normal to the unfolding and unresolved issues on directors' duties and related matters in UK and Australian courts. As demonstrated by the series of UK cases since the phased-in operation of the Companies Act, in practice there are key relationships between the provisions on directors' duties and various other provisions relating to corporate governance, in which crucial issues of legislative meaning and practical application continue to arise. In particular, the list of provisions involving direct or indirect reference to directors' duties includes the following:
(1) the relationship between directors' duties themselves (especially section 172 on the duty to promote the company's success and section 174 on the duty of care, as dictated by section 179's instruction that duties can operate upon one another at the same time);
(2) the business review (under section 417) as a resource for shareholders and others in monitoring directors' compliance with their duties under section 172 (see section 417(2));
(3) preconditions for shareholder derivative actions (under sections 260-269), including preconditions relating to the how a person complying with the duty under section 172 would view the claim and also the possibility of shareholder ratification (under section 263(3)) ;

[16] See J. Farrar, *Corporate Governance: Theories, Principles and Practice*, 3rd ed, 2008, Melbourne: Oxford University Press, at pp 108-109.

(4) the uses and limits of shareholder ratification of breaches of directors' duties (under section 239);
(5) petitions against unfairly prejudicial conduct (under section 994), perhaps even raising questions about staying within the bounds of corporate and directorial power under section 171 or properly fulfilling directors' duties under section 172 and other provisions; and
(6) exercises of power (and fulfilment of duties) by directors' in binding the company to contracts with corporations and others who deal with the company (eg sections 39, 40, 43, and 44).

Against that background, the new legislative statement of directors' duties of loyalty and care under the new UK Companies Act 2006 can usefully be compared and contrasted in the discussion that follows with their counterparts in Australian corporate law in the Corporations Act 2001 (Cth). For reference here and elsewhere in this paper's discussion of directors' duties, section 172 of the UK Companies Act says:

172. Duty to promote the success of the company

(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—
 (a) the likely consequences of any decision in the long term,
 (b) the interests of the company's employees,
 (c) the need to foster the company's business relationships with suppliers, customers and others,
 (d) the impact of the company's operations on the community and the environment,
 (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
 (f) the need to act fairly as between members of the company.

(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.

(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

The equivalent duty of loyalty in Australia is enshrined in section 181 of the Australian Corporations Act 2001, which says:

Good faith--civil obligations
Good faith--directors and other officers

(1) A director or other officer of a corporation must exercise their powers and discharge their duties:
 (a) in good faith in the best interests of the corporation; and
 (b) for a proper purpose.

Note 1: This subsection is a civil penalty provision (see section 1317E).
Note 2: Section 187 deals with the situation of directors of wholly-owned subsidiaries.

(2) A person who is involved in a contravention of subsection (1) contravenes this subsection.

Note 1: Section 79 defines *involved* .
Note 2: This subsection is a civil penalty provision (see section 1317E).

A defence to breach of this duty is available to directors of wholly-owned subsidiaries, under section 187 of the Australian Corporations Act 2001, as follows:

Directors of wholly-owned subsidiaries

A director of a corporation that is a wholly-owned subsidiary of a body corporate is taken to act in good faith in the best interests of the subsidiary if:
 (a) the constitution of the subsidiary expressly authorises the director to act in the best interests of the holding company; and
 (b) the director acts in good faith in the best interests of the holding company; and
 (c) the subsidiary is not insolvent at the time the director acts and does not become insolvent because of the director's act.

In terms of a director's duty of care, section 174 of the UK Companies Act 2006 says:

174. Duty to exercise reasonable care, skill and diligence

(1) A director of a company must exercise reasonable care, skill and diligence.

(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—
  (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and
  (b) the general knowledge, skill and experience that the director has.

The equivalent Australian duty of care and diligence, and its correlative statutory business judgment defence, are enshrined in section 180 of the Corporations Act 2001, as follows:

Care and diligence--civil obligation only

Care and diligence--directors and other officers

(1) A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:
  (a) were a director or officer of a corporation in the corporation's circumstances; and
  (b) occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.

Note: This subsection is a civil penalty provision (see section 1317E).

Business judgment rule

(2) A director or other officer of a corporation who makes a business judgment is taken to meet the requirements of subsection (1), and their equivalent duties at common law and in equity, in respect of the judgment if they:
  (a) make the judgment in good faith for a proper purpose; and
  (b) do not have a material personal interest in the subject matter of the judgment; and
  (c) inform themselves about the subject matter of the judgment to the extent they reasonably believe to be appropriate; and
  (d) rationally believe that the judgment is in the best interests of the corporation.

The director's or officer's belief that the judgment is in the best interests of the corporation is a rational one unless the belief is one that no reasonable person in their position would hold.

Note: This subsection only operates in relation to duties under this section and their equivalent duties at common law or in equity (including the duty of care that arises under the common law principles governing liability for negligence)--it does not operate in relation to duties under any other provision of this Act or under any other laws.

(3) In this section:

"business judgment" means any decision to take or not take action in respect of a matter relevant to the business operations of the corporation.

'Test Case' Issues and Practical Implications under the UK Companies Act 2006

The Bounded Socialisation of Directors' Duties in the UK and Elsewhere

The future legal and practical ramifications of the UK's new approach to directors' duties, business reviews, and other corporate governance aspects are significant enough to warrant a whole chapter in my recent book on CSR, entitled *Corporate Social Responsibility in the 21st Century: Debates, Models and Practices Across Government, Law and Business*. More broadly, whatever the ongoing impact in their own right of the corporate law reforms contained in the UK Companies Act 2006, they also form part of the body of comparative corporate law and regulation generally and emerging CSR-sensitive law and regulation in particular, for the purposes of regulatory modelling, legal interpretation, and academic critique. Reflecting on a series of recent legal and regulatory developments concerning both corporate governance generally and CSR in particular across Europe, North America, and Australasia, my book offers this summary of the ongoing transnational project in sensitizing boardroom obligations to CSR:[17]

> In short, we are witnessing the bounded socialization of corporate obligations generally and directors' duties in particular across all of these jurisdictions, in one shape or another. This trend is one of 'socialization' because of the stakeholder-sensitivity it introduces, and yet 'bounded' because of the limits imposed upon it through various shareholder-orientated mechanisms.

[17] Horrigan, note 5, at p 198.

> Still, the debate is no longer over *whether* but *how* boardroom decision-making and reporting should accommodate a company-specific balance of shareholder, non-shareholder and societal considerations, *and* to what ends. The law regulating the obligations, liabilities and reporting requirements confronting company directors is a strong driver and moderator of socially responsible corporate behaviour. As experienced corporate lawyer and corporate responsibility advocate Robert Hinkley notes, what each jurisdiction puts into the content of directors' duties offers a critical point of leverage in bringing about necessary changes in both boardroom conduct and wider corporate behaviour.
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> At the same time, we are yet to see a paradigm shift in the orientation and content of corporate law and regulation, towards a vision of corporate governance, responsibility and sustainability, for TNCs in particular, that fully accommodates corporate, societal and global concerns *as they relate to* the corporation. (original emphasis)

Potential Impact Upon Boardroom Practice

Some quarters of the legal and business communities in the UK might have returned to a 'business as usual' mindset after fears of a spate of new litigation and increased judicial second-guessing of directors proved to be unfounded, at least in the first few years of the new Companies Act's operation. However, any such complacency underplays the unexplored potential for test case issues to arise in corporate advice and enforcement proceedings, the unresolved issues even under pre-existing general corporate law, and the impact of both upon boardroom practice.

UK opinion remains divided on how much the new regime of directors' duties really changes things in law or practice, although perhaps it is still early days in legal time, given that few cases have yet tested all possible avenues under the new regime. Referring to Professor Birds' suggestion that '(o)n the whole it is thought that the effect of s 172 is more likely to be educational rather than in any sense restrictive and that business decisions taken in good faith will not be any more easily challengeable than they were before this provision existed', Professor Alcock offers a slightly different view:

> The present author is slightly less sanguine [and] is not as certain as the CLRSG that the pre-existing common law bona fide duty was one purely based on 'enlightened shareholder value' ... The statutory provision is clearly focused on shareholder supremacy. As for the listed other interests, these may almost give rise to a Catch-22 for directors. If directors pay too much attention to one of these interests (creditors, employees, the environment, etc) they may be challenged for being in breach of the primary duty towards shareholders. If they ignore any of these interests and that proves disastrous for the company, they may be challenged for breach of their duty to exercise reasonable care, skill and diligence.

Australian judges and commentators have weighed in on the debate about the new UK regime for directors' duties too. Commenting on the UK reform to directors' duties in the 2006 Companies Act, especially the pivotal duty of loyalty, former Australian judge and corporate law expert, Bob Austin, says:[18]

> It seems likely that the reform will have an effect on boardroom process. Directors will have to be sure that their consideration of the effect of their decisions on the six matters listed in [section 172] is duly and adequately minuted. It remains to be seen whether corporate decision-making will be affected in any substantive way.

One of the members of the UK's CLR Steering Group, Lady Justice Arden, has commented publicly on how the necessary decision-making considerations listed in legislative form under section 172 might need to be brought to the attention of directors and recorded in a suitable form to meet any later challenge to their decisions, as follows:[19]

> The relevant matters are often set out in the papers presented to the board of directors, and directors will generally be able to rely on such papers having been properly prepared. Board minutes are always important, and it would be sensible for directors to ensure that the minutes identify the relevant considerations for the purpose of section 172 (2). However, where there are board papers, the minutes can often do this by reference to the board papers.

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[18] R. Austin, 'Commentary by Justice RP Austin: Australian Company Law Reform and the UK Companies Bill', in R. Austin (ed), *Company Directors and Corporate Social Responsibility: UK and Australian Perspectives*, 2007, Ross Parsons Centre of Commercial, Corporate, and Taxation Law Monograph Series, at p 9.

[19] Lady Justice M. Arden, 'Companies Act 2006 (UK): A New Approach to Directors' Duties' (2007) 81 *Australian Law Journal* 162 at 168.

Citing early fears of a 'compliance-driven' approach to the exercise of directors' duties rather than one based on making good faith judgments, lawyer Alex Kay foresees the possibility of 'greater pressure on directors, at the least, a bigger procedural burden, leading to lengthier board minutes that seek to evidence that the board has indeed taken the various factors into account'.[20] As indicated in the paper by the co-speaker at the seminar that led to this article, the experience of company directors and those who advise and represent them in UK courts might reflect different experiences, especially at this early stage of the new law's interpretation and application.[21] Developing case law will determine whether courts interpret this new statutory framework for a form of due process in boardroom decision-making in procedural or more substantive ways. In any case, there are a number of hurdles to non-shareholders being able to use these provisions to challenge boardroom decisions or to sue directors.[22]

In the relevant chapter of *Corporate Social Responsibility in the 21st Century: Debates, Models and Practices Across Government, Law and Business*, I try to summarise the potential implications for UK directors' duties as follows:[23]

> A less obvious and yet far more dangerous stalking horse for directors lurks in the shadows of the statutory duties of loyalty and care. Although non-shareholders who are harmed by corporate actions face considerable obstacles ... in seeking to engage courts in sanctioning directors on due process grounds, circumstances can arise in which the statutory framework of decision-making factors points in a direction that bolsters claims by shareholders, liquidators or the company itself against directors. The framework makes explicit the possibility of corporate loss caused by a breach of duty being attributable to failures by directors to act earlier rather than later in addressing significant risks, to place and assess properly all designated matters on the corporate risk radar, to manage and consider all relevant information and drivers relevant to corporate success, and to exercise due care and diligence in doing so.
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> ... This prospect is enhanced by the legitimacy afforded now to non-financial drivers of business success and the different factors that they place on the corporate risk radar, as accepted by the UK Parliament in framing business review and reporting requirements. In other words, directors might face the twin possibilities that section 172 not only imposes a new order of informational and risk assessment for directors, but also makes it easier rather than harder for boardroom failures in complying with the legislatively mandated considerations to be connected in retrospect to a company's financial losses. At the very least, the combined effect of legislatively designating particular factors relating to business success, and then mandating their consideration in boardroom decision-making, affords those who are looking to sue directors with new pegs on which to hang their arguments.

Australian Lessons on Directors' Duties and Shareholder Ratification

What does Australian statutory and non-statutory corporate law have to offer such debates? Even allowing for the growing divide between UK and Australian law generally and each country's corporate legislation in particular, Australian precedent has something to offer on some of these issues and more, for those lawyers, judges, and regulators who keep abreast of Anglo-Australian developments. Some key areas for comparison and contrast in transposing and translating judicial lessons across the two jurisdictions are:

(1) the common underlying Anglo-Australian corporate law rationales of loyalty, proper purposes, care, and corporate best interests, notwithstanding differences in the legislative expressions giving effect to those rationales in directors' duties;
(2) the common background of legislated statements of directors' duties being drawn from equivalent duties under the general law, notwithstanding differences in the use to be made of the principles underlying those equivalent duties;
(3) the common impact of business judgment elements upon the preconditions for judicial determination of a breach of the directorial duty of care, notwithstanding the additional presence of a more extensive statutory business judgment defence in only one of the two jurisdictions;

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[20] A. Kay, 'United Kingdom', Comment, IFLR Supplement, 2006, at p 51.

[21] B. Hubble, 'Directors' Duties and Liabilities: Where Are We Now and Where Are We Going – A Talk by Ben Hubble QC', paper presented at Lloyds in London on 15 November 2010, as part of Four New Square's seminar on *Directors' Duties and Liabilities: Where Are We Now and Where Are We Going?*'.

[22] Horrigan, note 5, at pp 251-255.

[23] Horrigan, note 5, at pp 254-255.

(4) the capacity for directors under the corporate law in each jurisdiction to make decisions in the company's interest by reference to relevant shareholder and non-shareholder considerations, with additional legal force added through their mandatory consideration under UK law;
(5) the limits and preconditions of informed shareholder consent for ratification of boardroom decisions under the general corporate law, as maintained in both jurisdictions; and
(6) the interactions between directors' duties, shareholder ratification, and creditors' interests, both inside and outside insolvency contexts (see further below).

For example, notwithstanding other modifications to the position under general corporate law in the legislated ratification power in section 239 of the UK Companies Act,[24] the outcome in the UK decision, *Franbar Holdings Ltd v Patel* [2008] EWHC 1534, confirms the commonsense (although occasionally commercially inconvenient) result that shareholder ratification must be exercised within some legal limits, which are preserved under the ratification power (see section 239(7)). Similarly, where the formal steps for ratification have not been taken, any residual room for arguing implicit ratification or, alternatively, acquiescence by shareholders would need to accommodate Justice Austin's caveats in the *ASIC v Rich* trial judgment in 2009 that 'great caution needs to be exercised ... where there is not a precise coincidence between shareholders and directors', especially since 'there is no principle of law short of the doctrine of unanimous assent that would allow the informal acquiescence of a majority of shareholders to have the same effect as a formal resolution at a properly convened general meeting'.

The High Court of Australia's decision in *Angas Law Services Pty Ltd (In Liquidation) v Carabelas* [2005] HCA 23 offers some guidance on the meaning of 'the best interests of the company' and how shareholder approval or ratification might bear upon the propriety of what might otherwise amount to a breach of duty. Indeed, in a couple of passages in this High Court decision that repay careful reading for anyone in either country involved in advice or litigation surrounding directors' duties in situations of near or actual insolvency, Justices Bill Gummow and Ken Hayne bring together questions of directors' duties, self-interested ratification by director-shareholders, creditors' interests, and piercing the corporate veil in a remarkably distilled way, as follows:[25]

The starting point must be the general duty of a director to act in the best interests of the company. The best interests of the company will depend on various factors including solvency. In *Kinsela v Russell Kinsela Pty Ltd (In Liq)*, Street CJ said:

> In a solvent company the proprietary interests of the shareholders entitle them as a general body to be regarded as the company when questions of the duty of directors arise. If, as a general body, they authorise or ratify a particular action of the directors, there can be no challenge to the validity of what the directors have done. But where a company is insolvent the interests of the creditors intrude. They become prospectively entitled, through the mechanism of liquidation, to displace the power of the shareholders and directors to deal with the company's assets. It is in a practical sense their assets and not the shareholders' assets that, through the medium of the company, are under the management of the directors pending either liquidation, return to solvency, or the imposition of some alternative administration.

Nothing said in *Macleod v The Queen* suggests the contrary. It was decided in *Macleod* that the "consent" of a single shareholder company could not cure what otherwise would be a breach of s 173 of the Crimes Act 1900 (NSW). Section 173 created an offence where a director or officer of a body corporate fraudulently took or applied any of the property of the body corporate for his own use or benefit, or for any use or purpose other than that of the body corporate. Gleeson CJ, Gummow and Hayne JJ said:

> The self-interested 'consent' of the shareholder, given in furtherance of a crime committed against the company, cannot be said to represent the consent of the company.

In the present case, the mortgage was granted by ALS whilst it was solvent and at a time when there appeared to be no real chance of insolvency … Further, the granting of the mortgage was authorised by the shareholders of ALS. The combination of these two factors, solvency and authorisation, indicates that the standards of propriety expected of the directors was not breached. How might all of this have at least some modelling relevance for the inevitable arguments that will still arise about the scope and limits of shareholder ratification under section 239 of the UK Companies Act 2006?

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[24] S. Graham, 'Directors' Duties: Current Interpretation and Future Reforms', Wragge & Co, September 2009.
[25] [2005] HCA 23 at [67]-[69].

First, as noted in other commentary on this provision, it codifies and modifies the position of shareholder ratification under the general law. Secondly, section 239(7) contains an important qualification: 'This section does not affect any other enactment or rule of law imposing additional requirements for valid ratification or any rule of law as to acts that are incapable of being ratified by the company'. Importantly, this could be the locus of arguments about what directors must do to show that the consent of ratifying shareholders is fully informed, the limits on shareholder ratification in situations of near or actual insolvency under the general or statutory law, the position of conflicted directors, and the practical impact of this course of action in transactional circumstances, such as shareholder ratification of finance and security arrangements in corporate groups whose transactions raise controversial issues of conflicts of interest, disproportional corporate benefit, and other problems. Finally, as these High Court of Australia dicta reveal, shareholder approval can prevent a breach of duty from arising in the first place.

Australian and Canadian Lessons on Directors' Duties and the Interests of Creditors

The ongoing need for consideration of the relationship between directors' duties and creditors' interests under UK corporate law arises because of the terms and reservations of the duty of loyalty in section 172 of the UK Companies Act. In particular, section 172(3) says: 'The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company'. Is there a duty to creditors that they can enforce and are there other ways in which their interests might need consideration by directors too? Such a question also tests the legitimacy and boundaries of shareholder-based accounts of corporations, because of the possible dissonance in such business-threatening circumstances between the best interests of each of the shareholders, creditors, employees, and the corporation as a sustainable business enterprise.

Recent Anglo-Australian law has insights to offer on this level too. In *Spies v The Queen* [2000] HCA 43, relying upon an earlier judgment by Justice Gummow, Justices Gaudron, McHugh, Gummow, and Hayne cut through the confusion in some earlier UK, Australian, and New Zealand cases about duties owed to creditors, in terms that have ongoing relevance in UK corporate law too, especially in light of section 172(3) of the UK Companies Act. This confusion arises whenever there is unnecessary conflation of the question of whether directors directly or indirectly owe creditors any independent and enforceable duty with the question of the conditions under which directors can or must consider the interests of creditors in fulfilling their directors' duties owed to the company. In the words of the majority judgment of the High Court of Australia, a director's duty to consider creditor interests at or near insolvency is still a duty owed to (and enforceable by) the company or those who stand lawfully in its shoes; it is never to be conceptualised in any sense as a duty owed to (and enforceable by) creditors in their own right:[26]

> It is true that there are statements in the authorities, beginning with that of Mason J in *Walker v Wimborne*, which would suggest that ... the appellant, as one of its directors, owed a duty to that company to consider the interests of the creditors and potential creditors of the company in entering into transactions on behalf of the company. *Walker v Wimborne* was an appeal by a liquidator against the dismissal of his misfeasance summons brought against former directors under s 367B of the Companies Act (NSW). Statements in this and other cases came within Professor Sealy's description of:
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>> words of censure directed at conduct which anyway comes within some well-established rule of law, such as the law imposing liability for misfeasance, the expropriation of corporate assets or fraudulent preference.

Hence the view that it is "extremely doubtful" whether Mason J "intended to suggest that directors owe an independent duty directly to creditors." To give some unsecured creditors remedies in an insolvency which are denied to others would undermine the basic principle of pari passu participation by creditors.

In *Re New World Alliance Pty Ltd; Sycotex Pty Ltd v Baseler*, Gummow J pointed out:

> It is clear that the duty to take into account the interests of creditors is merely a restriction on the right of shareholders to ratify breaches of the duty owed to the company. The restriction is similar to that found in cases involving fraud on the minority.

[26] [2000] HCA 43 at [93]-[95].

> Where a company is insolvent or nearing insolvency, the creditors are to be seen as having a direct interest in the company and that interest cannot be overridden by the shareholders. This restriction does not, in the absence of any conferral of such a right by statute, confer upon creditors any general law right against former directors of the company to recover losses suffered by those creditors ... The result is that there is a duty of imperfect obligation owed to creditors, one which the creditors cannot enforce save to the extent that the company acts on its own motion or through a liquidator.

In so far as remarks in *Grove v Flavel* suggest that the directors owe an independent duty to, and enforceable by, the creditors by reason of their position as directors, they are contrary to principle and later authority and do not correctly state the law.

In practice, of course, UK creditors can use other avenues (eg wrongful trading provisions of the UK Insolvency Act) to bring home claims against directors of insolvent companies, rendering much of this discussion academic. Moreover, UK law now has an interesting interplay between the law on directors' duties and defences under the Companies Act, the law on insolvent trading, and the treatment of negligence in corporate contexts under the principles of the Compensation Act.

Still, the High Court of Australia's clinical evisceration of any lingering fuzziness surrounding the idea of directors' duties being owed to creditors as a particular constituency should put that idea to rest, if anyone ever attempts to develop the law in that direction through the avenue technically left open under section 172(3). At the very least, the High Court of Australia's current line of thinking matches and reinforces where UK law has also finally landed on this issue, in terms of the basis of the requirement under the general corporate law for directors to consider creditors' interests at or near insolvency – summarised in *Palmer's Company Law: Annotated Guide* as follows:

> The scope of the common law duty requiring directors to consider the interests of creditors is more controversial. Cases support a variety of propositions but the better accepted view is that a duty is owed by directors to the company (and not to the creditors themselves: *Kuwait Asia Bank EC v National Mutual Life Nominees Ltd* [1991] 1 AC 187 at 217 PC; *Yukong Line Ltd v Rendsburg Investments Corp (No 2)* [1998] 1 WLR 294), and this duty requires directors of insolvent or borderline insolvent companies to have regard to the interests of the company's creditors (*West Mercia Safetyware Ltd v Dodd* [1988] BCLC 250 CA). The duty does not seem to require directors to act to the best advantage of creditors, but merely not to act in a way that would leave the creditors in a worse position than on liquidation (*Weldfab Engineers Ltd, Re* [1990] BCLC 833. Hoffmann J). Although the duty is relatively easy to state, the boundary between acceptable entrepreneurial risk-taking and unacceptable breaches of duties to creditors in the lead up to insolvency is not clear-cut, especially without the benefit of hindsight (*Facia Footwear Ltd v Hinchcliffe* [1998] BCLC 218 at 228).

Nevertheless, there are residual issues here about what the duty to the company requires by way of taking account of creditors' interests in different circumstances, what the duty requires at different points along the trajectory towards insolvency, and what directors must do to avoid harming creditors' interests in light of the options available to them. One of the most recent, detailed, and boundary-pushing discussions of such issues in the Australian context appears in the judgment of Justice Owen – previously head of the HIH Commission of Inquiry – in *The Bell Group Ltd (In Liq) v Westpac Banking Corporation (No 9)* [2008] WASC 239. As this case focused upon the security taken from a financially pressured corporate group as part of a work-out, it contains lessons and arguments for post-GFC litigation on a variety of issues related to boardroom decisions, including questions of corporate benefit in third party corporate security contexts, when the duty to take account of creditors' interests arises and what it means, and both recipient and accessory liability under the rule in *Barnes v Addy*. This long-running Bell Group litigation arose from the 1989-1990 economic downturn, and the judgment raised concerns amongst commercial lawyers about the precise scope of the obligation upon directors to consider creditor interests and for what purposes, as part of their directors' duties when a company nears or arrives at insolvency.[27] Canadian corporate law also contains important insights on these questions.

[27] Allens Arthur Robinson, *Focus: Insolvency & Restructuring – November 2008*, 'The Bell Group Litigation – The Lessons Learned'.

Notwithstanding the possible reading of other Anglo-Commonwealth cases to adjust the duty of directors somewhere towards or at the insolvent end of the corporate lifeline, judicial authority at the highest level in Canada affirms that '(t)he directors' fiduciary duty does not change when a corporation is in the nebulous "viscinity of insolvency"'.[28] Following on from its landmark and explicit recognition in *Peoples Department Stores Inc (Trustee of) v Wise* 2004 SCC 68 (CanLII) that directors' duties are not owed directly to creditors but that directors nevertheless are entitled to take the interests of creditors into account as part of meeting their duties to the company, the Supreme Court of Canada further summarised the general Canadian position on directors' duties and creditors' interests in *BCE Inc v 1976 Debentureholders* 2008 SCC 69 (CanLII) at [38]-[42]as follows:

> The fiduciary duty of the directors to the corporation is a broad, contextual concept. It is not confined to short-term profit or share value. Where the corporation is an ongoing concern, it looks to the long-term interests of the corporation. The content of this duty varies with the situation at hand. At a minimum, it requires the directors to ensure that the corporation meets its statutory obligations. But, depending on the context, there may also be other requirements. In any event, the fiduciary duty owed by directors is mandatory; directors must look to what is in the best interests of the corporation.
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> In *Peoples Department Stores,* this Court found that although directors must consider the best interests of the corporation, it may also be appropriate, although not mandatory, to consider the impact of corporate decisions on shareholders or particular groups of stakeholders. As stated by Major and Deschamps JJ., at para. 42:

We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, *inter alia,* the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment. As will be discussed, cases dealing with claims of oppression have further clarified the content of the fiduciary duty of directors with respect to the range of interests that should be considered in determining what is in the best interests of the corporation, acting fairly and responsibly.

In considering what is in the best interests of the corporation, directors may look to the interests of, *inter alia*, shareholders, employees, creditors, consumers, governments and the environment to inform their decisions. Courts should give appropriate deference to the business judgment of directors who take into account these ancillary interests, as reflected by the business judgment rule. The "business judgment rule" accords deference to a business decision, so long as it lies within a range of reasonable alternatives: see *Maple Leaf Foods Inc. v. Schneider Corp*. 1998 CanLII 5121 (ON C.A.), (1998), 42 O.R. (3d) 177 (C.A.); *Kerr v. Danier Leather Inc.*, 2007 SCC 44 (CanLII), [2007] 3 S.C.R. 331, 2007 SCC 44. It reflects the reality that directors, who are mandated under s. 102(1) of the *CBCA* to manage the corporation's business and affairs, are often better suited to determine what is in the best interests of the corporation. This applies to decisions on stakeholders' interests, as much as other directorial decisions.

Normally only the beneficiary of a fiduciary duty can enforce the duty. In the corporate context, however, this may offer little comfort. The directors who control the corporation are unlikely to bring an action against themselves for breach of their own fiduciary duty. The shareholders cannot act in the stead of the corporation; their only power is the right to oversee the conduct of the directors by way of votes at shareholder assemblies. Other stakeholders may not even have that.

To meet these difficulties, the common law developed a number of special remedies to protect the interests of shareholders and stakeholders of the corporation. These remedies have been affirmed, modified and supplemented by the *CBCA*.

The Canadian Supreme Court's view in the earlier case of *Peoples Department Stores v Wise* arguably supports an 'enterprise value' conception of corporations,[29] in the sense that 'the phrase the "best interests of the corporation" should be read not simply as the "best interests of the shareholders" [because] (f)rom an economic perspective, the "best interests of the corporation" means the maximisation of the value of the corporation'.[30]

[28] *Peoples Department Stores Inc (Trustee of) v Wise* 2004 SCC 68 at [46].

[29] J. Sheahan, 'Directors' Duties in the Zone of Insolvency', T. C. Beirne School of Law Seminar Series, 2009, Brisbane.

[30] 2004 SCC 68 at [42].

These two statements of high-level judicial authority from Canada also have CSR implications, in terms of the correlation between fulfilment of directors' duties and the range of stakeholder interests that might be considered by directors, including 'shareholders, employees, *creditors*, consumers, governments and the environment' (emphasis added).

In short, despite some earlier confusion, Anglo-Commonwealth law seems to be coalescing around the following broad propositions, at least as a matter of general corporate law:

(1) Directors' duties are owed to the company and not to creditors directly;
(2) Directors are entitled to consider creditors' interests in fulfilling their duty to the company, and might be required to do so, depending upon the circumstances;
(3) The general corporate law allows directors some leeway in making their 'business judgments' about the company's best interests, including accommodation where necessary of the interests of creditors in any action or decision taken by the directors;
(4) Given that the consideration of creditors' interests forms part of the directors' duties to the company, such consideration is not necessarily confined to circumstances of actual or impending insolvency; and
(5) Special considerations govern the relation between directors' duties, shareholder interests, and creditor interests in insolvency situations under the general law, such as the inability of shareholder ratification to cure a breach of directors' duties that might prejudice creditors when the company is insolvent.

In light of these propositions, it is possible to crystallise the following propositions about the relation between the directors' duty of loyalty and creditors' interests under section 172 of the UK Companies Act 2006:

(1) To the extent that they are implicit in the listed considerations for directors in section 172 (eg 'the need to foster the company's business relationships with suppliers … and others'), creditors' interests must be taken into account by directors, in fulfilment of their duty to the company;
(2) Section 172(3)'s reference to creditors' interests is broad enough to cover duties owed to creditors and other obligations to take creditors' interests into account under the general law, as well as legislative remedies for creditors under insolvent trading laws;
(3) To the extent that the pre-existing law on directors' duties is not displaced and, further, is used to inform interpretation of the duty of loyalty, directors will still be afforded some discretion for their 'business judgments' under the general law, including appropriate consideration of creditors' interests where necessary, without having courts second-guess their commercial decisions; and
(4) Nothing in the listed considerations for boardroom decision-making, their mandatory nature as considerations for directors, or the express caveat under section 172(3) changes the pre-existing position under Anglo-Commonwealth law that directors' duties are directly owed to the company and nobody else, including creditors.

Australian Lessons on Different Standards for Different Directors

Directors might all be subject to the same directors' duties, but do those duties and their correlative standards apply to all directors in exactly the same way? In a pre-trial determination before final judgment in *ASIC v Rich*, on an application brought by Australia's corporate regulator (ASIC), Justice Austin accepted the legitimacy of the Australian Securities and Investments (ASIC) pleading that board members such as chairpersons could have responsibilities not shared by other directors. This early decision in the long-running *ASIC v Rich* litigation after the collapse of One.Tel initially generated some misplaced concern amongst some quarters of the business and legal communities, who feared it would lead to different judicial and community expectations being placed upon different kinds of directors – chairpersons today, independent directors tomorrow, and so on.

However, a more sanguine assessment of the decision appears in one of the leading modern Australian legal texts on company directors and corporate governance, co-authored by the architect of the *Rich* decision, Justice Bob Austin. In *Company Directors: Principles of Law and Governance*, the learned authors Austin, Ford, and Ramsay say this about the *Rich* decision and its nuances:[31]

> There is a question whether a non-executive director who occupies the position of chairman of the company and chairman of the audit committee is subject to a special standard of care, skill and diligence. This question was explored in *ASIC v Rich* (2003) 44 ACSR 341; 21 ACLC 450.

[31] R. Austin, HAJ Ford, and I. Ramsay, *Company Directors: Principles of Law and Corporate Governance*, 2005, Australia: LexisNexis Butterworths, at pp 248-249.

> ... It can be seen from the alleged special responsibilities that the claim of ASIC related not to the duties of company chairmen generally but to the duties of a company chairman who is also chairman of the audit committee, having regard to the particular circumstances of the company and the person's special qualifications.

What appears in the company's constitution and other formal documents (eg board resolutions) might therefore have some bearing upon the respective responsibilities and roles of different directors and between directors and management, depending upon the particular circumstances and corporate governance arrangements for the company concerned. The *Rich* judgment and subsequent judgments also signal the important role that can be played by authoritative extrinsic material on corporate governance standards in judicial interpretation and application of directors' duties and defences, as follows.

Most significantly for an Anglo-Commonwealth audience, the *Rich* judgment draws upon major UK references on corporate governance and boardroom standards, such as the Higgs Report and the much-cited case, *Re City Equitable Fire Insurance Co* [1925] 1 Ch 407. The judgment in *ASIC v Rich* also bolstered its conclusion that ASIC had a reasonably arguable case for alleging special responsibilities of the One.Tel chairperson by referring to cases in which courts contemplated that board chairpersons might have responsibilities beyond procedural matters at boardroom and company meetings, and evidence that ASIC intended to use in the form of expert evidence from experienced board chairpersons and expert commentaries and standard-setting guidance on corporate governance practice.[32]

Similar reference was made to expert commentary and authoritative regulatory and industry guidance on corporate governance in the landmark subsequent decision on the liability of Centro directors for errors in financial statements and reporting by the company. This was despite the trial judge's acceptance that the directors 'operated under a set of practices and procedures which accorded with good practice' and 'the safety nets [on financial reporting by the company] failed due to no fault of the non-executive directors'.[33] The opposite outcome, in favour of directors faced with non-compliance with relevant accounting standards in the company's financial statements, occurred in the equivalent and recent New Zealand decision in *Ministry of Economic Development v Feeney* (also known as the *Feltex* decision), although under different legislative provisions and corporate circumstances.[34] The outcomes in the Centro case and other recent test cases by ASIC on directors' duties and defences have renewed calls for further reform of Australian corporate law, in light of the presumed gulf between community and regulatory expectations of directors, on one hand, and the realities of managing complex corporate enterprises for directors, on the other.[35] The question in the Australian context is whether the pressure for reform from these directions can be met without also reopening boardroom and regulatory doors to broader CSR-related concerns of the kinds covered in this article.

As corporate governance codes and other standards in each country move towards delineating in greater detail the expected roles and responsibilities of particular board members (eg chairpersons, independent directors, board committee members etc), under the influence of rising judicial, community, and even business expectations of corporate governance and conduct, the risk increases that such material will inform judicial assessments down the track of what is expected of different kinds of board members with different capabilities and responsibilities, all within the same boardroom and fulfilling the same formal legal duties. *ASIC v Rich* is a landmark case in point. In light of the UK's ongoing refinement of its Combined Code to give more attention to various board member roles and responsibilities, as reflected also in the 2009 UK *Review of Corporate Governance in UK Banks and Other Financial Industry Entities*, it is interesting to note the *Rich* judgment's assessment that some of the Higgs recommendations and suggested guidance for directors reinforced the thrust of ASIC's submissions that the One.Tel chairperson had special responsibilities.

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[32] Austin, Ford, and Ramsay, 2005: 249.

[33] *ASIC v Healey (No 2)* [2011] FCA 1003 at [172] and [175] (on penalties); and *ASIC v Healey* [2011] FCA 717 (on liability).

[34] DC AK CRI-2008-004-029199 (2 August 2010).

[35] Eg B. Baxt, 'Is the Time Right to Reform the Law Governing the Duties of Public Company Directors and Non-Executive Directors in Particular?', University of New South Wales Thought Leadership Series, August 2011; and R. Austin, 'Directors' Duties After *James Hardie* and *Centro*', Supreme Court of Victoria Commercial Law Conference, August 2011.

The thrust of these points is reinforced by the eventual trial of such issues, again before Justice Austin, in ASIC's action against One.Tel's joint chief executive officer (Rich) and finance director (Silbermann). Hearings commenced in 2004 and judgment was delivered in late 2009.[36] The judgment by Justice Austin in *ASIC v Rich* [2009] NSWSC 1229 is the first major judicial analysis of the statutory business judgment defence and its application.[37] It has set the markers for subsequent judicial exploration of its many issues, including the equally landmark enforcement proceedings against directors of the James Hardie group, in which the overturning of the trial judge's finding on liability of the directors by the NSW Court of Appeal[38] is on further appeal to the High Court at the time of writing.[39]

In *ASIC v Rich* [2009] NSWSC 1229, ASIC relied solely upon the directorial duty of care and diligence, and the defendants raised the statutory business judgment defence against all claims. In the end, ASIC failed in its action against them, and there is much in the judgment of relevance to the law and practice in both Australia and the UK. For example, the judgment canvasses the following matters:

(1) the interaction between equitable and common law elements in the formulation of directors' duties as enshrined in legislation, including balances between the influence of negligence and fiduciary obligations, as well as the possible but limited application of doctrines such as res ipsa loquitur to the context of directors' duties;
(2) the extent to which responsibilities of directors are shaped not only formally under the corporate constitution and board resolutions, but also 'the factual arrangements operating within the company and affecting the director or officer in question', including 'arrangements flowing from the experience and skills that he or she brings to bear to the office, and also any arrangements within the board or between the person and the executive management affecting the work that the person is expected to carry out';[40]
(3) the minimum standards needed to fulfil the duty of care and diligence;
(4) the scope for implicit ratification or shareholder acquiescence, at least in companies where the correlation between directors and shareholders is complete;
(5) the scope in enforcement proceedings for expert evidence of the roles and responsibilities of managing and finance directors, and the basic standards set by that expert evidence;
(6) the onus of proof in proving the elements of the statutory business judgment defence;
(7) the matters constituting a 'decision' for the purpose of the statutory business judgment defence, excluding the actions of '(m)onitoring the company's affairs and maintaining familiarity with its financial position' but including 'decisions taken in planning, budgeting and forecasting' in the set of matters that are capable of requiring a 'decision to take or not take action';[41]
(8) the factors going to the reasonableness of a director's belief for the purpose of the statutory business judgment defence; and
(9) the 'business judgment considerations' under the general law that condition a court's finding of a breach of duty by preventing judicial second-guessing of the merits of business decisions, above and beyond the additional protection afforded to directors under the statutory business judgment defence, which itself offers extra protection to directors for what would otherwise be a breach of duty.

For UK and Australian comparisons, consider the final item in the list above. Even without a statutory business judgment defence, the pre-existing general corporate law already contains some 'business judgment' considerations that provide some degree of protection to directors from mere judicial disagreement after the event with their commercial decisions at the time, at least in the eyes of the High Court of Australia and the Privy Council (albeit on appeal from Australia, when such avenues of appeal still existed). In the words of the Privy Council in *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821 at 832:

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[36] *ASIC v Rich* [2009] NSWSC 1229.
[37] For a discussion of the case's significance and implications by an Australian law firm partner and published expert on corporate law matters, see: A. Lumsden, 'The Business Judgment Defence: Insights from ASIC v Rich' (2010) 28 *Company and Securities Law Journal* 164.
[38] *Morley v ASIC* [2010] NSWCA 331; see also *James Hardie Industries NV v ASIC* [2010] NSWCA 332.
[39] *ASIC v Hellicar* [2011] HCATrans 293-295 (25 October – 27 October 2011).
[40] *ASIC v Rich* [2009] NSWSC 1229 at [7202].
[41] *ASIC v Rich* [2009] NSWSC 1229 at [7278]-[7280].

'There is no appeal on the merits from management decisions to courts of law: nor will courts of law assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at'. In the words of the High Court of Australia in *Harlowe's Nominees Pty Ltd v Woodside (Lake's Entrance) Oil Co NL* (1968) 121 CLR 483 at 493: 'Directors in whom are vested the right and duty of deciding where the company's interests lie and how they are to be served may be concerned with a wide range of practical considerations, and their judgment, if exercised in good faith and not for irrelevant purposes, is not open to review in the courts'. Both cases are cited in Justice Austin's judgment in *ASIC v Rich* [2009] NSWSC 1229 at [7251].
In terms of the additional protection for directors supplied by the statutory business judgment defence under section 180(2) of the Corporations Act 2001 (Cth), Justice Austin considered that it was 'more than mere window dressing' and distilled its essential elements as follows:[42]

The idea that the business judgment rule does not protect directors and officers from liability for inadequate performance is echoed by some commentary on the Australian s 180(2) ... It seems to me, however, that section 180(2) is capable of providing a defence in some cases that would otherwise involve breach of s 180(1). These are cases where:

- the impugned conduct is a business judgment as defined;
- the directors or officers are acting in good faith, for proper purpose and without any material personal interest in the subject matter;
- they make their decision after informing themselves about the subject matter to the extent they believe to be appropriate having regard to the practicalities listed at 23.9.5.4 [of the judgment];
- their belief about the appropriate extent of information gathering is reasonable in terms of the practicalities of the information gathering exercise (including such matters as the accessibility of information and the time available to collect it);
- they believe that their decision is in the best interests of the corporation; and
- that belief is rational in the sense that it is supported by an arguable chain of reasoning and is not a belief that no reasonable person in their position would hold.

The business judgment rule applicable in Australia is narrower than that which applies in US (especially Delaware) corporate jurisprudence, in the sense that the version of the business judgment rule enshrined in the Corporations Act operates only as a defence to one of the directors' duties (ie the duty of care and diligence). It is supplemented by other rules and principles of general corporate law that allow some margin of appreciation for the commercial judgments of boards and managers. Nevertheless, there has not yet been a successful invocation of the statutory business judgment defence in a reported Australian decision since its inception more than a decade ago,[43] and the political impetus for broadening business judgment defences appears to have slowed for now. Moreover, the expert commentary is not unanimous in its assessment of what the defence adds to the law on directors' duties. In contrast to Justice Austin's view and terminology, for example, a leading Australian member of the commercial bar states that '(t)he business judgment rule arguably offers nothing but window dressing [and] it is somewhat difficult to conceive of a situation in which a director makes a good faith, rational decision for a proper purpose and yet breaches [the duty of care and diligence]'.[44]

CSR Trends and Official Inquiries in the UK and Australia

Official Australian Reaction to UK Approach to Directors' Duties

CSR and directors' duties are connected, to one degree or another. The necessity or permissibility of boards considering or even giving effect to non-shareholder interests is a core way in which the law interacts with CSR.

[42] *ASIC v Rich* [2009] NSWSC 1229 at [7293]-[7295].

[43] Most recently, it was unsuccessfully raised in the corporate regulator's successful appeal against a chairman and chief executive for breach of his director's duty of care and diligence arising out of misleading public statements about concluded commercial contracts and associated continuous disclosure obligations (*ASIC v Fortescue Metals Group Ltd* [2011] FCAFC 19), currently on appeal to and reserved for judgment by the High Court at the time of writing (*Fortescue Metals Group Ltd v ASIC* [2011] HCATrans 271 (29 September 2011).

[44] N. Young QC, 'Has Directors' Liability Gone Too Far or Not Far Enough?: A Review of the Standards of Conduct Required of Directors Under Sections 180-184 of the Corporations Act' (2008) 26 *Companies and Securities Law Journal* 216 at 222.

Both Australia and the UK have entertained major public inquiries into the need for corporate law reform dealing with shareholder and other stakeholder interests. This is of primary importance for the transnational legal regulation of CSR and the emergence of a comparative body of CSR-related law and regulation. Australia has lived through three such major governmental or parliamentary inquiries in the last 25 years, none of which has resulted in much change to corporate law on CSR grounds.

Indeed, Australia's official inquiries into CSR-related corporate law reform reject the need for a provision under Australian corporate law such as the new duty of loyalty under section 172 of the UK Companies Act 2006. Contrary to the UK Corporate Law Review Steering Group's conclusions and the UK Government's agreement on enshrining 'enlightened shareholder value' (ESV) in UK corporate law, Australia's Corporation's and Markets Advisory Committee (CAMAC) foresaw no meaningful improvement to the clarity and application of the law or the quality of boardroom decision-making from prescribing designated decision-making factors by law, such as those under section 172 in the UK:[45]

> The Committee is not persuaded that the elaboration of interests that, where relevant, can already be taken into account would improve the quality of corporate decision-making in any practical way. A non-exhaustive catalogue of interests to be taken into account serves little useful purpose for directors and affords them no guidance on how various interests are to be weighed, prioritised or reconciled.
> Also, the courts, through their interpretation of the law, including the requirement … for directors and others to act in the 'best interest of the company', can assist in aligning corporate behaviour with changing community expectations. Given this, it is unnecessary to amend [the law] along the lines of section 172 of the UK Companies Act and no worthwhile benefit is to be gained.

Global and Transnational CSR Developments

Recent regulatory developments across Anglo-American countries and on the world stage reflect the emerging global significance of the CSR agenda in corporate law and regulation in each country. CSR is now a global force, despite strong residual resistance. Milton Friedman famously warned against it in the 1970s. Recently, The Wall Street Journal published 'The Case Against Corporate Social Responsibility'.[46] Corporate social responsibility is a 'potentially dangerous … illusion' that is either 'irrelevant' or 'ineffective'. While corporations might 'do well by doing good' on occasions, 'the idea that companies have a responsibility to act in the public interest and will profit from doing so is fundamentally flawed'. Striking a balance between corporate profit-making and the common good depends ultimately upon 'government regulation' and monitorial 'watchdog' and 'advocacy' pressure from civil society, with corporate self-regulation playing a subsidiary role. So claims Associate Professor Aneel Karnani from the University of Michigan in his much-publicised recent polemic against CSR in *The Wall Street Journal*.[47]

This is the latest in a decades-long series of landmark writings in the global financial press that attacks CSR. Milton Freedman crystallised the orthodox politico-economic opposition to CSR in his much-cited 1970 article in *The New York Times Magazine*, ' The Social Responsibility of Business is to Increase its Profits'. Most recently, Professor Robert Reich's *Supercapitalism* sounded a similar warning bell against CSR, foreshadowing Karnani's concern that CSR deflects the public and governmental focus on necessary business regulation to improve social welfare and invests misplaced hope in business contributing to that public policy need of its own free will. Even *The Economist'*s landmark concession this decade that CSR has won the battle for our hearts as well as our minds was framed as a grudging concession to the inevitability to CSR's pervasiveness in 21st century business regulation and practice. Is CSR really as bad or flimsy as the latest reaction against it suggests?

The fact that CSR might be undergoing a rapprochement with orthodox corporate governance and responsibility does not deprive CSR of its essential character. Nor should a company's integration of CSR within its strategising, decision-making, and other standard business operations necessarily result in either a hollowing-out of CSR's contribution or its subsumption by the essential business imperatives of corporate profit-maximisation and shareholder wealth-generation.

[45] CAMAC, *The Social Responsibility of Corporations*, 2006, at [3.12].
[46] A. Karnani, 'The Case Against Corporate Social Responsibility, *The Wall Street Journal*, 23 August 2010.
[47] A. Karnani, 'The Case Against Corporate Social Responsibility, *The Wall Street Journal*, 23 August 2010.

The fact that a company behaves as we would expect a company to behave in relation to all matters that affect its business operations, including its approach to CSR, does not mean that a company has suddenly begun to behave like a government on one hand, or a community charity on the other. A parallel can be drawn with courts, who do not suddenly become legislatures or trespass beyond the judicial role simply because they take account of social or policy considerations in appropriate ways within the institutional roles and reasoning processes associated with courts and the body of existing law.

International regulatory developments are also moving towards CSR. The US Securities and Exchange Commission has recently rethought its guidance on shareholder proposals in a way that enhances the prospect of using shareholder proposals to ventilate CSR-related issues.[48] Any UK, Australian, and other non-US companies with operations in the USA and facing possible litigation over their alleged complicity in their own or state-based violations of international customary law are critically affected by a recent US court decision that overturns previous assumptions that corporations are caught by the US Alien Tort Claims Act.[49]

Despite its undoubted benefits, shareholder capitalism's exposed weaknesses generate calls for more sustainable capitalism. Democracy is simultaneously evolving towards greater public accountability for both governmental and corporate uses of power over people's lives. Global business and regulatory conditions are pushing companies to be more economically, socially, and environmentally responsible. The G8 and G20 list CSR-related concerns about responsible lending, sustainable development, and climate change as geopolitical priorities. Mass business adoption of the Global Compact, Global Reporting Initiative, and similar standards swings the pendulum further towards CSR. Good CSR track records give business a seat at the table with government on sustainability issues. Successful businesses are aligning their business models and corporate governance accordingly.

Those in favour of no change to corporate regulation on CSR's account habitually warn against adding to the overall regulatory burden for business or doing anything that is counter-productive to overall social welfare through effective and efficient corporate production of goods and services. Of course, judgments about the efficiency and effectiveness are predicated upon what is counted, what is left out of the equation, and how this changes as society changes in its expectations of corporate governance, responsibility, and sustainability. Nobody on either side of this debate seriously pretends that the law of limited liability established in the late 19th century adequately accommodates all social costs of multinational corporate activity in multiple sites of business operations (eg mass consumer or human rights abuses, long-tail liability for future tort victims, catastrophic environmental damage etc), at least when viewed through 21st century eyes. All sides of the debate simply disagree on the appropriate corrective mechanism and whether it sits inside or outside the core concerns of corporate law. Yet, such evaluations are contingent ones.

In other words, arguments based upon either corporate or social effectiveness and efficiency that might have prevailed 50 years ago or even earlier do not automatically represent the evaluations reached today. No doubt many business leaders, corporate advisers, and even governmental regulators would prefer not to have any change in the law, given how the decks are stacked largely in favour of what they perceive favours shareholder value, but even that perception is not without its faults and limitations.[50] The rush to embrace CSR cannot be marginalised as either a threat to shareholder value or else just good business sense. CSR has evolved beyond PR, philanthropy, and a voluntary business add-on. It has become part of a new order of interdependent governance and regulation involving state and non-state actors, who tackle major social problems together. Businesses, law firms, and universities, for example, are joining governments and civil society in the move towards environmental and other forms of sustainability.

Moreover, CSR has much to say about the institutional and personal roles and ethics of the corporate actors through whom corporations exercise their power and make decisions. Indeed, just as a right of free speech does not properly travel to the point of permitting anyone to yell 'fire!' in a London theatre or 'shark!' on an Australian beach, or allow the freedom of sexual expression to travel beyond its proper domain of sexual activity between rational and consenting adults to its abuse in the sexual corruption of children by adults, so too the exercise of corporate power in the name of shareholder value cannot travel beyond its proper limits.

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[48] See Allens Arthur Robinson, 'Focus: New Guidance on US Shareholder Resolutions', December 2009.

[49] *Kiobel v Royal Dutch Petroleum*, US Court of Appeals for the Second Circuit, 17 September 2010, discussed in Allens Arthur Robinson, 'Focus: Changes to Corporate Liability Under the US Alien Tort Claims Act', September 2010.

[50] Horrigan, note 5, Ch 3.

It is conditioned by a range of societal, regulatory, and organisational influences. Once we move beyond accepting that corporate success is achievable through the floor of the minimum necessary to comply with the law, we begin a journey towards the ceiling of aspirational corporate governance, responsibility, and sustainability. Similarly, once we accept that corporate directors and other actors who are legitimately pursuing the interest of shareholders as a whole are susceptible in some way not only to minimal legal requirements but also to prevailing standards of business ethics, market norms, and even societal trends of a kind that relate to a company and its business, we are immediately in the domain of having to account for the range of considerations that affect corporate and boardroom decisions and how they affect them. In other words, if companies and boards must take account of a range of social, economic, environmental, and other business drivers and risks beyond the minimum that they are required to do under the law, we are in a realm of debate about exactly what kinds of considerations properly bear upon enduring business success, and how.

CSR and the UK Companies Act 2006 – Directors' Duties

Accordingly, the legislative statement of duties in the UK Companies Act can be seen as the latest governmental attempt to relate corporate law to sustainable business profitability for the greater good of society, under conditions in which boards must meaningfully relate a range of organisational, market, environmental, and other societal dynamics to their particular business model, strategy, and operations within the communities in which they do business. The UK Companies Act's adoption of its underlying ESV philosophy enshrines a range of shareholder and other stakeholder interests in directors' duties and business reviews, albeit still grounded in shareholder primacy. Of course, some CSR advocates would still view that outcome as not going far enough in reforming corporate law to sensitise boards to CSR concerns and otherwise providing adequate safeguards and remedies for corporate irresponsibility.

The interaction between directors' duties, CSR concerns, and human rights as part of an integrated approach to corporate governance generally and an aspect of human rights due diligence in particular is a live matter under the UK's newly legislated approach to ESV. In their public report on UK law for the Corporate Law Tools Project under the mandate from the UN Human Rights Council for Harvard's Professor John Ruggie on business and human rights (also see further discussion below), law firm Clifford Chance LLP makes the following connections between directors' duties and human rights:

> *Impact on non-shareholders*
> The text of section 172 of the Companies Act 2006 ... requires directors to 'have regard to' certain issues which affect non-shareholders, including those that have an impact on the community and the environment. *This could presumably encompass human rights issues where they are relevant to the business.*
> Directors are also permitted to consider anything else they consider relevant, although section 172(1) requires them to act in a way that they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. The impact of decisions on members is again key.
>
> *Impact outside the jurisdiction*
>
> There is no express guidance on whether the duty to have regard to the company's impact on the community is understood to encompass communities outside the UK, although there would appear to be no reason why it could not, and every reason why it might do so if the company's relevant operations were situated out of the UK and overseas communities were those primarily affected by those operations. Even if 'community' is intended to be more narrowly defined, the directors are still required to have regard to 'the desirability of the company maintaining a reputation for high standards of business conduct' which would include all of its operations.
>
> The same is the case for impacts by subsidiaries, suppliers and other business partners. The activities of all of these people and organisations have a potential impact on the reputation of the company, and can certainly be considered by directors. (emphasis added)

Doubtless, there would be some corporate lawyers, barristers, and judges in Australia and elsewhere who would be surprised by this signalled convergence of corporate and human rights considerations in the law of directors' duties. This trend sits within a broader trend of convergence between CSR and at least some aspects of corporate governance under international and domestic legal orders.

CSR and the UK Companies Act 2006 – Business Review Reporting

In any case, integrated corporate governance reporting systems for the purpose of UK business review requirements under section 417 of the Companies Act leave adequate room for the incorporation of reporting on human rights due diligence too, as part of overall corporate reporting. For reference here, section 417 of the UK Companies Act 2006 says:

417. Contents of directors' report: business review

(1) Unless the company is subject to the small companies’ regime, the directors' report must contain a business review.

(2) The purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company).

(3) The business review must contain—

(a) a fair review of the company's business, and

(b) a description of the principal risks and uncertainties facing the company.

(4) The review required is a balanced and comprehensive analysis of—

(a) the development and performance of the company's business during the financial year, and

(b) the position of the company's business at the end of that year, consistent with the size and complexity of the business.

(5) In the case of a quoted company the business review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—

(a) the main trends and factors likely to affect the future development, performance and position of the company's business; and

(b) information about—

(i) environmental matters (including the impact of the company's business on the environment),

(ii) the company's employees, and

(iii) social and community issues,

including information about any policies of the company in relation to those matters and the effectiveness of those policies; and

(c) subject to subsection (11), information about persons with whom the company has contractual or other arrangements which are essential to the business of the company.

If the review does not contain information of each kind mentioned in paragraphs (b)(i), (ii) and (iii) and (c), it must state which of those kinds of information it does not contain.

(6) The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—

(a) analysis using financial key performance indicators, and

(b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.

“Key performance indicators” means factors by reference to which the development, performance or position of the company's business can be measured effectively.

(7) Where a company qualifies as medium-sized in relation to a financial year (see sections 465 to 467), the directors' report for the year need not comply with the requirements of subsection (6) so far as they relate to non-financial information.

(8) The review must, where appropriate, include references to, and additional explanations of, amounts included in the company's annual accounts.

(9) In relation to a group directors' report this section has effect as if the references to the company were references to the undertakings included in the consolidation.

(10) Nothing in this section requires the disclosure of information about impending developments or matters in the course of negotiation if the disclosure would, in the opinion of the directors, be seriously prejudicial to the interests of the company.

(11) Nothing in subsection (5)(c) requires the disclosure of information about a person if the disclosure would, in the opinion of the directors, be seriously prejudicial to that person and contrary to the public interest.

In light of these business review requirements, human rights matters arguably are at least included under the umbrella of 'information about: (i) environmental matters (including the impact of the company's business on the environment); (ii) the company's employees; and (iii) social and community issues. This includes information about any policies of the company in relation to those matters and the effectiveness of those policies' (section 417(5)(b)), as well as 'information about persons with whom the company has contractual or other arrangements which are essential to the business of the company' (section 417(5)(c)). The link back to directors' duties is provided by section 417(2), which states that '(t)he purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company)'.

The UK Government and the Ruggie Mandate on Business and Human Rights

The mandate from the UN Human Rights Council for the UN Secretary-General's Special Representative on Business and Human Rights, Professor John Ruggie from Harvard University, affects the UK, Australia, and other UN member nations, and might yet have an impact on public policy and law governing corporations. By mid-2011, the work of the UN mandate had already produced a three-pronged 'protect, respect and remedy' framework for business and human rights, with correlative implications for governments, corporations, and institutional architecture. Under the global Corporate Law Tools project, the mandate also produced a comprehensive review of the extent to which corporate, securities, and related laws in many countries promote or impede business respect for human rights. These interim outcomes of Professor Ruggie's mandate stimulated a legislative resolution in the Australian Senate, road-testing of the three-pronged framework by UK and other business networks, comment and recommendations by the UK Parliament's Joint Committee on Human Rights,[51] and a push in his formal reports towards the importance of human rights due diligence on the ground.

In one of the consultation documents produced under his mandate to set up his final recommendations to the UN Human Rights Council in 2011, Professor Ruggie and his team identify, amongst the key issues for the business responsibility to respect human rights, the following issues surrounding human rights due diligence by companies:[52]

- **Assessing** actual or potential adverse human rights impacts on an ongoing basis, drawing on internal or external expert resources; involving meaningful engagement with relevant stakeholders as appropriate to the size of the business enterprise and the nature and context of its activities.
- **Integrating** the findings from their assessments across internal functions and processes to enable appropriate action, including by clarifying internal accountabilities and aligning personnel incentive structures.
- **Tracking** performance to know whether human rights risks are being effectively addressed, based on appropriate qualitative and quantitative metrics, drawing on feedback from both internal and external stakeholders, and supporting continuous improvement processes.
- **Communicating** performance on human rights in response to stakeholder concerns, including reporting formally as appropriate, taking into account any risks posed to stakeholders themselves, company personnel or to the legitimate requirements of commercial confidentiality.

All that needs to be noted in passing here is that this shows how human rights due diligence can already become a corporate governance issue, whether any new laws come into effect as a result of this UN mandate or not. Recent reporting commissioned by the UK Government about UK corporate attitudes on the ground to human rights issues reveals varied understanding of the issues and drivers amongst UK companies of different kinds and sizes, and a strong and unsurprising business call for 'no new law' in this area.[53]

The UK Brown Government's 2010 response to the report of the UK Joint Committee gives a flavour of the potentially significant directions in which the business and human rights agenda is heading, in the UK and elsewhere, under the impetus of Professor Ruggie's UN mandate:[54]

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[51] UK Joint Committee on Human Rights, *Any of Our Business? Human Rights and the UK Private Sector*, December 2009.

[52] UNSRSG, 'Mandate Consultation Outline, October 2010.

[53] TwentyFifty Limited, *The Private Sector and Human Rights in the UK*, Report for the Ministry of Justice and the Department of Health, October 2009.

[54] UK Government, *Any of Our Business? Human Rights and the UK Private Sector: Government Response to the Committee's First Report of Session 2009-10*, February 2010.

> As a consequence of work undertaken by the UN Special Representative on Business and Human Rights, for the first time there is agreement on a framework developed by him, and he is in the process of elaborating guidance on its implementation ... The Government supports all three pillars of Professor Ruggie's framework and is keen to encourage and participate in constructive dialogue around how best to operationalise the framework ... At the same time the Committee has recognised the need for coherence in the approach of different countries. The Government believes that this will be achieved best by allowing the Special Representative time to inform and shape the international community's approach as he operationalises his Protect, Respect and Remedy framework.

Cynics might argue that this response is high on rhetorical support and low on promised action. It is certainly far from signalling a new wave of corporate legal and regulatory reform. Its emphasis elsewhere on governmental initiatives 'to strengthen voluntary regimes, raise awareness and encourage wider use of tools such as the OECD Guidelines, and to support the UN Special Representative' highlights 'light touch' measures in favour of enlightened self-regulation, at the expense of new mandatory regulation on business and human rights, at least at this stage. Still, regulating business and human rights now requires a wide range of regulatory mechanisms involving state and non-state actors, and it is hard to imagine meaningful progress on this front without developing the international consensus and architecture for implementation flagged in the UK Government's response, especially in then light of Professor Ruggie's final report to the UN in mid-2011.

In that final report, Professor Ruggie secured unanimous UN Human Rights Council endorsement for a set of guiding principles to implement the three-pronged 'protect, respect, and remedy' framework for business and human rights. Human rights due diligence and impact assessments figure in numerous principles, as part of an overarching approach to the integration of human rights considerations within standard business systems and operations. The implementation process from here involves the take-up of these tools by government and business alike, through 'vertical' alignment of international and national laws and standards as well as 'horizontal' alignment of the Ruggie outcomes with other international standards of relevance to business (such as the UN Global Compact, OECD Guidelines for Multinational Enterprises, and the World Bank IFC standards).

Conclusion

For present purposes, the point to be made is that there is an emerging connection between the matrix of decision-making concerns for directors under relevant corporate laws, their correlative legal duties and defences and their associated due diligence safeguards, and the standards on human rights and business from such sources. Indeed, the country-by-country reports on corporate law and human rights that were produced as part of the Ruggie mandate's Corporate Law Tools project reflect strongly the view that, while compliance with internationally recognised human rights is neither a mandatory requirement nor a characteristic feature of corporate law in most countries, there is a variety of due diligence contexts under various national laws in which human rights due diligence is a necessary or desirable element.

As indicated in the report on the Australian legal position, for example, these human rights contexts for due diligence by business include conformance with rights-based legislation (eg non-discrimination, equal opportunity, privacy, and workplace health and safety laws), human rights impact assessments as part of business cases for securing public approvals and licences, satisfaction of socially and environmentally relevant considerations in investment decision-making, corporate governance requirements for corporate governance reporting and compliance with directors' duties and defences.[55] Whatever the path for business and human rights from here, the ongoing practice and reform of directors' duties and defences in a number of countries is increasingly intermingled with a range of CSR-related concerns and standards, many of which have only been developed in the first decade of the 21st century. On the evidence of the international and cross-jurisdictional developments canvassed in this article, there is reason to expect that the way ahead for business success increasingly lies on the path towards integration of conventional corporate governance concerns about board responsibilities and shareholder interests with an emerging range of concerns and tools for CSR, human rights due diligence, and related aspects of enhanced corporate responsibility and sustainability.

[55] The author is a consultant to the law firm that produced this report and also had some involvement in it.