THE LIABILITIES OF THE INATTENTIVE COMPANY OFFICER

L.A. WARNICK*

Introduction

Conventional wisdom has it that the liabilities of company directors are onerous, even oppressive. Is this true? Is the inattentive company officer really at such a high degree of risk?

The answer is clear: no and yes and maybe. No, because the statutory and common law duties of care and diligence have been paper tigers so far. Yes, because there are some potentially onerous statutory liabilities lurking in wait for the inattentive director or manager. Maybe, because the statutory liabilities are only a threat if they are enforced; and the level of enforcement activity can range from zeal to zero.

The Duty of Care

Superficially, it's easy to advise a director, manager, receiver or liquidator on the risks he faces if he takes his eye off the ball. There is no need to look further than section 229(2) of the *Companies Code*, which says:

> An officer of a corporation shall at all times exercise a reasonable degree of care and diligence in the exercise of his powers and the discharge of his duties.

But it's one thing to say that, and another to know what it means. This is not an acute problem when giving prophylactic advice to directors or managers, because in that situation one will always err on the side of caution and state the duty at its highest. But it does become an acute problem when advising a shareholder or receiver or liquidator, who comes in wanting to sue directors or other officers

* B A , LL B (Hons) (A N.U), LL M (Melb)

because they have blundered and cost the company some money. How does one assess the chances of suing inattentive company officers successfully?

There have been no reported cases on section 229(2) in the six years since the Code came in; so despite the best intentions of the legislators in providing a simple formulation of the duty in the Code, the legal adviser must still form his own view as to what a reasonable degree of care and diligence is. In attempting to formulate advice to clients lawyers are inevitably drawn to two sources:

- the common law and statutory antecedents of section 229; and
- policy or what a Court can be persuaded to accept as the standard of care that should apply.

The classic statement of the common law duty is in the judgment of Romer, J., in *Re City Equitable Fire Insurance Co.*[1] That, incidentally, was a misfeasance action under a predecessor of section 542 of the Code, of which more will be said later. Romer, J., was wrestling with issues which are only too familiar today. A large insurance company with a good trading record went into liquidation because the managing director misappropriated large sums of money. The liquidator took out a misfeasance summons against the non executive directors and the auditors. Romer, J., held that no general case of misconduct or negligence had been made out against the directors or auditors. However, they had in certain particulars failed in their full duty to the company; but they were exonerated from liability for these breaches by a provision in the company's Articles (which would now be void under section 237 of the Code).

Romer, J., said:

> In discharging the duties of his position thus ascertained a director must, of course, act honestly; but he must also exercise some degree of both skill and diligence. To the question of what is the particular degree of skill and diligence required of him, the authorities do not, I think, give any very clear answer. It has been laid down that so long as a director acts honestly he cannot be made responsible in damages unless guilty of gross or culpable negligence in a business sense.
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> If, therefore, a director is only liable for gross or culpable negligence, this means that he does not owe a duty to his company, to take all possible care. It is some degree of care less than that. The care that he is bound to take has been described as "reasonable care" to be measured by the care an ordinary man might be expected to take in the circumstances on his own behalf.

1 [1925] 1 Ch 407.

> There are, in addition, one or two other general propositions that seem to be warranted by the reported cases: (1) A director need not exhibit in the performance of his duties a greater degree of skill than may reasonably be expected from a person of his knowledge and experience. A director of a life insurance company, for instance, does not guarantee that he has the skill of an actuary or of a physician. In the words of Lindley, M.R.: "If directors act within their powers, if they act with such care as is reasonably to be expected from them, having regard to their knowledge and experience, and if they act honestly for the benefit of the company they represent, they discharge both their equitable as well as their legal duty to the company": see *Lagunas Nitrate Co. v. Lagunas Syndicate* ([1899] 2 Ch. 392, 435). It is perhaps only another way of stating the same proposition to say that directors are not liable for mere errors of judgment. (2) A director is not bound to give continuous attention to the affairs of his company. His duties are of an intermittent nature to be performed at periodical board meetings, and at meetings of any committee of the board upon which he happens to be placed. He is not, however, bound to attend all such meetings, though he ought to attend whenever, in the circumstances, he is reasonably able to do so. (3) In respect of all duties that, having regard to the exigencies of business, and the articles of association, may properly be left to some other official, a director is, in the absence of grounds for suspicion, justified in trusting that official to perform such duties honestly.[2]

How much further forward does this take us? The basic test is still very nebulous: a director is liable only for "gross negligence", and the standard of care is to be measured by the care an ordinary man takes on his own behalf. Perhaps what is meant is the standard of care an ordinary man takes in the practice of his own profession.[3] This overlaps with the first of the "other general propositions" cited by Romer, J.: the degree of skill a director is expected to show depends on his knowledge and experience. So it is a subjective test. There's no such thing as a model director, the average man travelling in a limousine to the up market equivalent of Clapham. Each director must be considered against the background of his own skill and experience; but in determining what should reasonably be expected from that man, one uses an objective standard. Romer, J., sums up with one proposition that everyone agrees with: directors are not liable for mere errors of judgment.

This "business judgment" rule features prominently in the

2. Ibid., 427-429
3 Solicitors in particular are notorious for their lack of attention to their own affairs If they are anything to go by, the duty will in many cases be all but non existent.

American cases in this area[4] and it has authoritative support in Australia as well.[5] What's more, it makes good business sense: commerce would grind to a halt if the Courts could second guess every decision of the directors or management. This writer's theory is that at least six out of ten business decisions are wrong to some degree, and another three are right for the wrong reasons. But that's business: after all, directors are only human. The art of business survival is turning a decision that's at least half wrong into a result that's at least half right, and the Courts have no role to play in this.

The other two "general propositions" cited by Romer, J., fairly summarize the previous authorities, and they indicate how low the Courts' expectations of directors were. The second proposition was about diligence: directors were not bound to attend meetings. Romer, J., did not mention the high water mark of this non duty, *The Marquis of Bute's Case.*[6] There the Marquis, who had inherited the office of president of a bank at the ripe old age of six months, attended one board meeting in 38 years. He was held not to be liable for breach of duty.[7]

The third proposition referred to by Romer, J., was about delegation. This was an important issue in the *City Equitable* case, and it is even more important today because it's so common for non executive directors to rely on what they're told by executive directors or management. The leading case was *Dovey v. Corey*, where Lord Davey had said:

> I think the respondent was bound to give his attention to and exercise his judgment as a man of business on the matters which were brought before the board at the meetings he attended, and it is not proved that he did not do so. But I think he was entitled to rely upon the judgment, information and advice of the chairman and general manager, as to whose integrity, skill and competence he had no reason for suspicion.[8]

His Lordship went on to agree with statements in earlier cases that directors were not obliged to examine entries in the books of the company to form their own opinion on the conduct of its affairs.

4 For detailed discussion of the business judgment rule as applied in the United States, see 18B Am Jur 2d 547-561

5 See *Harlowe's Nominees Pty Ltd v Woodside (Lake's Entrance) Oil Company N L* (1968), 121 C L R 483 at 493, *Howard Smith Ltd v Ampol Petroleum Ltd*, [1974] A C 821 at 832

6 [1892] 2 Ch 100

7 See also *In re Denham and Company* (1884), 25 Ch D 752, where a director was not held liable for co directors' fraud despite four years of non attendance at directors' meetings

8 [1901] A C 477 at 492

English and Australian cases in this area since *City Equitable* have been few and far between. Two reasons for this can be identified. The first is that the common law standard is highly flexible and allows the Courts to set the standard of acceptable conduct wherever they see fit. In the early cases they did not set it very high, so it was difficult to be confident in advising a potential plaintiff to take action. The second is that the range of potential plaintiffs was so limited. The 1956 English case *Pavlides v. Jensen*[9] provides a good example. Directors of a company sold a mine for £182,000 when its true value was about £1,000,000. The directors, when sued for breach of their common law duty of care by a minority shareholder, took the preliminary point that the plaintiff was not competent to bring the action. They relied on the rule in *Foss v. Harbottle*[10] which, it will be recalled, states that directors' duties are owed to the company and the decision whether to sue for a breach is a matter of internal management with which a Court will not interfere. Danckwerts, J., upheld the directors' argument. He found that none of the recognized exceptions to the rule in *Foss v. Harbottle* were applicable in the absence of a plea of fraud.

The rule in *Foss v. Harbottle*, as applied in *Pavlides v. Jensen*, effectively blocked action by shareholders as a means of enforcing directors' duties of care and contributed to the paucity of authority on the scope of the duty. Contrast this situation with the relatively rich vein of authority on the business judgment rule in the United States, where stockholders are able to bring an action on behalf of the corporation if the directors refuse to sue or are themselves the potential defendants.[11]

So for many years, the principles stated in *City Equitable* remained unchallenged and unexplained. By the late 50's, however, the increasing sophistication of the business world began to generate some discomfort about the nebulous nature of directors' duties of care. In 1958, Victoria took a tentative step toward reform in its new *Companies Act*. Section 107 provided: "A director shall at all times act honestly and with reasonable diligence in the discharge of the duties of his office".

9 [1956] Ch 565
10 (1843) 2 Hare 461, 67 E R 189
11 See 18B Am Jur 2d 675

Failure to comply with the section was an offence with a maximum penalty of £500, and also made the offending director liable to compensate the company for any loss suffered by it. The same provision was adopted in the *Uniform Companies Acts* of 1961, as section 124.

In fact, section 124 did not advance matters a great deal. The "reasonable diligence" standard was not significantly easier to identify or apply than the existing common law duty, with which it substantially overlapped. There were few reported cases on the "diligence" aspect of the section. No doubt difficulties of enforcement were again largely to blame; and, although enforcement actions could now be brought by the Corporate Affairs authorities, their occasional attempts met with little success.[12]

A snapshot of changing legal attitudes to directors' duties is provided by a paper delivered by Sir Douglas Menzies, then a Justice of the High Court, at the Eleventh Legal Convention of the Law Council of Australia, held in Perth in 1959. Sir Douglas referred at some length to the *City Equitable* case, then said:

> Romer, J., in the passage quoted,said that the director of a life insurance company does not guarantee that he has the skill of an actuary or of a physician: this is clearly still the case, nor is it necessary that such a person should have mastered in detail all the provisions of a Commonwealth Life Insurance Act; but of such a director it can properly be demanded that he should have or obtain at least a general understanding of the business of life assurance, that he should know or learn something about the investment of large sums of money in a changing economy, that he should concern himself with important staff problems and that he should bring an informed and independent judgment to bear upon the various matters that come to the board for decision. Any life insurance company appointing a director would expect all this of him; any person accepting office as director would expect to do as much and ... what is expected is the best indication of the content of the duty of care that rests upon an office holder.[13]

Nearly thirty years later, this remains a valuable observation on the standards which should apply to non executive directors; but unfortunately there is no judicial authority to back it up.

When the *Companies Code* was being drafted, dissatisfaction with

12 See *Byrne v Baker*, [1964] V.R. 443. Besides being an example of an unsuccessful prosecution under *U C A* section 124, this case is authority for the proposition that an information under section 124 (and now under section 229(2) of the Code) must specify the particular acts relied upon as the foundation of the charge: a "general characterisation of the conduct of a director over a specified period" is not enough

13 *Company Directors* (1959), 33 A L J 156 at 164

the nebulous common law standard and the limited scope of U.C.A. section 124 gave rise to a proposal to extend the statutory duty beyond diligence to care and skill as well. It was also proposed to impose the duty on all company officers,not just directors; and the penalty for failure to meet the required standard was to be not only a fine, but a jail term.

Two aspects of this proposal generated so much controversy that they were dropped. One was the duty to act with skill; the other was the introduction of jail terms as a penalty for breach. The protests were based on the same policy argument that led to the establishment of lenient standards in the early days of the joint stock company: that the imposition of stringent standards and sanctions would make it impossible to persuade anyone to take on the job.

What emerged from all this was section 229(2) as we now know it: a statutory duty to exercise a "reasonable degree of care and diligence", extending to all company officers and backed by a maximum penalty of $5,000. Potentially more significant sanctions are contained in sub sections (6) and (7) of section 229. Section 229(6) says that where a person is convicted of an offence under section 229, the Court convicting him may (as well as imposing a penalty) order him to pay compensation to the corporation. Section 229(7) goes further. It says that where section 229 has been breached, the company can sue the defaulting officer. The measure of damages is expressed in terms of:

> any profit made by the defaulting officer or any other person as a result of the breach; and
>
> any loss or damage suffered by the corporation.

It is interesting that the amount of compensation recoverable is expressed as any profit made by any person and any loss suffered by the company. The C.C.H. commentary suggests that, "The possibility of double damages makes the statutory remedy more valuable to the corporation than the common law action for damages (which is preserved by section 229(10))...."[14]

However, whether there really is a potential liability for double damages is questionable. On the "net loss or damage" approach applied by Young, J., of the Supreme Court of New South Wales in

14 C.C.H *Australian Company Law and Practice* Vol. 1 para 25 790.

Ross McConnell Kitchen & Co. Pty. Limited (in liq.) v. Ross & Ors[15] it would seem reasonable to argue that the net loss suffered by the company should be calculated after taking into account the amount of any profit recovered from the defaulting officer. The explanatory memorandum on the Code does not deal with the issue, but it appears to support the "net loss" view inasmuch as it describes the measure of damages as "an amount equal to the profit made by that person or the loss suffered by the corporation".

The first *Ross McConnell Kitchen* case is also of interest for its discussion of the principles of causation under section 229(7). Young, J., makes the point that the section uses the words "a result", not "the result", "so that if the officer's conduct was a cause of the loss even though no loss may have occurred but for some other person's conduct, there will still be a liability...."[16]

Another point on causation is made in the C.C.H. commentary: where a director's lack of diligence consists of failure to attend a meeting, it may be difficult to prove that "the corporation suffered loss... as a result of the... failure..." in terms of section 229. If so, the common law remedy may be more effective than section 229 in this situation.[17]

The only plaintiff with standing to sue under section 229(7) is the company. At first glance, it looks as though the right to enforce the duty under section 229(2) is no wider than at common law. But there are two other sections of the Code which may permit an individual shareholder to bring an action. The first is section 574, which permits "any person whose interests have been, are or would be affected" by conduct amounting to a contravention of the Code to get an injunction restraining the contravention. Tacked on the end of section 574 is sub section (8), which says that where a Court has power under the section to grant an injunction, it can award damages as well or instead. This seems to mean that where any contravention of the Code (such as a breach of section 229(2)) has occurred, any person whose interests are affected (presumably including a shareholder) can ask the Court to award damages to whoever has suffered loss (usually only the company).

15 (1985), 3 A.C.L.C. 326, (1985), 1 N.S.W.L.R. 238
16 Ibid., 330.
17 C.C.H. op.cit. Vol. 1 para. 25 790

For a provision hailed on its introduction as having the potential to "revolutionise the settlement of contentious issues arising out of the *Companies Act* ... for the rest of the century"[18] section 574 has had surprisingly little use by private plaintiffs so far. BHP used it against Bell Resources[19] and there has been one case in Western Australia, heard by Master Seaman, Q.C. (as he then was) on an interlocutory application (*Eastern Petroleum Australia Ltd. v. Horseshoe Lights Gold Pty. Ltd.*[20]). The defendants in *Eastern Petroleum* attacked the statement of claim on the basis that the contract which was supposed to be a breach of the Code had already been concluded, with the result that it was too late to grant an injunction and section 574 could not apply. Master Seaman dealt with the issue very briefly by pointing out that the contract had not been fully performed, and in these circumstances it was open to argue that section 574 could operate. He said: "It contemplates a past engagement in conduct which constituted a contravention of the Code and the Court has wide powers to require the person engaging in that conduct to do any act or thing."[21]

But what is the situation where a breach, say a negligent act by an officer, has occurred and caused damage to the company, but is not continuing? Can section 574 apply? There must at least be doubt about the application of section 574(8) in those circumstances, because there is no continuing conduct which could be restrained. On the other hand, the Court still has power to "require a person to do a particular act or thing", so arguably the power to order payment of damages under section 574(8) still exists.

Doubts like this about the ambit of section 574 are one reason why it has been used so little. Perhaps the reason is that potential plaintiffs' lawyers are wary of section 574, especially sub section (8), because it seems too good to be true. At face value it gives a shareholder standing to bring an action which under another section of the Code is restricted to the company. Even though damages could probably only be recovered for the company rather than the shareholders, lawyers seem to have an instinctive suspicion that Courts may bend over

18 A B Greenwood (then an N.C SC Commissioner), in a paper presented on 16 November 1981 and quoted by C C H. op cit Vol 2 para 71 450

19 *Broken Hill Proprietary Company Limited v Bell Resources Limited* (1984), 2 A C L C 157

20 *Eastern Petroleum Australia Ltd & Anor v Horseshoe Lights Lights Gold Pty Ltd & Ors* (1985), 3 A C L C 594.

21 Ibid , 599

backwards to construe the section so that it does not have this result. One way they could do this would be to put a narrow interpretation on "person whose interests are affected". In a negligence situation, this could conceivably be restricted to the company itself as distinct from individual shareholders. A similarly restrictive approach was taken by Olney, J., of the Supreme Court of Western Australia, when construing the words "person aggrieved" in section 42 of the *Securities Industry Code* in *Robox Nominees Pty Ltd v. Bell Resources Ltd.*[22] Western Australian judges have not taken a favourable view of attempts by shareholders with more or less nominal shareholdings to enforce rights under the Codes. In the *Robox* case Olney, J., said: "I do not take the view that a shareholder is inevitably a policeman for the enforcement of the statute law...."[23] It may be argued that at a time when the resources of enforcement authorities are so chronically limited, public policy would be better served by a broad interpretation of shareholders' rights than by a narrow one.

Perhaps a more significant reason why section 574 has had little use by shareholders is that it takes an altruistic plaintiff to put his own money at risk to recover damages for the company. There is no provision for the company to give an indemnity for costs. If a shareholder wins, he still has to pay the excess of solicitor and client over party and party costs, while the damages flow to the company. If he loses, he will be up for the other side's costs as well as his own. Is it any wonder that minority shareholder actions are rare?

The position is slightly better under the alternative avenue a shareholder can use to sue negligent officers: section 320 of the Code. Section 320 gives the Court power to make a wide range of orders where (*inter alia*) the way a company's affairs are being conducted, or a particular act or omission by or on behalf of the company, is contrary to the interests of the members as a whole.

One of the orders the Court can make is that the company should institute legal proceedings, or that a particular member should be authorized to institute proceedings in the name and on behalf of the

22. *Robox Nominees Pty Ltd & Anor v Bell Resources Limited & Ors* (1986), 4 A.C.L.C. 164. But contrast the approach of Kirby, P. of the New South Wales Court of Appeal in *FAI Insurances Ltd v Pioneer Concrete Services Ltd* (1986), 4 A.C.L.C 698 at 707, where his Honour described section 42 of the *Securities Industry Code* as a "beneficial, protective provision" which "should not be given a narrow construction"

23 (1986), 4 A C L.C 164 at 165

company (and presumably at its cost). In a shareholder's action based on the negligence of an officer, the objective would be to get authority from the Court to bring proceedings against the negligent officer, on the company's behalf and at its cost.

There is no reported case where this has happened. The reasons are familiar. Even if he succeeds, the shareholder will have to pay some costs; and if he loses, he will be up for the company's costs as well as his own. This could be a crippling financial blow if the trial lasts a week or more, as can easily happen. Couple this with the fact that no lawyer can tell a potential plaintiff exactly what the standard of duty is, and it's not surprising that one doesn't see more shareholder actions against negligent directors.

Two propositions emerge from all this:

first, directors and officers of a company do owe a duty of care and diligence to the company, but it is uncertain what the requisite standards of care and diligence are; and

secondly, inattentive directors have little to fear from their shareholders: their real exposure to liability arises only if their blunders are severe enough to put the company into receivership or liquidation, and then at the hands of the receiver or liquidator or (possibly) the Corporate Affairs authorities. They may also be at risk when control of the company changes and the new controllers decide to take action against former directors and management; but these actions too are almost unknown in practice, principally because the new owners usually want to get on with business rather than spending money on litigation when standards are so uncertain and the defendants may at the end of the day have no money.

If the authorities and statutes don't make it clear what the boundaries of liability are, we can only ask: in what circumstances should an inattentive company officer be liable? The question immediately splits into two parts: there must be one standard for the non-executive director, and another for the officer who is an employee with executive functions. This difference was recognized even in the early cases, but the position of executive directors received little attention because in those days they were a comparative rarity. It was recognized, however, that executives were subject to a stricter standard. Pennington cites the judgment of Neville, J., in the 1911 case *Re Brazilian*

Rubber Plantations and Estates Ltd.[24] in support of his observation that:

> Such directors will usually be specialists in their own field, be it accountancy, engineering, marketing, finance or anything else, and they will be expected to exhibit the skill and care of a competent practitioner in that field when handling the company's affairs.[25]

As Ford points out[26], it will be an implied term of an executive director's contract of service that he or she should exercise the care and skill reasonably associated with a person in that position. As full time employees these people will also be subject to a higher standard of diligence; executive directors, for example, could scarcely expect to escape liability for repeated failure to attend Board meetings.

If the standard of care and diligence for executive directors is comparatively high, and this has been established since the turn of the century, why haven't there been more actions against negligent executive directors? That the elevation of executives other than the managing director to Board level is a comparatively recent phenomenon is only part of the answer. Companies simply do not sue negligent executives: they fire them, demote them or kick them upstairs, but they don't sue them. So far, it remains an empirically sound proposition that, where the company is not in receivership or liquidation, section 229(2) is not in practice a serious threat to executive directors. It seems safe to suggest that it never will be, unless the barriers to shareholder action are removed. Even for a liquidator, a legal action against a negligent employee is seldom likely to yield a large enough or certain enough return to make it worthwhile.

For non executive directors, it is to be hoped that the change in business conditions since 1925 will prompt the Courts, if and when an action against an inattentive officer finally does come before them, to turn the *City Equitable*/ section 229 duty from a paper tiger into one that has some teeth. The statement of Sir Douglas Menzies, made in 1959 and quoted above, deserves some attention when a modern standard is being formulated. So too does the recent American case *Smith v. Van Gorkom.*[27] There, directors were held to have breached their duties when they approved a merger proposal after two hours'

24 [1911] 1 Ch 425

25 R R Pennington, *Company Law*, 5th ed (1985), 678

26 H A J Ford, *Principles of Company Law*, 4th ed (1986), 419, citing *Lister v Romford Ice and Cold Storage Co*, [1957] A C 555

27 Del Supr, 488 A 2d 858 (1985)

discussion and without prior notice. A majority of the Supreme Court of Delaware held that they had failed to reach an informed judgment and had therefore been grossly negligent; this took them outside the protection of the "business judgment" rule. It should be noted that the action was brought as a class action by a shareholder. Another aspect which deserves attention is the right of non executive directors to rely on what they are told by executives. The Courts may well continue to apply the *Dovey v. Corey* analysis,[28] and say that directors are entitled to assume executives are doing their job unless they have reason to suspect they are not; but they might also be a little harder on directors in determining when they should reasonably begin to suspect that all is not well, and what they should do about it.

Misfeasance Liability

I have expressed the view that, leaving aside Corporate Affairs, liquidators are the people from who inattentive company officers have most to fear. These days, liquidators can proceed against defaulting officers in the name of the company under sub-sections (2) and (7) of section 229. However, the traditional remedy of the liquidator has always been the "misfeasance" provision of the companies legislation: section 542 of the Code, *U.C.A.* section 367B and their predecessors.

Section 542 says that where on the application of the National Companies and Securities Commission or a "prescribed person" (an official manager, liquidator, provisional liquidator or any other person authorised by the N.C.S.C.) the Court is satisfied that:

a person is guilty of fraud, negligence, default, breach of trust or breach of duty in relation to a corporation; and

the corporation has suffered or is likely to suffer loss as a result, the Court can order the person to pay to the corporation the amount of the loss or damage.

The definition of "prescribed person" raises some interesting issues. First, it's been cut back from the version which appeared in *U.C.A.* section 367B, by the exclusion of contributories. This is more important than it might seem, because "contributories" includes shareholders. Needless to say this omission is not explained in the explanatory memorandum on the Code. Another interesting point

28. See p.94 supra

is who the N.C.S.C. will authorise to bring proceedings under the section. Presumably the authority will be given only to N.C.S.C. officers, although there is no reason in principle why it should not be given to a responsible private plaintiff having the requisite interest, such as a substantial shareholder.

Until amendments in the mid 70's introduced the specific references to "fraud, negligence, default, breach of trust or breach of duty", *U.C.A.* section 367B and its predecessors referred simply to "misfeasance" on the part of company officers. In the 1967 case *Re Tropic Isle Ltd,*[29] the Full Court in Queensland held that "negligence ... such as would expose the directors to an action for damages..." was not enough to make directors liable on a misfeasance summons. Something more had to be shown: either fraud, or that the directors "had completely failed to exercise the faculties of independent judgment and discretion...".[30]

The High Court considered U.C.A. section 367B in its original form (i.e. while it still referred only to misfeasance) in *Walker v. Wimborne.*[31] Mason, J. (as he then was), who delivered the majority judgment, said:

> To constitute misfeasance it must appear that there has been something more than mere negligence; it must be shown that what occurred amounted to a breach of duty.[32]

This is subtly but distinctly different from the approach in *Tropic Isle*, where the Court said that something more than negligence, *even where the negligence did amount to a breach of duty*, was required: there had to be a total failure to perform the duty at all.

After section 367B was amended to substitute specific heads of liability for the general reference to misfeasance, the key question was whether this made any substantive difference to the liability threshold. This question arose directly in *Kimberley Mineral Holdings Ltd. (in liq.) v. Triguboff.*[33] Needham, J., of the New South Wales Supreme Court held that the test of "negligence" in the amended section 367B (and now in section 542) was no different in substance from the old standard of misfeasance as applied in *Walker v. Wimborne*. The reference

29. *Re Tropic Isle Ltd (in liq.), Rees & Anor v King & Ors*, [1967] Qd R 193
30 Ibid, 204
31 (1976-77), 137 C L R. 1
32 (1976-77), 137 C.L R 1 at 8
33 (1977-1978), C L C 40 412 [1978] 1 N SW L R. 364

was not to "common law negligence" of the *Donoghue v. Stevenson*[34] variety, but to negligence amounting to a breach of a director's common law duty as described in *City Equitable.*

It seems to follow from *Walker v. Wimborne* and *Kimberley Mineral Holdings v. Triguboff* that in negligence cases, the tests for liability of directors and officers at common law, under section 229 and under section 542 are the same, and that to the extent that *Re Tropic Isle* represents a contrary view it should not be followed. But that again raises the same problem: what is the test?

In theory, if the standard is the same it should be possible to use the misfeasance cases as examples to show where Courts draw the line. The difficulty is that negligence is not the only head of misfeasance liability; in fact, pure negligence cases under section 542 and antecedent sections have been rare. Most of the cases involve breaches of statutory duty,[35] ultra vires acts,[36] or breach of directors' duty to act in the best interests of the company[37] *Tropic Isle* was a negligence case, but the directors were held not liable even though the Court seemed to think they were in breach of their common law duty. In Western Australia there is the somewhat perplexing judgment of Pidgeon, J., in *Re Boyagarra Pty. Ltd.*[38] where his Honour found a breach of duty, decided this amounted to misfeasance, and concluded there had been negligence for the purposes of *U.C.A.* section 367B (in its amended form). It is not clear why the decision was not simply based on the breach of duty, which is itself a head of liability under U.C.A. section 367B and section 542 of the Code.

In re Australasian Venezolana Pty Ltd[39] is a better example of a negligence case. There, a director signed cheques at the direction of the managing director, without bothering to ask what they were for; in fact they were drawn for a purpose which had nothing to do with

34 (1932) A C 562

35. See *Re Duomatic Ltd*, [1969] 2 Ch. 365, [1969] 1 All E R. 161, *Steen v Law*, [1963] 3 All E.R 770, *Re Yorke (Stationers) Pty Ltd*, [1965] N.S.W.R. 466

36 See *Re Claridge's Patent Asphalte Co Ltd*, [1921] 1 Ch. 543.

37 See *Walker v Wimborne*, n 32 supra ; *Wright v Frisina* (1983), A.C.L C. 858 This case is also authority for the proposition that the liability of a deceased director under the misfeasance provisions becomes a liability of his estate

38 *Re Boyagarra Pty Ltd (in liq), Evans v Dean & Ors* (1983), 1 A C.L.C. 858. This case is also authority for the proposition that the liability of a deceased director under the misfeasance provisions becomes a liability of his estate

39. (1962), 4 F L R. 60.

the interests of the company. Eggleston, J., made a finding of misfeasance, on the basis that the director had not made reasonable efforts to acquaint himself with the affairs of the company. However, he decided not to make an order for compensation because there was no evidence that the loans to which the funds had been applied could not be recovered. By way of contrast, as against the managing director who orchestrated the misapplication of funds, he did make an order for repayment to the company apparently on the basis that where misfeasance is deliberate rather than negligent the Court needs less evidence on which to base an order for compensation.

Apart from *City Equitable* itself the only other misfeasance case this writer has located containing a reference to the liability of careless directors is *Re Horsley & Weight Ltd.* There, Templeman, L.J., remarked that but for defects of pleading and evidence it might have been established that directors, who made a substantial and gratuitous pension payment when the company was experiencing financial problems, might have been guilty of "gross negligence, amounting to misfeasance".[40]

Other Civil Liability

Besides sections 229 and 542, there are a number of specific sections in the Code which impose civil liability on directors. Examples are:

- section 107 untrue statements or non disclosures in a prospectus;
- section 110 repayment of subscriptions where minimum subscription not achieved;
- section 116 prohibited payments for subscribing or procuring subscriptions for shares;
- section 130 company providing financial assistance for the purchase of its own shares;
- section 144A failure to keep a register of substantial shareholders; and
- section 230 loans to directors.

Sections 116 and 230 provide for compensation to the company. The others provide for compensation to third parties, except section 230 under which the Court may order the payment of compensation to either or both.

40. *Re Horsley & Weight Ltd,* [1982] 3 All E R 1045 at 1056

In most of these cases, liability depends on complicity in the breach. However, this can be a real risk for inattentive officers, especially non executive directors, where they are called upon to authorize a proposal and do so without realizing it is a breach of the law. These matters are dealt with in more detail.

Section 535: When Defaulting Officers Ought Fairly To Be Excused

On the rare occasions when civil actions against negligent directors or officers do come to Court, the defendants will usually try to take refuge in section 535 of the Code.

Section 535(1) gives a Court power to relieve directors or other officers from liability if satisfied that they "acted honestly" and having regard to all the circumstances, "ought fairly to be excused". Section 535(1) is intended to be pleaded as a defence. Section 535(2) is in similar terms, but enables directors or officers to make preemptive applications to the Court if they think they are going to be sued. Both apply only to *civil* proceedings, so they are not available against a prosecution or anticipated prosecution by the N.C.S.C (for example, for breach of section 229).

Section 535 is deliberately expressed in terms which give the Court a wide discretion, exercisable on a case by case basis. As a result, each case will depend on its own facts and it is difficult to lay down general principles. Nevertheless, in the negligence area it is difficult to see how there is much room for the operation of section 535 as an absolute defence. The reason for this is that in deciding whether directors or officers are in breach of their duty in the first place, Courts will already have been through the process of considering all the circumstances of the case to see whether it is "fair" that the director or officer should be held liable. If they think that his or her negligence is not "gross" or "culpable" enough to deserve liability, they will simply hold that there has been no breach of duty. In other words, whether a negligent company officer ought to be liable and whether he ought fairly to be excused is really the same question.

The position may be different where, in addition to negligence, another "misfeasance" element is present. This kind of situation arose in *Re Duomatic Ltd.*,[41] where directors had drawn funds in breach of

41 [1969] 2 Ch. 365, [1969] 1 All E.R. 161

a provision corresponding to section 233 of the Code. Buckley, J., was quick to conclude that there had been misfeasance because the payment was unlawful and ultra vires. However, he went on to consider whether the directors ought to be relieved under the provision corresponding to section 535. As with the Australian antecedents of section 535, the section applied only where the directors were found to have acted *reasonably* as well as honestly (a requirement omitted by the draftsman of the Code: see below). In deciding whether the directors had acted reasonably, Buckley, J., applied a test which would seem to apply with equal force to the determination of whether a negligent director or officer should be liable at common law, under section 229 or under section 542. He said:

> In my judgment a director of a company dealing with a matter of this kind who does not seek any legal advice at all but elects to deal with the matter himself without a proper exploration of the considerations which contribute, or ought to contribute to a decision as to what should be done on the company's behalf, cannot be said to act reasonably. ...I do not think he was *acting in the way in which a man of affairs dealing with his own affairs with reasonable care and circumspection could reasonably be expected to act in such a case*, for I think that any such imaginary character would take pains to find out all the relevant circumstances, many of which in this case depended on some knowledge of the law and ought to have encouraged Mr. Elvins to seek the assistance of a legal adviser.[42]

The conclusion is that whether in determining liability under section 229(2) or section 542, or in deciding whether relief should be given under section 535, the Courts must sooner or later come to the question: did the officer act reasonably in the circumstances?

Whether the director or officer has taken and acted on legal or other professional advice has been regarded as relevant in several cases.[43] Generally, a director who has followed professional advice will either escape liability altogether or be relieved under section 535. Has the situation changed now that section 535 does not expressly require the defaulting officer to have acted *reasonably* before he can claim relief? According to the New South Wales Court of Appeal in *Advance Bank Australia Limited & Ors v. FAI Insurances Limited,*[44] the answer is no. The Advance Bank directors, the appellants in that case, made much

42 [1969] 1 All E.R 161 at 171 (emphasis added).

43. In addition to *Re Duomatic Ltd,* supra, see *Re Toowoomba Welding Works Pty Ltd (No 2),* [1969] Qd.R. 337, *Re Claridge's Patent Asphalte Co Ltd,* n.37 *supra*

44. (1987), 5 A C L.C 725.

of the trial judge's finding that they had acted honestly and bona fide. It was submitted on their behalf that the omission of "reasonably" focussed attention on "honestly" as the principal criterion. Kirby, P., (with whom Glass, J.A., agreed) said:

> The difficulty of this argument is that it overlooks the fact that, for the relief provided under sec. 535, honesty is a requirement but it is not alone sufficient. The section also calls the attention of the Court to "all the circumstances of the case". The "case" referred to directs attention to the way in which the default or breach has occurred.[45]

His Honour, referring to the letters the directors had sent to shareholders soliciting proxies to oppose the election of FAI nominees to the Board and the telephone canvassing they had commissioned, went on:

> The letter and the soliciting script contained at once too much irrelevant, prejudicial and inaccurate information which was misleading and did not contain some of the countervailing information which directors, properly discharging their duties in these circumstances, would place before the shareholders.[46]

The clear message is that defaulting officers must still be able to show that they acted reasonably as well as honestly before they can hope to succeed in a claim for relief under section 535.

It is interesting that in the *Advance Bank* case, the directors had received comprehensive legal advice, and in broad terms had followed it; but their enthusiasm got the better of them in drafting the communications to shareholders, and they failed "to make the full and true disclosure which the Bank's lawyers had cautioned to be necessary". It is not unknown for clients to take legal advice and decide not to follow it; the moral of the *Advance Bank* story is that one of the risks inherent in doing that may be the loss of protection under section 535.

Criminal Liability: Companies & Securities Legislation

So far this article has concentrated on civil liability and enforcement by the company, a liquidator or a shareholder. But there are also many provisions in the companies and securities legislation which impose duties on companies and their officers, where failure to comply is an offence for which defaulting officers may be prosecuted by the N.C.S.C. or its delegates, under section 36 of the *Companies (Interpreta-*

45 Ibid , 746.
46. Ibid., 747.

tion and Miscellaneous Provisions) Code. Whether proceedings are brought summarily or on indictment is determined under section 35 of that Code, and section 34 provides that proceedings may be commenced within 5 years, or longer with the consent of the Ministerial Council.

A breach of section 229(2) itself is of course an offence. However, there has been little enforcement activity under this section and its predecessors. An inattentive company officer is more likely to find himself charged with one of the many specific offences provided for under the Codes. The most common type of offence is where an obligation is imposed on the company, and breach is an offence both by the company and by "any officer who is in default". Sections 131(7), 143(4), 148(10), 188(3), 217(5), 219(5) and 238(5) provide just a few examples and see also the general provisions to the same effect in section 143 of the *Securities Industry Code* and section 151(1) of the *Futures Industry Code.*

There are other sections which provide that where a breach occurs, the company is not guilty of an offence; the liability falls only on any officer who is in default. Examples are sections 116(3) and 230(5). The policy distinction is based on the view that these are really offences committed against, rather than by, the company, resulting in the depletion of shareholders' funds which should not be further depleted by a fine. Under both of the sections cited as examples, the Court has power to order defaulting officers to compensate the company. The meaning of "officer in default" in these sections is explained by section 572: it means any officer or former officer, "who is in any way, by act or omission, directly or indirectly, *knowingly* concerned in or party to the contravention or failure" (emphasis added).

The requirement that the prosecution should prove an officer was *knowingly* concerned before he is guilty of an offence may exonerate inattentive officers who can rely on the defence of ignorance. However, this is subject to a number of qualifications. First, the element of knowledge goes to the factual substance of the breach, not that it was an offence; lack of knowledge of the law is no defence.[47] Nor is it necessary that precise details be known, if the officer knows the main substance of what has happened.[48] Secondly, nominee directors who

47 *Abley v Crosara,* [1946] V L R 53
48 *D P P v Maxwell,* [1978] 3 All E R 1140

exercise no independent discretion will be fixed with the knowledge of the party who nominated them.[49] Thirdly, if a person lacks knowledge only because he has turned a blind eye to facts which are obvious, or because he has refrained from making an enquiry which he knew he should have made, he may be held to have constructive knowledge.[50] Fourthly, the secretary cannot claim lack of knowledge in a number of cases; he or she is deemed by section 572(2) to be knowingly concerned in breaches of section 216 (registered office) and the provisions requiring lodgement of returns of directors, managers and secretaries (section 238) and annual returns (section 263).

Corporate Affairs' most prolific area of enforcement activity is in prosecuting company secretaries for failing to lodge annual returns. It is no coincidence that this is an area where no proof of knowledge is required. Generally speaking, inattentive non executive directors have been safe from prosecution for offences where knowledge is an element; a combination of the evidentiary problems and Corporate Affairs' chronic shortage of resources has meant those cases are just not worth taking on. In the case of officers who are executives, it is much more likely that they will be directly involved; and if their inattention consists of failure to acquaint themselves with the law, they are at risk.

There are other offences, however, where the risks for inattentive officers are much higher. One example is section 564. Under section 564(1), any officer who furnishes, or authorizes the furnishing of, false or misleading information to any of a range of parties including directors, auditors, shareholders and stock exchanges is guilty of an offence with a maximum penalty of $10,000 or 2 years imprisonment if he knows the information is false or misleading. Under section 564(2) a lesser offence (maximum penalty $5,000 or one years imprisonment) is committed by an officer who does exactly the same thing *without knowing* the information is false or misleading, but without having taken reasonable steps to ensure that it was not. In

49 *Selangor United Rubber Estates Ltd v Cradock*, [1968] 2 All E R 1073 at 1123.
50 *The Zamora (No 2)*, [1921] 1 A.C 801 at 812-3.

theory at least, this one is a real trap for the inattentive director. Misleading reports to shareholders and the Stock Exchange are all too common, and in many cases they are approved by the issuing company's Board without proper scrutiny by the directors who were not actually involved in writing them. But inattentive directors may take some comfort from the fact that it is hard for the N.C.S.C. or Corporate Affairs authorities to find out when Stock Exchange releases about such things as levels of gold production or reserves are false, and even when they do they have so far shown very little inclination to do anything about them.

To obtain a conviction under section 564(2), the prosecution has to prove that the defendant did not take "reasonable steps". The prosecution's task is made easier under sections 267(11) and 555, where a director of a company which did not keep proper accounts is guilty of an offence if he did not take all reasonable steps to see that the accounts were kept properly. This means, in theory, that if there was even one step a director should have taken but did not take, he is guilty. However, the sting is taken out of these sections to a large extent by sections 267(12) and 555(2), which make it a defence that the director had reasonable grounds to believe and did believe that a competent and reliable person was responsible for seeing that the accounts were properly kept. In many cases, this will save everyone except the finance director from responsibility.

Finally, note should be taken of section 108, which imposes criminal liability on every person who authorized the issue of a prospectus containing an untrue statement or non disclosure. As soon as the prosecution proves the authority and the untrue statement, the onus of proof shifts to the defendant; he will be guilty unless he can prove that the statement or non disclosure was immaterial, that he believed on reasonable grounds that the statement was true or the non disclosure was immaterial, or that the non disclosure was inadvertent. Prospectuses are a special case in a number of ways. One is that they are subjected to detailed scrutiny by Corporate Affairs. Nevertheless, cases of false and misleading prospectuses are by no means unknown. This is another area where there has been little enforcement activity. The Western Australian Corporate Affairs Department was supposed to be spearheading a campaign to change all that, with its prosecution of three directors of Sadleir Computer Research Limited. The failure to obtain a committal in that case is eloquent enough without further comment.

So, even though there is a formidable list of offences under the *Companies Code* for which directors may become liable, successful prosecutions against inattentive directors are extremely rare. The defence of lack of knowledge often protects outside directors, and even for executive officers the combination of evidentiary difficulties and the limited resources of Corporate Affairs authorities make the risk of prosecution remote in all but the most egregious cases.

Ironically, perhaps the greatest risk for an officer whose inattention leads him to commit an offence is not prosecution for the offence itself, but the possibility that the offence may constitute a "default" under section 542 and so expose him to civil liability to compensate the company if it goes into liquidation. The Courts have always been prepared to hold that a breach of statutory duty amounted to misfeasance under the predecessors of section 542,[51] and this propensity has continued despite the change in wording. As recently as last year in *Re Indopal Pty Ltd*,[52] it was held that failure by directors to make out a report to a liquidator under section 375 of the Code was a "default" under section 542. It is in this area that section 535 will have its greatest role to play. A combination of breach of statutory duty and section 542 may provide liquidators with a short cut to liability as against inattentive company officers; but, as happened in *Re Duomatic*,[53] the Courts are likely to make the real determination of liability under section 535, applying the same test of reasonableness as they do in deciding whether a director has breached his duty at common law.

Criminal Liability: Other Legislation

It has become reasonably common in State legislation in recent years to "lift the corporate veil" by providing that where a company commits an offence, officers of the company are guilty of the offence as well. One Western Australian example is section 55 of the *Occupational Health, Safety and Welfare Act, 1984*, as amended in 1987. That section says that where a body corporate is guilty of an offence under

51 See the cases cited at n.36 supra
52 (1987), 5 A C L C 278
53 n 42 supra

the Act and it is proved that the offence "occurred with the consent or connivance of, *or was attributable to any neglect on the part of* any officer of the body corporate, that officer is guilty of the same offence" (emphasis added). Other examples may be found in the *Transport Co-ordination Act, 1966* (section 55A), the *State Energy Commission Act, 1979* (section 86(2), the *Western Australian Products Symbol Act, 1972* (section 13), the *Business Franchise (Tobacco) Act, 1975* (section 12D), the *Industrial Arbitration Act, 1979* (section 96C), the *Machinery Safety Act, 1974* (section 82), the *Consumer Affairs Act, 1971* (section 23Y), the *Motor Vehicle Dealers Act, 1973* (section 55) and the *Factories and Shops Act, 1963* (section 116A). The directors and officers of building societies are liable for any offence committed by their society, unless they show that they used "all due diligence" to prevent the commission of the offence (*Building Societies Act, 1976,* section 84). The *Land Tax Act, 1976,* section 52 makes directors and managers resident in Western Australia liable for contraventions of the Act by their corporations, and section 89 of the *Finance Brokers Control Act, 1975* makes directors of an incorporated finance broker jointly and severally liable to clients for defalcations by the company.

A provision that should be of particular concern to companies that do business in New South Wales is section 25(1C) of the *Stamp Duties Act, 1920* (NSW). That section provides that if documents on which a company is liable for stamp duty are not lodged for stamping as required by the Act, the company and all of its directors are guilty of an offence. To escape liability, a director must satisfy the Court that he used "all due diligence" to prevent the commission of the offence: a heavy onus indeed. The Western Australian *Stamp Act* has not been taken to the same lengths — at least, not yet.

Another revenue statute with a sting in its tail for inattentive company officers is the *Taxation Administration Act.* Section 8Y(1) says that where a corporation commits a taxation offence, every person concerned in the management of the corporation is deemed to have committed the same offence. Sub-section (2) offers relief to an officer who is able to discharge the onus of proving that he was not knowingly involved in the offence. The "knowledge" element is reminiscent of the *Companies Code*; but there the onus is on the officer to prove his lack of knowledge before he is discharged from liability.

The policy behind the decision to impose personal liability on directors is not hard to identify. Directors clearly have a more direct personal interest in ensuring that the law is not breached if they are at risk of having to pay substantial fines out of their own money, or even going to jail. The increasing prevalence of this kind of legislation, with its tendency to penalize inattention and/or to reverse the onus of proof, is perhaps the most serious threat that an officer faces while his company remains a going concern. In my opinion, it is a salutary one.

Insurance

Company directors frequently ask their lawyers about directors' and officers' liability insurance. It is available, but it is costly. What is more, section 237 of the *Companies Code* prevents the company from paying the premiums at least for that part of the policy which indemnifies the director against liability.

The company can pay the premiums for that part of the policy which indemnifies the officer against the costs of a successful defence. Brokers are wont to offer packages which involve a large premium for the latter component (paid by the company) and a small premium for the former (paid by the officer). Since the potential payout associated with liability is considerably greater than that associated with a successful defence, the legality of this practice in terms of section 237 is dubious.

There is a body of opinion that directors' and officers' liability insurance is of questionable value. First, it may be cynical but it is certainly realistic to observe that an insured director is more likely to be sued, because the insurance turns him into a "deep pocket" defendant. Secondly, directors and officers can protect themselves far more effectively by doing their jobs with reasonable care, skill and diligence. The substantial cost of the insurance is better spent on ensuring that the company and, in the case of outside directors, the directors as individuals can get all the advice they need on the extent of their legal responsibilities under the Code and the specific legislation that affects the company's business.

For non-executive directors in particular, there are some simple steps that can be taken to minimize risk. The first is to have a working knowledge of their legal responsibilities, including those specific to the area where the company does business. There are simple publications available, but they should always be read in conjunction with specific legal advice on the particular situation of the company. Secondly, directors should do their homework — read the papers that are sent to them and if the information is insufficient, ask for more. Thirdly, every director should play an active role in Board meetings expressing opinions and questioning anything not understood. Finally, directors should keep their Board papers and notes, and make a written record of their opinions, especially where they disagree with the majority decision on a contentious subject.

Conclusion

In determining the standards of liability which apply to inattentive company officers, the principal policy objective should be to make company officers pay attention. The standard of conduct expected should be clear enough, and the risk of enforcement immediate enough, to create an effective deterrent.

The duty of care which arises at common law and under section 229 of the Companies Code is not an effective deterrent at present. In the first place, there is very little modern case law to tell us where the threshold of liability lies. Secondly, the duty is in practice enforced in one situation only: where the company has gone into liquidation. As a practical matter, the duty of care is not a threat to inattentive officers and especially not to inattentive directors while their companies remain going concerns.

The first of these factors may soon change; as a result of spectacular crashes like TEA and Teachers' Credit, we may see some new case law on the standards of care and diligence expected from directors. However, the second factor is unlikely to change unless more effective enforcement action is taken by regulatory authorities, or alternatively the barriers to shareholder action are removed. One way to do this would be to take up the suggestion made by the Chief Justice of Western Australia in his speech to last year's 24th Australian Legal Convention in Perth[54] and introduce a controlled system of contingent fees.

Most of the law on the duties of inattentive company officers has been made in actions by liquidators. With the introduction of the

54. The Hon Sir Francis Burt, K C M G., "The Moving Finger or the Irremovable Digit", Law Council of Australia Papers of the 24th Australian Legal Convention (1987), 9 at 13

specific concept of negligence instead of the broader concept of misfeasance, section 542 of the *Companies Code* is the main threat to inattentive company directors in the area of civil liability. The authorities now seem to establish that "negligence" in section 542 means the same thing as a breach of the common law duty or of section 229.

Where an officer's inattention results in a breach of statutory duty, a liquidator may have an easier road to success under section 542 by relying on the alternative head of liability, "default". In practice, however, there is likely to be little difference because the Court will apply the same test in determining the officer's entitlement to relief under section 535 as it would in determining liability for negligence.

The key question is : what is this test? It seems likely that the Courts will continue to apply the tests enunciated in *City Equitable*, but that the flexible nature of those tests will be tightened to reflect the increasing sophistication of corporate life. Basically, the test is this : what might reasonably be expected of that particular director, in his position as a director of that particular company? In determining what is reasonable, the Courts will need to create a deterrent to inattention without creating a disincentive to involvement in the management or direction of companies.

While we wait for the duty of care and diligence to arrive in the second half of the 20th century, we are beyond Orwell's 1984 when it comes to statutory liabilities. The legislators have made it very clear that they are prepared to impose liabilities on directors and officers to deter breaches of the law; and where necessary to give effect to this policy they have removed barriers to enforcement by such means as reversing the presumption of innocence. The fact that so little is heard of derivative prosecutions against directors, however, indicates that governments have yet to take the further step of committing adequate resources to enforcement; and laws without enforcement have little deterrent value.

In the increasingly complex society we live in, the inattention of a company officer can cost millions of dollars. Worse still, it can cost the lives of thousands of people, in a tragedy like the one that occurred at the Union Carbide plant at Bhopal. We are approaching the stage where we can no longer afford to be lenient toward inattention on the part of company officers, and it is time our legal system developed sophisticated standards to deal with it. In short, the inattentive company officer deserves all the liability he gets and at present, he is getting nowhere near the liability he deserves.