



How do we assess the risk of personal liability for directors arising out of tortious acts?

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This is well-recognised as a confusing area of the law. This question is still unsettled today even though the first test which attempted to resolve the matter was introduced in 1924. Further tests have developed and a great deal of scrutiny has been given to them all as alternatives to a solution. This article attempts to summarise the origins of the law and then follow its progress in order to propose a way forward that may provide the certainty and predictability that directors must crave to properly assess their personal risk. It will be argued that all tests should not have to stand alone but contribute to a scale of analysis that will find a director either a primary or joint tortfeasor.

I Introduction

It is trite law to say that a director even acting under cover of a company's responsibility can attract personal liability for the commission of a tort if he or she becomes an actor in the conduct of that tort by invading the rights of another (for example, trespassing on another's land or seizing their goods).¹ Similarly it is also true that a company, as a separate entity, can be liable in tort for its own actions (naturally carried out singularly or collectively by its physical agents). Some examples would include breaches of contracts generally (the tort of inducing a breach of contract, interfering in contractual relations or conspiracy to breach a contract), breaches of intellectual property rights (the tort of passing off) and actions for misleading and deceptive conduct (the tort of negligent misrepresentation).

The real risk however in terms of personal liability for directors in tortious actions, is being joined with the company as a joint tortfeasor. The significance of this article is that this type of potential personal liability would not be expected to be high on the list of concerns for directors. This could be expected when their focus is primarily on satisfying the many statutory duties and obligations they have, whether it be under the *Corporations Act 2001* (Cth) or the myriad of other pieces of legislation requiring compliance. But as this article will show, the risk is definitely real, particularly when it comes to closely held companies, and has been the subject of many significant cases. Directors generally think in terms of their duties and obligations to the company and to the shareholders as a whole, whereas this risk is another example of an exception where liability could come directly and personally to the directors from external parties under the right circumstances.

One of the reasons directors may be more blasé about this risk is that it is

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¹ *Knights Capital Group Ltd v Bajada and Associates Pty Ltd* [2016] WASC 69 (4 March 2016) [68] ('*Knights Capital*').

easy to get caught up in the express statutory regimes. This article should serve as a timely reminder that the *Corporations Act*, dealing with the personal liability of directors, for example, has ‘effect in addition to, and not in derogation of, any rule of law relating to the duty or liability of a person because of their office or employment in relation to a corporation; and ... [does] not prevent the commencement of civil proceedings for a breach of a duty ...’.² So it is yet another example where third parties may include directors in a personal action and overcome the directors’ ability to hide behind the corporate veil.

Even when directors consider this potential liability as a joint tortfeasor with their company, their concerns may be low because of the long standing principle that has become known as the rule in *Said v Butt*.³

The application of that principle has been held to have the consequence that where a director of a company, acting within the scope of his or her authority, causes the company to breach a contract with a third party, the director cannot be held liable for inducing or procuring the company to breach the contract.⁴

It seems that directors may have taken comfort from this approach even in a broader context than just inducing or procuring a breach of contract. That is, provided the director is acting within the scope of their authority the corporate veil will protect them.

However in reality there have been many cases that have demonstrated a preparedness of the courts to lift that corporate veil and find the director personally liable. The difficulty is that the law to determine this is unsettled and still being debated. Numerous tests and criteria have been put forward, but the elements that should make up a certain set of principles to be applied have not been resolved.

there may be room for further judicial exploration of the basis for, and limits of, the rule in *Said v Butt*, and the place of that rule within the common law’s approach to the tort liability of directors more generally. Furthermore, the test for determining when a director is involved in the company’s tortious conduct beyond merely being a director of the company, so that the director may be found liable as a joint tortfeasor with a company, for torts committed by that company, is not settled.⁵

It is worth noting that the above commentary was made in 2016. It has taken us more than 90 years to get to this point of analysis. Is it not about time that we can provide the principles and the underlying elements that we can rely upon with certainty and predictability?

The main goals therefore of this article are to:

- (1) Highlight the potential risk of liability for directors who may not currently or adequately perceive it;

² *Corporations Act 2001* (Cth) s 185. See also s 179.

³ [1920] 3 KB 497. It is worth noting that the principle comes from the judgment of McCardie J. He hypothetically considered the position of directors’ liability as joint tortfeasors even though there was no breach of contract by the relevant company. Despite the arguments therefore, that the comments are obiter, its weight has broadly been accepted as the ‘rule’ so described.

⁴ *Knights Capital* [2016] WASC 69 (4 March 2016) [57].

⁵ *Ibid* [81].

- (2) Identify the key elements of that liability as far as we can distil them to date; and
- (3) Suggest a way forward that will provide a level of certainty that all directors must crave in making their own personal risk assessments.

II A summary of the tests developed to find a director personally liable as a primary or joint tortfeasor

This summary of the tests includes approaches across a number of jurisdictions including the United Kingdom, Canada, New Zealand and Australia. The 1920s saw the genesis of these tests and by the time we reached the next century there had arguably been at least four distinct approaches that can be identified but it has been hard to find consistency. We still have the confusing situation in Australia where State Supreme Courts and Federal Courts have been emphasising various criteria but have not been definitive. This is often because no matter which test is applied, liability would flow or because of the slightly different language being used in the earlier cases relied upon. On closer inspection, at the end of this article, it will be argued there is good reason to rationalise elements and provide a great deal more certainty. It is worth noting on this point that most of the key cases in this area have been dealt with in the Federal Court of Australia or State Supreme Courts and without necessarily binding authority.

Judges⁶ and commentators⁷ have long suggested that the uncertainty in this area is a consequence of a clash between the principles of company law and the law of torts. For some, it is even a question of which should dominate.⁸ A cornerstone of company law is the existence of the corporation as a separate legal entity distinct from its human controllers. There is an apparent conflict in allowing directors, when carrying out their functions as directors, to be held personally liable for the tortious acts of this separate corporate being. Unfortunately the existing theoretical models that support the company have been unable to find a way through the complex policy considerations. It has been argued that, 'neither theory nor commonly accepted corporate law doctrines are of particular use in the resolution of disputes between directors and the tort creditors of their companies'.⁹ While company law theory struggles to find an appropriate solution, tort law is simply trying to hold the wrongdoer responsible for the harm caused.¹⁰

The development of these tests has been the subject of many academic

6 *Mentmore Manufacturing Co Ltd v National Merchandising Manufacturing Co Inc* (1978) 89 DLR (3d) 195, 202.

7 John H Farrar, 'The Personal Liability of Directors for Corporate Torts' (1997) 9 *Bond Law Review* 102, 112.

8 Ross Grantham and Charles Rickett, 'Directors' "tortious" liability: Contract, tort or company law?' (1999) 62 *Modern Law Review* 133, 139.

9 Helen Anderson, 'The theory of the corporation and its relevance to directors' tortious liability to creditors' (2004) 16 *Australian Journal of Corporate Law* 73; Ross Grantham and Charles Rickett, 'Company directors' liability for torts' [2003] *New Zealand Law Journal* 155.

10 The principle that everyone should be answerable for his or her tortious wrongs (*alterum non laedere*): John H Farrar, 'Personal Liability of Directors for Torts of Company' (1997) 71 *Australian Law Journal* 20.

articles that have critiqued and analysed the approaches.¹¹ Although they may have been described in slightly different ways there are arguably four distinct categories of test that can be identified. They are:

- (1) The 'direct or procure test' (or the '*Performing Right Society*'¹² test);
- (2) The 'make the tort his own test' (or the '*Mentmore*'¹³ test);
- (3) The 'assumption of responsibility test' (or the '*Trevor Ivory*'¹⁴ test);
and
- (4) The '*Root Quality*'¹⁵ test including the general notion of directors procuring the company to violate a legal right.

A The direct or procure test

The approach which has been called 'the direct or procure test' has its origins in the case of *Rainham Chemical Works Ltd (in liq) v Belvedere Fish Guano Co Ltd*.¹⁶ The House of Lords in this appeal was trying to determine whether the directors of a company should be personally liable, along with the company, on the basis of an action on the principle of *Rylands v Fletcher*.¹⁷ In an often quoted part of his judgment, Lord Buckmaster considered the general question of the personal liability of directors of the tortious acts of the company as follows:

If the company was really trading independently on its own account, the fact that it was directed by Messrs Feldman and Partridge would not render them responsible for its tortious acts unless, indeed, they were acts expressly directed by them. If a company is formed for the express purpose of doing a wrongful act or if, when formed, those in control expressly directed a wrongful thing be done, individuals as well as the company are responsible for the consequences, but there is no evidence in the present case to establish liability under either of these heads.¹⁸

Lord Atkin relied upon this judgment in *Performing Right Society Ltd v Caryl Theatrical Syndicate Ltd*¹⁹ as supporting the following statement of principle: 'Prima facie a managing director is not liable for tortious acts done by servants

11 David A Wishart, 'The personal liability of directors in tort' (1992) 10 *Company and Securities Law Journal* 363; G H L Fridman, 'Personal tort liability of company directors' (1992) 5 *Canterbury Law Review* 41; Mary-Anne Simpson, 'Directors' liability in tort' (1995) *New Zealand Law Journal* 6; *ibid*; Farrar, 'The Personal Liability of Directors for Corporate Torts', above n 7; Grantham and Rickett, 'Directors' "Tortious" Liability, above n 8; Grantham and Charles Rickett, 'Company directors' liability for torts', above n 9; Stephen Todd, 'Assuming responsibility for torts' (2003) 119 *Law Quarterly Review* 199; Anderson, above n 9; Peter Watts, '*Trevor Ivory v Anderson*; reasoning from outer space' [2007] *New Zealand Law Journal* 25; Susan Watson, 'Liability of individuals for torts of the company' (2007) *New Zealand Law Journal* 27; Neil Foster, 'Personal civil liability of company officers for company workplace torts' (2008) 16 *Torts Law Journal* 20.

12 *Performing Right Society Ltd v Caryl Theatrical Syndicate Ltd* [1924] 1 KB 1 ('*Performing Right Society*').

13 *Mentmore Manufacturing Co Ltd v National Merchandising Manufacturing Co Inc* (1978) 89 DLR (3d) 195.

14 *Trevor Ivory Ltd v Anderson* [1992] 2 NZLR 517 ('*Trevor Ivory*').

15 *Root Quality Pty Ltd v Root Control Technologies Pty Ltd* (2000) 177 ALR 231 ('*Root Quality*').

16 [1921] 2 AC 465 ('*Rainham Chemical*').

17 [1861–73] All ER Rep 1.

18 *Rainham Chemical* [1921] 2 AC 465, 476.

19 [1924] 1 KB 1.

of the company unless he himself is privy to the acts, that is to say unless he ordered or procured the acts to be done.’²⁰

He thought however this was more narrowly put than would be needed as a general pronouncement of the law. He was of the view that the express direction from the directors is not necessary for their personal liability. ‘If the directors themselves directed or procured the commission of the act they would be liable in whatever sense they did so, whether expressly or impliedly.’²¹

The approach in these cases received further approval in the Privy Council in *Wah Tat Bank Ltd v Chan Cheng Kum*.²² The Court of Appeal too in *C Evans & Sons Ltd v Spritebrand Ltd*²³ endorsed this test but with the view that it could not ‘be regarded as a precise and unqualified statement of the principles governing a director’s personal liability for his company’s torts’.²⁴ This was not intended as a criticism of the previous judgments as Slade LJ felt the description of principle in the test was not intended to be so precise and he did not wish to attempt to define the circumstances in which a director may have authorised, directed or procured a tortious act of the company.²⁵

B The ‘make the tort his own’ test

The ‘make the tort his own’ test, originated in the Canadian decision of *Mentmore Manufacturing Co Inc v National Merchandising Manufacturing Co Inc*.²⁶ The Federal Court of Appeal, as in so many cases in this area, was considering the potential personal liability of a director arising out of the infringement by the company of intellectual property rights. The court was presented with the authorities of *Rainham Chemical*²⁷ and *Performing Right Society*²⁸ which were relied upon by the trial judge as representing the applicable law. Le Dain J was concerned that the ‘direct or procure test’ could too easily mean that a director of the company could be personally liable where their conduct was only such that would be normally required in the management of the relevant corporation. He was very conscious of the competing issues of policy but thought something more than mere direction should be required to look behind the corporate structure and this should apply not only to large corporations but also the smaller closely held ones as well.

What is involved here is a very difficult question of policy. On the one hand, there is the principle that an incorporated company is separate and distinct in law from its shareholders, directors and officers, and it is in the interests of the commercial purposes served by incorporated enterprise that they should as a general rule enjoy the benefit of a limited liability afforded by incorporation. On the other hand, there is the principle that everyone should answer for his tortious acts ... It would render the offices of director or principal officer unduly hazardous if the degree of direction

²⁰ Ibid 14.

²¹ *Performing Right Society* [1924] 1 KB 1, 15.

²² [1975] AC 507 (*‘Wah Tat Bank’*).

²³ [1985] 2 All ER 415 (*‘C Evans’*).

²⁴ Ibid 424.

²⁵ Ibid.

²⁶ (1978) 89 DLR (3d) 195.

²⁷ *Rainham Chemical Works Ltd (in liq) v Belvedere Fish Guano Co Ltd* [1921] 2 AC 465.

²⁸ *Performing Right Society Ltd v Cyril Theatrical Syndicate Ltd* [1924] 1 KB 1.

normally required in the management of the corporations manufacturing and selling activity could by itself make the director or officer personally liable for infringement by his company.²⁹

So what should this further requirement be? Le Dain J relied upon a number of English decisions³⁰ as support for the proposition that personal liability was seen as only being warranted where the directors were knowing, deliberate or wilful participants in the tort. Liability, to his mind then, required this extra quality in order to 'make the tortious act his own'.

What ... is the kind of participation in the acts of the company that should give rise to personal liability? It is an elusive question. It would appear to be that degree and kind of personal involvement by which the director or officer makes the tortious act his own. It is obviously a question of fact to be decided on the circumstances of each case. I have not found much assistance in the particular cases in which courts have concluded that the facts were such as to warrant personal liability. But there would appear to have been in these cases a knowing, deliberate, wilful quality to the participation.³¹

This is of course a higher test than one requiring evidence of direction or procurement but this is defended on the grounds that to require less would open the floodgates of potential liability particularly to directors of small companies.

This stricter test was rejected by the Court of Appeal in *C Evans*.³² Significantly the Court of Appeal did not try to refine the broad nature of the direct or procure test but seemed content to let each case be resolved on its own particular acts.

Although the *Mentmore* test has been criticised and specifically rejected by Australian courts,³³ there has also been some support for the approach. In a number of cases over this period it has been demonstrated that the courts in Australia have been reluctant to resolve the issue of the competing tests. Commonly this has been because on the facts of the relevant case any distinction has not been necessary. Directors have commonly been found to be knowing, deliberate or wilful participants in the tort. It has even been suggested that any difference between the tests is more apparent than real.³⁴

²⁹ *Mentmore* (1978) 89 DLR (3d) 195, 202.

³⁰ *Reitzman v Grahame-Chapman and Derustit Ltd* (1950) 67 RPC 178; *Oertli AG v EJ Bowman (London) Ltd* [1956] RPC 282; *Yuille v B & B Fisheries (Leigh) Ltd and Bates* [1958] 2 Lloyds Rep 596; *Wah Tat Bank* [1975] AC 507.

³¹ *Mentmore* (1978) 89 DLR (3d) 195, 203. This approach was endorsed by Nourse J in the High Court of Justice (Chancery Division) decision of *White Horse Distillers Ltd v Gregson Associates Ltd* [1984] RPC 61,91-2.

³² *C Evans & Sons Ltd v Spritebrand Ltd* [1985] 2 All ER 415.

³³ Eg, *Johnson Matthey (Aust) Ltd v Dascorp Pty Ltd* (2003) 9 VR 171; *Foxtel Management Pty Ltd v Mod Shop Pty Ltd* (2007) 165 FCR 149; *Huhtamaki Australia Ltd v Australia Pak Pty Ltd* [2006] FCA 62 (10 February 2006).

³⁴ As discussed later in the article: *Allen Manufacturing Co Pty Ltd v McCallum & Co Pty Ltd* (2001) 53 IPR 400, 410 [43] ('*Allen Manufacturing*').

C The assumption of responsibility test

This test originated in the NZ Court of Appeal in the decision of *Trevor Ivory Ltd v Anderson*.³⁵ At first instance, Heron J had found Mr Ivory, the director of Trevor Ivory Ltd, personally liable in tort for the breach of a duty of care to clients of the company. Mr Ivory had supplied negligent advice and instructions. Mr Ivory arguably had provided this advice through a contract that existed between his company and the client. Damages were awarded against the company on the basis of both contract and tort. Most significantly however the judge found Mr Ivory to have had a personal duty of care to the clients in giving his advice and that he should be personally liable, along with the company, for his negligence in breaching that duty.

All three appeal judges, Cooke P, Hardie Boys and McGechan JJ supported the trial judge's decision in relation to the liability of the company but rejected the finding that Mr Ivory in these circumstances should have a personal liability in tort. Although they all recognised that such a liability was possible they were each concerned to find in the conduct of the director some evidence that he had assumed a personal responsibility. Hardie Boys and McGechan JJ believed Mr Ivory's conduct had brought him close to that position but in the end the court unanimously found no liability for him.

The clearest expression of what has come to be known as the 'assumption of responsibility' test is contained in the judgment of Hardie Boys J. The judge carefully drew a distinction between the situation where directors will be personally liable for their own tortious acts and the position where the director's acts are actually the acts of the company in a legal sense. In a passage which included a discussion of *Lee v Lee's Air Farming Ltd*,³⁶ *Tesco Supermarkets Ltd v Natrass*³⁷ and *Sealand of the Pacific v Robert C McHaffie Ltd*³⁸ the judge stressed the significance of these different capacities. He thought it would be the usual case that the director's conduct would be seen as the acts of the company as the separate entity rather than the acts of the director as agent. In these circumstances, personal liability could only arise where there was evidence that the director had done something more than merely act for the company, so as to assume that personal liability.

In the policy area, I find no difficulty in the imposition of personal liability on a director in appropriate circumstances. To make a director liable for his personal negligence does not in my opinion run counter to the purposes and effect of incorporation. Those purposes relevantly include protection of shareholders from the company's liabilities, but that affords no reason to protect directors from the consequences of their own acts and omissions. What does run counter to the purposes and effect of incorporation is a failure to recognise the two capacities in which directors may act; that in appropriate circumstances they are to be identified with the company itself, so that their acts are in truth the company's acts. Indeed I consider that the nature of corporate personality requires that this identification normally be the basic premise and that clear evidence be needed to displace it with

35 [1992] 2 NZLR 517.

36 [1961] NZLR 325.

37 [1972] AC 153.

38 (1974) 51 DLR (3d) 702 ('*Sealand of the Pacific*').

a finding that a director is acting not as the company but as the company's agent or servant in a way that renders him personally liable ...

Essentially, I think the test is, or at least includes, whether there has been an assumption of responsibility, actual or imputed. That is an appropriate test for the personal liability of both a director and an employee.³⁹

There is the clear indication in this passage that the personal liability of the director arises under this test, not as a joint tortfeasor with the company, but because their conduct was such that they could be said to have personally assumed responsibility as an agent for the company. In other words, if the director gets so personally involved in the relevant act they will lose the protection of the company structure because they will be seen as becoming an agent of the company and not simply part of the company performing its own act. So for *Hardie Boys J*, the assumption of responsibility test on this basis is about properly identifying when the acts of the director become their own acts rather than simply carrying out their functions within the company structure.

For *Cooke P* it seemed the whole question turned on whether the relevant director in the course of activities on behalf of the company came under a personal duty to a third party.⁴⁰ In *Centrepac Partnership v Foreign Currency Consultants Ltd*⁴¹ *Gault J* in the High Court of New Zealand did not follow this test because it was found that the advice given by the relevant employee was the result of a clear personal engagement⁴² to provide the service. However the principles described by *Gault J* are directly on point.

To find a duty of care in this situation, in my view, does not involve lifting the corporate veil. The duty of care exists directly between the plaintiffs and *Mr Rutherford*. That applies notwithstanding the separate obligations existing in contract between *Mr Rutherford's* company and client. It will not be in all cases in which a duty of care will be found to exist between a company director and the clients of the company. Each situation will depend upon its own facts as in any case of negligence, and it is only where there is a sufficient degree of proximity and harm is foreseeable that the individual director personally will be held to owe a duty of care. These separate liability of a director or other employee of a company that torts committed by him is not excluded simply because the company also is vicariously liable. Similarly the fact that the company may be liable in contract is no reason to exclude liability upon directors or employees for tortious acts.⁴³

Cooke P was of the view that while *Mr Ivory's* personal advice was very important to the client he was identifying himself with the company and providing that advice through the company in such a manner which could not give rise to a separate personal duty of care.⁴⁴

In the final judgment, *McGechan J* is also clearly of the opinion, after his analysis of *Fairline Shipping Corporation v Adamson*⁴⁵ that the touchstone for liability is whether or not there has been an 'assumption of responsibility' by

³⁹ *Trevor Ivory* [1992] 2 NZLR 517, 527.

⁴⁰ Relying upon *Sealand of the Pacific* (1974) 51 DLR (3d) 702.

⁴¹ *Centrepac Partnership v Foreign Currency Consultants Ltd* (1989) 4 NZCLC 64,940.

⁴² *Ibid* 64,951.

⁴³ *Ibid*.

⁴⁴ *Trevor Ivory* [1992] 2 NZLR 517, 524.

⁴⁵ [1975] QB 180 (*'Fairline Shipping'*).

the director even if given in the course of the company's operations.⁴⁶

The 'assumption of responsibility' test received endorsement in the House of Lords decision of *Williams v Natural Life Health Foods Ltd*.⁴⁷ Lord Steyn delivered a judgment which was supported by all four of the other Lords. His Lordship confirmed that the assumption of responsibility test is simply the application of the principles enunciated in *Hedley Byrne & Co Ltd v Heller*.⁴⁸ It seemed clear that for Lord Steyn a personal liability for a director of the company could only be found where it could be demonstrated that there was a special relationship between that director and the other party. The nature of the relationship that the plaintiff may have had with the company does not bear on this issue. It is how the director himself or herself has personally engaged with the plaintiff which must be considered to determine if they have so assumed responsibility in circumstances as to make them a primary tortfeasor.⁴⁹

The conclusion that must be drawn here from the *Trevor Ivory* case and the *Williams* case is that the focus of these courts has been upon finding personal liability for the director as a primary tortfeasor. In other words, it is a question of finding that the director has acted in such a way as it can be said that he or she has stepped out from behind the company and should be liable for their own acts because they have personally satisfied the requirements of the tort. It does not matter then that a company has been involved contractually because the director has brought the liability upon themselves by their own direct relationship with the plaintiff. The company in the *Williams* case was already held to be liable for the negligent advice under *Hedley Byrne*. Although the matter was not pleaded in the case, Lord Steyn considered this possibility of the director being a joint tortfeasor and found the argument unsustainable.⁵⁰

The House of Lords reviewed this decision again in *Standard Chartered Bank v Pakistan National Shipping Corporation [Nos 2 and 4]*.⁵¹ Lord Hoffmann, who had concurred with Lord Steyn in the *Williams*'s case, delivered the lead judgment. He confirmed the principles discussed above as having application to the tort of negligent misrepresentation. However, when the Court of Appeal in this decision had tried to apply the same principles to the tort of deceit, Lord Hoffmann confirmed how inappropriate this was.⁵² The director in this case was not being sued for the company's tort. It was simply a question of his own liability for fraud and the court should consider whether the elements of the tort could be proved against him. The assumption of responsibility test therefore was never meant to have general application to all torts. Its application, given its origins in *Hedley Byrne*, is to the potential liability for the giving of negligent advice or services. Its use is to determine whether it is appropriate to find a duty of care directly between a director (as

46 *Trevor Ivory* [1992] 2 NZLR 517, 529.

47 *Williams v Natural Life Health Foods Ltd* [1998] 2 All ER 577 ('*Williams*').

48 [1964] AC 465 ('*Hedley Byrne*').

49 *Williams* [1998] 2 All ER 577, 582, 584. Note however that it is seen as a question of finding the director liable as a primary tortfeasor rather than as a joint tortfeasor with the company.

50 *Ibid* 585.

51 [2003] 1 All ER 173.

52 *Ibid* 180.

a potential primary tortfeasor) and the party who has dealt with the company.

In Australia, McPherson JA in the Court of Appeal of the Supreme Court of Queensland in *Interchase Corp Ltd v ACN 010087573 Pty Ltd*⁵³ expressed ‘serious misgivings’ about the *Williams* case as well as others that followed it.⁵⁴ This case involved an action in negligence in respect of a valuation of real estate. The valuer who had carried out the valuation as an employee of Hillier Parker (Queensland) Pty Ltd was found not liable personally at trial. This is because the Court had followed the *Williams* case and had found that the valuer had not assumed personal responsibility for the valuation which, although signed by him, was provided in the name of the company. McPherson JA was very critical of this analysis.

Hillier Parker was held liable to Interchase in tort because Mr Waghorn was personally negligent in carrying out his valuation of the Myer Centre, for which Hillier Parker as his employer or principal was in law vicariously responsible to Interchase. Vicarious liability proceeds on the footing that the individual wrongdoer and the person who is vicariously liable are joint tortfeasors. To say that the principal or employer is legally responsible but that the actual wrongdoer is not, seems to me to be an inversion of the whole doctrine.⁵⁵

The whole question of how the tortious liability of directors or employees is categorised or framed is obviously so crucial when considering how the legal principles apply and how one case can be reconciled with another. In *Interchase* the Court of Appeal was clearly of the view that the employee in that instance was a primary tortfeasor as the person who provided the third-party plaintiff with the negligent valuation. His employer, was then also liable in tort, vicariously. In the words of McPherson JA, this means the employee and the employer company are joint tortfeasors. In *Williams* the court started with a different proposition. They started by accepting that the company in that case was already liable in negligence given its duty to the plaintiff. The question was whether the director also owed a personal duty to the plaintiff, a breach of which would mean he could be personally liable. For the House of Lords it was not a question of joint tortfeasance.

Arguably the fundamental difference in these cases is how the acts of the individual are perceived. In *Interchase*, the valuation by the employee is clearly seen as the personal professional act by that individual as agent for the employer company. The negligence by the employee is then seen as the primary tort liability and the liability of the employer company is vicarious. In *Williams*, the advice provided to the plaintiff through the acts of the director was seen as, the advice of and the act of, the company. Therefore the company had the primary liability in tort and the only question was whether or not the director should themselves also be liable, not as a joint tortfeasor, but because they themselves separately owed a personal duty of care. *Trevor Ivory*, like *Williams*, has as its foundation that the acts of the director were indeed the acts of the company. Again, on this basis the primary tortfeasor in negligence is the

⁵³ *Interchase Corporation Ltd (in liq) v Grosvenor Hill (Queensland) Pty Ltd* [No 3] [2003] 1 Qd R 26 (*Interchase*).

⁵⁴ *Ibid* 59 [77]. McMurdo P in this decision also indicated she was not persuaded that *Williams* [1998] 2 All ER 577 correctly states the law in Queensland: at 32 [9].

⁵⁵ *Ibid* 59 [77].

company. Perhaps the real criticism of *Williams* and *Trevor Ivory* should lie, not in a discussion about the competing interests of tort law and company law, but in the way in which the acts of the players are interpreted. If in these cases, the directors were seen as engaging in their own acts as agents for the company the result would have been quite different. The principles of tort law, as applied by McPherson JA to the employee in *Interchase*, would dictate that the director must be the primary tortfeasor and the company's liability is vicarious. The real question therefore must be the interpretation of the law that determines when a director's acts as agent can be seen as the acts of the company.

On the basis of this analysis, it is interesting to review the English decision following *Williams* in *MCA Records Inc v Charly Records Ltd*⁵⁶ and the subsequent appeal to the Court of Appeal (Civil Division) in *MCA Records Inc v Charly Records Ltd*.⁵⁷ In the case of the former, Rimer J, attempted to summarise when directors or employees could be liable for tortious acts. He found there were three circumstances. First, when the director or employee commits the tort themselves. Second, when the director or employee assumes a personal liability (consistent with the authorities of *Fairline Shipping*; *Trevor Ivory* and *Williams*). Third, when he or she procures and induces the company to commit the tort.⁵⁸ In his review of *Williams* he did not interpret Lord Steyn's discussion regarding joint tortfeasance by the company and the director as preventing the third type of liability.⁵⁹

In the Court of Appeal, Chadwick LJ, in the lead judgment, was supportive of Rimer J. Like Rimer J he thought it was impossible to read Lord Steyn's judgment in the *Williams* case as meaning that a director could never be liable as a joint tortfeasor with the company. He described four propositions as being supported by the authorities. The most significant however is the last.

[W]hether or not there is a separate tort procuring an infringement of the statutory right, actionable at common law, an individual who does 'intend, procure and share a common design' that the infringement should take place may be liable as a joint tortfeasor.⁶⁰

As will be discussed at the conclusion of this article, it appears the original purpose of this test in finding whether a director is the primary tortfeasor, has in many respects confused the development of the law in this area.

D The Root Quality test

The decision of *Root Quality Pty Ltd v Root Control Technologies Pty Ltd*⁶¹ came at a time when all of the earlier tests had been debated and considered for some years. Finkelstein J described the position at the time as follows:

Much has been written about the liability of directors and other officers for corporate wrongdoing. The cases present a confusing picture on an issue that has persistently

56 [2000] EMLR 743.

57 [2003] 1 BCLC 93.

58 *MCA Records Inc v Charly Records Ltd* [2000] EMLR 743, 751 [17].

59 *Ibid* 754 [21], 756 [24].

60 *MCA Records Inc v Charly Records Ltd* [2003] 1 BCLC 93, 117 [52].

61 (2000) 177 ALR 231.

vexed the common law. In recent years the uncertainty has increased partly by reason of divergent decisions and partly for other reasons.⁶²

This description is probably as apt today as it was then. Finkelstein J was of the opinion that to be a joint tortfeasor with a company the director must procure the corporation to violate the legal rights of another and considers this a separate tort based on the case of *Lumley v Gye*^{63,64}. He considered the authority of *Said v Butt*⁶⁵ and if applied this meant ‘a director or officer acting in that capacity could not be found liable for procuring his corporation to infringe the rights of another’.⁶⁶ He confirmed that *Said v Butt*⁶⁷ did indeed represent the law of Australia. The reason the director might escape liability, if only acting in that capacity, is that in those circumstances the acts of the director are actually the acts of the company.

So ultimately the question for Finkelstein J was when the director should lose his or her protection behind the company.⁶⁸ At what point would their conduct mean that they have themselves committed the tort of procuring the company to infringe the rights of another? As mentioned earlier, to answer this question he does seem to rely upon the *Mentmore* line of cases.

Finkelstein J seems to be supporting the added mental element from the *Mentmore* test that for a director to be liable personally he or she needs to have at least acted with reckless indifference as to the unlawfulness and harm that might be caused.⁶⁹

III Distilling and rationalising these varying tests into one set of key criteria

At the time of writing this article it has been 17 years since the last of the above tests arose (‘the *Root Quality* Test’). The Federal Courts however and at least one Supreme Court has had the opportunity to revisit the various tests and their elements and some significant headway has been made. However, as pointed out in the introduction to this article⁷⁰ the law is still unsettled. Even as late as 2015, although there had been considerable analysis of the issues, the Federal Court, at least on the face of it, was considering the application of the last three of the above tests (to the exclusion of the ‘direct or procure test’).⁷¹

Despite this continuing uncertainty the tests have been distilling and

62 Ibid 258 [115].

63 (1853) 118 ER 749.

64 *Root Quality* (2000) 177 ALR 231, 258 [118].

65 [1920] 3 KB 497.

66 (2000) 177 ALR 231, 262 [130].

67 [1920] 3 KB 497.

68 He considered in some detail the decision of *Trevor Ivory* [1992] 2 NZLR 517 but confirmed in reliance on *Banfield v Johnson* (1994) 7 NZCLC 260,496 that it should not be regarded as authority for the proposition that it will only be in the case of ‘an assumption of liability’ that a director or officer will be found liable for a personal tort: *Root Quality* (2000) 177 ALR 231, 265–6.

69 This was certainly the interpretation given to Finkelstein J’s judgment in *Allen Manufacturing* (2001) 53 IPR 400, 410 [40].

70 See discussion above in *Knights Capital* [2016] WASC 69 (4 March 2016) [57].

71 *Facton Ltd v XU* (2015) 111 IPR 103.

concentrating to reveal the key criteria. The first significant case to do so was *Keller v LED Technologies Pty Ltd*.⁷² This case provided a review of the tests and the first significant issue was the view that to be a joint tortfeasor there must be some mental element involved. Merely directing or procuring the company to act in his or her capacity as a director will not be enough. He or she must be doing something more which includes him or her in addition to the company as an invader of the victim's rights.⁷³ An example of this is where the director is using the company as an instrument for the infringement. That is, attempting to hide behind the corporate veil.⁷⁴ There was an endorsement also by Jessup J of the 'Mentmore test' with regard to the degree of knowledge required of the director before liability could ensue. 'A close personal involvement in the infringing acts by the director must be shown before he or she will be held liable. The director's knowledge will be relevant.'⁷⁵ In conclusion, Jessup J thought the director's liability required 'a dimension to his or her role which was separate from the good faith discharge of his or her duties in the service of the company. If so, there will be a basis, in accordance with general principles, for making the individual liable because he or she was involved in a joint, wrongful, enterprise with the company.'⁷⁶

So at least two key issues within the original tests were questioned and the development of this was taken up in *Sporte Leisure Pty Ltd v Paul's International Pty Ltd [No 3]*.⁷⁷ In reliance on *Keller*.⁷⁸ Nicholas J in the Federal Court confirmed the growing opinion that the 'direct or procure test' could not be applied literally.⁷⁹ In fact, if it had in that case, the relevant director would have been found liable but in the end he was not. He confirmed the necessity of the mental element of the director as in 'Mentmore' which he could not find in this case. But what level of personal knowledge and involvement is necessary? Personal involvement, in his opinion, was not a prerequisite to being a joint tortfeasor. 'Knowledge of a director that his or her company is invading another person's legal rights is something which may in a particular case be no less significant ...'⁸⁰ However, a director who held an honest belief that the relevant acts they performed for the company were not unlawful can be decisive.

It is rational to conclude to this point that directing or procuring acts, of itself, is not enough and that some extra level of knowledge and involvement must be present. *Taleb v GM Holden Ltd*⁸¹ continued in this vein. On appeal, in a joint judgment by Finn and Bennett JJ they referred to the questions asked in the original action to potentially find if the relevant director could be liable as a joint tortfeasor (the company was already determined to be liable) and apparently endorsed them. They were:

72 *Keller v LED Technologies Pty Ltd* (2010) 185 FCR 449 ('Keller').

73 *Ibid* 469 [83]–[84].

74 *Ibid* 469 [84].

75 *Ibid* 512–13 [291].

76 *Ibid* 543 [407].

77 (2010) 275 ALR 258 ('*Sporte Leisure*').

78 *Keller v LED Technologies Pty Ltd* (2010) 185 FCR 449.

79 *Sporte Leisure* (2010) 275 ALR 258, 279 [111].

80 *Ibid* 280–1 [115].

81 (2011) 286 ALR 309.

- (i) Did he have the necessary knowledge of the wrongs being committed by the company?
- (ii) Did he use the company as an instrument of his own wrong?
- (iii) Did he make the tort his own?
- (iv) Did he have a close personal involvement in the infringing acts of [the principal company tortfeasor]?⁸²

Arguably all these questions are on a scale that is simply being used to find that extra element necessary on top of ‘directing and procuring’. Presumably the answer, should it be found in the affirmative to any of them, could give rise to liability.

In *JR Consulting & Drafting Pty Ltd v Cummings*⁸³ while endorsing the ‘make the tort his own test’ the key legal principle to determine liability as a joint tortfeasor was put as follows:

[T]here must be a concurrence in the acts of both the company and the director causing the damage rather than coincidence of roles comprised of the company as an entity doing something and a director discharging duties as a director of the company doing that thing.⁸⁴

Significantly, after reviewing the authorities it was clear that a director;

must be shown to have directed or procured the tort and the conduct must, clearly enough, *go beyond* causing the company to take a commercial or business course of action or directing the company’s decision-making where both steps are the good faith and reasonable expression of the discharge of the duties and obligations of the director, as a director. The additional component required is a ‘close personal involvement’ in the infringing conduct of the company and inevitably the quality or degree of that closeness will require careful examination on a case by case basis.⁸⁵

Again, this endorses the need to go beyond merely ‘directing and procuring’ and the language of ‘close personal involvement’ incorporates this.

Similarly in *Knights Capital Group Ltd v Bajada and Associates Pty Ltd*⁸⁶ the language is enhanced by the view that a director could not escape personal liability if they became an ‘actor’ in the invasion of the plaintiff’s rights.⁸⁷ Again, it is merely a description that still goes to the heart of the issue, which is the level of knowledge and involvement. It is such a significant case however in the way it traces back this whole question of liability to the rule in *Said v Butt*.⁸⁸ Most importantly it recently confirms for us the following three things:

- (1) That we must accept the possibility of exceptions to *Said v Butt*;
- (2) That the scope of *Said v Butt* remains largely unexplored; and

⁸² Ibid 314 [18].

⁸³ (2016) 329 ALR 625.

⁸⁴ Ibid 686 [335].

⁸⁵ Ibid 689 [350].

⁸⁶ [2016] WASC 69 (4 March 2016).

⁸⁷ Ibid [68].

⁸⁸ [1920] 3 KB 497.

- (3) That outside of procuring or interfering with contractual relations a director can be personally liable for a tort committed by the corporation for such things as procuring a breach of trust, statutory duty, other wrongs.⁸⁹

[T]here may be room for further judicial exploration of the basis for, and the limits of, the rule in *Said v Butt* and the place of that rule within the common law's approach to the tort liability of directors more generally. Furthermore the test for determining when a director is involved in the company's tortious conduct ... so that the director may be found liable as a joint tortfeasor with a company, for torts committed by that company, is not settled.⁹⁰

There is one final case that deserves review. It puts into perspective the significance of this whole unsettled area of law and the debates above. It highlights the difference between the ability of an external party or client of a company being able to join a director with the company in a tortious action and an action based on the *Corporations Act* itself. *Australian Securities and Investments Commission v Cassimatis [No 8]*⁹¹ was essentially an action taken by Australian Securities and Investments Commission ('ASIC') against the two directors (and only shareholders) of a company for contravention of s 180(1) of the *Corporations Act*. That is, a breach of their duties of care and diligence.

The first important thing to note is that the action is taken by ASIC rather than an external client of the company where that third party joins the directors with the company as joint tortfeasors. This is a very interesting case in the way in which it considers the question of whether a breach of s 180(1) which has long been held as a private duty owed to the corporation, could also have a public character. Its public nature is said to be borne out by:

- (1) A public body prosecution which can result in remedies for persons affected by the conduct (including the external client);
- (2) Pecuniary penalties payable to the Commonwealth;
- (3) Disqualification as a director; and
- (4) The inability of the company to ratify the statutory breach.⁹²

Although not being able to resolve the question of the public nature of s 180(1)⁹³ there was clearly a view that the action could and would afford third party clients of the company that conducted dubious financial business practices appropriate remedies.

With respect, while all of this is true, the real issue is that such a breach of duty must be taken by ASIC or the company itself. The plaintiff client of the company as an external party would not have the locus standi to sue the directors directly for the breach of duty. ASIC may not choose to bring the action depending on its own assessment and resources. The company, particularly in this case where the directors and shareholders are the same would not bring the claim. Although in theory this could be overcome by a derivative action the third party client is not in a position to seek leave to do so.

89 *Knights Capital* [2016] WASC 69 (4 March 2016) [79]–[81].

90 *Ibid* [81].

91 (2016) 336 ALR 209.

92 *Ibid* 297 [457].

93 *Ibid* 299 [469], 301 [478].

If ASIC could be successful in such a claim the client may recover for their loss. But if the client can sue the company in tort and join the directors as defendants to that tort the corporate veil can be lifted and direct access gained to the directors' resources. This is but one reason why this matter must be resolved. Not only for the benefit of the third party but to allow directors some certainty in assessing their own risk in operating their corporate structures.

IV Conclusion: Suggesting a way forward to provide certainty for directors' own risk management

After consideration of all of the original tests, their applications and the varying language that has come from later decisions, it is suggested that we should simplify the steps in the judicial process as much as possible. It is proposed that those deliberations should be as follows:

(1) The court must first deal with the question of whether it could be a case of the director being the primary tortfeasor (rare on the basis of the analysis above) or whether the company has committed the tort but there is evidence to suggest the director may be joined in the action behind the company as a joint tortfeasor. The failure to make this clear initially or to make presumptions in this regard only added to the continuing confusion in the developments of the tests; particularly the 'make the tort his own test' and the 'assumption of responsibility test'. As even their names suggest, the norm would be liability for the company and it would take something special for a director to be considered the primary tortfeasor. But what if the test fails to find a liability for the director in this way? The impression given is an 'all or nothing approach'.

(2) How should the law then do the work of resolving if the director could still be a secondary joint tortfeasor behind the company? It is proposed the resolution requires two stages. The 'direct and procure test' should be the first step. It should not be considered however, as originally proposed to be, the only criteria to obtain a result. It cannot survive as a stand-alone test, at least in its literal form. Something more is needed. That is, a further degree of knowledge and involvement in the tort.

The second step therefore is consideration of what could meet this added requirement of knowledge of the unlawfulness of the act and involvement in the tortious act of the company which is now so plainly crucial. But the way in which the courts have considered these questions needs to be brought together. Arguably the slightly different language used and the circumstances of the particular cases has been key in causing confusion. Where the company is the primary tortfeasor, the question of knowledge, relationship with the company's acts and the director's intentions should be recognised within a scale of involvement that will raise liability as a joint tortfeasor. The court could draw on all of the case examples above, relevant to the particular circumstances of the case, to substantiate it. At the lower end of this scale, knowledge that the company is invading the rights of another (or perhaps even with reckless

indifference) may be enough in the relevant case and at the other end of the spectrum, deliberately using the company as the conduit through which the tort can be committed will definitely create the liability and will be seen as another example of the common law and equity legitimately raising the corporate veil.

(3) In this way we can prevent ongoing disputes of the merits of 'apparently' different tests and concentrate on bringing them together as examples of the one key question: Did the director direct or procure the company to commit the tort with a degree of knowledge and involvement recognised as causing liability within the scale above? Where one fits on that scale would obviously then be taken into account in the court's decision as to appropriate remedies.

Finally, the potential use of s 180(1) of the *Corporations Act* (should ASIC or the company be of a mind to do so) as a means by which public remedies might afford benefits to third parties is possible. However recognition of the rights of these third parties, in their own name, to sue directors as primary or joint tortfeasors is still powerful and real and must be added to the checklist directors should consider when using the corporate structure as a means of protecting personal assets.