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Directors and Officers Alert
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ASIC v Rich: Don't be discouraged: Judicial support for responsible risk taking in a corporate environment is still good law

One aspect of the recent decision in the *Australian Securities and Investments Commission* v *Rich* [2009] NSWSC 1229 not covered by commentators, or the press, is the continued recognition by the Court of the importance of responsible risk taking in a commercial setting.

Two former Officers have been cleared of breaching their duties of care in the latest Supreme Court fall-out from the collapse of telecommunications giant, the One.Tel Group.

ASIC failed to make out its case against two former Officers of the billion dollar company that spiralled into liquidation in 2001. One.Tel became insolvent after financial investors pulled the plug on a $132 million injection of funds, claiming they had been misled about the company's troubled finances.

ASIC argued that joint CEO Jodee Rich and Finance Director Mark Silbermann breached their duties of care and diligence under section 180(1) of the *Corporations Act 2001* (Cth) as they should have:

- known about One.Tel's true financial position;
- promptly ensured that the board was made aware and fully informed of the Group's position; and
- immediately recommended that the Group cease trading.

In addition to claims that they misled the Board by including unfounded forecasts and earning positions in board papers and failing to disclose accurate material on the Group's cashflow, Rich was accused of failing to ensure *"proper systems were maintained to produce accurate financial information flowing from management to the board"*.

This allegation by the corporate regulator is an important indicator for Directors and Officers that proper systems must be in place to support the flow of information about decisions being made, particularly in large Corporations.

After a 232-day hearing, however, Austin J held that the Officers' decisions were protected by the business judgment rule in section 180(2) of the Corporations Act.

If you are a Director or an Officer, you will not be liable for breaching your duty of care and diligence where you can show:

- you have made a business judgment;
- you acted in good faith, for a proper purpose and without any material personal interest in the subject-matter;

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- you informed yourself of the subject to what you believe is an appropriate extent that is reasonable (in light of time constraints and the accessibility of information);
- you believe your decision is in the best interests of your corporation; and
- your belief is rational, based on an arguable chain of reasoning, and is not a belief that no reasonable person in your position would hold.

A *"business judgment"* is any decision to take or not to take action in relation to a matter relevant to your Corporation's business operations, which Austin J held to include decisions in planning, budgeting and forecasting. His Honour guided that the question to be asked is:

"whether the director or officer has turned his or her mind to the matter."

Arguing that the defence was not available to Rich and Silbermann, ASIC claimed that inaction and omissions could not be spun into *"conscious and considered acts involving the exercise of judgment"*. Rejecting this argument, His Honour said that the Officers had turned their minds to the matters in issue and made decisions - ASIC just did not agree with them.

While noting that the defence does not extend protection to a failure of oversight where there is a complete lack of decision-making, His Honour explained that the defence seeks to:

"ensure that directors and officers are not discouraged from taking advantage of opportunities that involve responsible risk taking".

In your decision-making as a Director or Officer at the Board or management level, you may have protection from the consequences of your decision where you can demonstrate that you have taken the steps outlined above.

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