



Curtin University of Technology

The Office of Ethics, Equity and Social Justice presents their

Annual Ethics Lecture

Justice, Business and Ethics:
In Search of Business Ethics

An Address by:

By the Hon David K Malcolm AC CitWA
Chief Justice of Western Australia

Bankwest Lecture Theatre

Curtin University of Technology

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Distinguished Guests

Ladies and Gentlemen

I was very pleased and privileged to accept the invitation of the Office of Ethics, Equity and Social Justice at Curtin University of Technology to speak to you on the topic: "Justice, Business and Ethics: In Search of Business Ethics".

It is a truism that ethical standards in any field of human endeavour are hard to define with any degree or precision. Most people have an intuitive, and largely shared, sense of when the line between ethical and unethical conduct has been crossed. Why should there be such agreement on matters which are, paradoxically, so difficult to pin down?

A dictionary will tell you that ethics are: "*A system of moral principles, by which human actions and proposals may be judged good or bad or right or wrong.*"¹ In an era of moral liberalism it is fashionable to say that there are no absolute principles by which conduct can be judged. In my view that flies in the face of our common experience. The reason that there is such a remarkable degree of agreement on the hallmarks of ethical conduct is its moral content. That common morality informs our day to day conduct and, to my mind, is undoubtedly based on fundamental and enduring principles of right and wrong.

¹ *Macquarie Dictionary* (1981) at 614.

Society only exists because of the basic acceptance of a set of rules. We regard it as a sign of a civilised society that murderers, rapists and robbers are a controllable minority rather than representative of the average members of society. Thus, the vast majority of citizens accept the rules represented by laws such as those against murder, rape and robbery. Similarly, the vast majority accept that in Australia we drive on the left hand side of the road. We have enough accidents as it is. But imagine the chaos on the roads if everyone were free to drive on whatever side they chose.

The laws which members of society accept and obey are the very fabric which holds the society together. They are like the reinforcing in concrete. Without the reinforcing, the concrete would shatter and disintegrate under pressure. Without laws which are generally accepted and obeyed our society would similarly disintegrate. A democratic society depends upon acceptance and observance of what is called "the rule of law". Without that we would have either tyranny or anarchy. The degree of acceptance and observance of the law is closely linked with the acceptance and observance of the basic moral or ethical values reflected in the law.

Since the "big R" recession of the 1990s and, more recently, the spectacular collapses of high-profile Australian companies HIH and One.Tel, WorldCom and Enron in the United States, and the recent public outcry over "golden handshakes" payments to outgoing CEO's, much has been said and written about the alleged lamentable standards of business ethics revealed in an examination of some of the corporate successes and failures of the recent past. In many instances it has been suggested that the pursuit of profit has led to a tendency to focus only on the bottom line, on the ends rather than the means. Speaking generally, on the basis of reported allegations in the financial press and elsewhere, one gets the impression that some people in business have adopted the view that "If it's legal it's alright" or "If we can get away with it, it's alright."

There are said to have been occasions when commercial reality has been camouflaged by "creative accounting". There are also said to have been occasions when year-end results have been achieved by last-minute round robins or cheque swaps, off-balance sheet transactions and the like. There are said to have been many instances of inflated management fees and loans to directors or their associated companies as well as insider trading. Reference has been made to "four-on-the-floor" entrepreneurs, presumably so-called because their commercial driving habits have involved cutting corners, weaving in and out of the traffic, seeing an orange light as merely a signal to accelerate and regarding a speed limit only as a means by which the average driver is compelled to drive slowly and leave room for them to speed in the fast lane.

We may sometimes be tempted to think that these problems are of a kind more likely to occur elsewhere in Australia or overseas, but not in Western Australia. The experience of the 1990s certainly put paid to that idea. It was probably based on the comparatively isolated character of Perth as a commercial centre. Between 1983 and February 1987 Perth had become known internationally as "The Home of the America's Cup". Before that it was known commercially only to a comparatively select few. In a case in which I appeared before the Privy Council in 1984, involving two Perth businessmen this point was brought home to me. My opponent, a very bright London commercial barrister, in an argument described by the judgment as of "conspicuous ability", was unkind enough to invite their Lordships to take judicial notice of the "notorious fact" that Perth was the most remote English-speaking commercial centre in the world.

There is no doubt that Perth produced a number of corporate high flyers who have attracted considerable media attention in the 1980s and 1990s. The State is still dealing with the results of some of their dealings long after the demise of the companies concerned. Whether Perth produced more than its fair share of such persons I do not know. Other financial centres such as New

York, London, Sydney, Melbourne and Brisbane seem to have produced a fair representative sample of high flyers. In all of these centres there have been instances of alleged illegal and unethical business behaviour in the same period. Some allegations have been proved in court. Others have led to various persons being charged who await trial. Naturally, my comments are not directed at any pending or potential proceedings in the courts of this State. All of those involved are entitled to the benefit of the presumption of innocence and are entitled to a fair trial without preconceptions.

The Deputy Chairman of the Australian Securities Commission, Charles Williams, quoted in 1993² the following passage from John Kenneth Galbraith's *The Great Crash*:

“At any given time there exists an inventory of undiscovered embezzlement in - or more precisely *not* in - the country's businesses and banks. This inventory - it should perhaps be called the bezzle - amounts at any moment to many millions of dollars. It also varies in size with the business cycle. In good times people are relaxed, trusting, and money is plentiful. But even though money is plentiful, there are always many people who need more. Under these circumstances the rate of embezzlement grows, the rate of discovery falls off, the bezzle increases rapidly. In depression all this is reversed. Money is watched with a narrow suspicious eye. The man who handles it is assumed to be dishonest until he proves himself otherwise. Audits are penetrating and meticulous. Commercial morality is enormously improved. The bezzle shrinks.”

Against this background it is hardly surprising that there should have been steps taken to improve the standards of commercial morality and business ethics in our community. This does not mean that *all* business or *all* businessmen fail to observe proper standards of commercial morality or are unethical. Far from it. It does mean, however, that in order to raise the general level of observance of appropriate standards, some form of action is

² (1993) 3 ASC Digest, SPCH 53

required. At the same time, it is important to remember that there are many, many people in business who do observe proper standards of commercial morality and business ethics.

What action is required? First, we need business and commercial leaders who lead in the right direction by their personal example. Secondly, we need to educate and inculcate in those in business and those who deal with them proper standards of commercial morality and business ethics. Thirdly, we need to have the necessary apparatus and resources to detect, expose and punish those who fail to observe the basic standards of honesty and due diligence required and to deter others from doing so.

Let me first say something about leadership. A person who is a leader in the community is primarily a person who by his words and actions guides and persuades others to adopt, follow or at least respect his or her views. This may be done by reasoned argument, but it may well also be done by propaganda so as to confuse images and perceptions with reality. The best form of leadership is that which shows the way by being out front and encouraging others by example. "Do as I do" is more effective than "Do as I say". In today's language our community, especially children, teenagers and young adults, needs leadership by role models. The same is true of business.

Leaders who are perceived as shallow, hypocritical pretenders will not do. This was clearly the case in the HIH inquiry. Owen J went to great lengths to point out that, while the Royal Commission did not uncover acts of gross fraud and embezzlement, it did uncover a corporate culture which placed undue reliance on the vision and strategies of the CEO, without the imposition of the necessary checks and balances by the Board. In his findings, Owen J said:

“The problematic aspects of the corporate culture of HIH – which led directly to poor decision making – can be summarised succinctly. There was blind faith in a leadership that was ill-equipped for the task. There was insufficient ability and independence of mind

in an associated with the organisation to see what had to be done and what had to be stopped and avoided...Unpleasant information was hidden, filtered or sanitised. And there was a lack of sceptical questioning and analysis when and where it mattered.”³

There is a great need in every aspect of life, whether in politics, the professions, business, education, science, sport and entertainment for leaders who use their capacities to earn the respect and admiration of others and use their talents wisely to give the rest of us a good example and good ideas to follow. Service above self and a clear definition of what is right and what is wrong, as well as an ability to act and persuade in terms of the definition, are the essentials of leadership.

Reference to the need for a definition of what is right and what is wrong immediately takes me into the realms of ethics and morality. The word "ethics" is a difficult word because it means different things to different people. The term "ethics" is often used to refer to professional ethics as incorporated into ethical codes of conduct adopted by professional associations, such as the Australian Medical Association and the Law Society or Bar Association. In this respect I note that it was reported⁴ in 1993 that a survey had identified 143 individual companies and government enterprises which had produced ethical codes. During 2002, the Australian Institute of Directors increased numbers attending its company directors' course, which covers corporate governance, by 54 per cent to a total of about 2000. Courses were fully booked and there was at least a two-month waiting list.

We also refer to "ethics" to refer to the particular values or standards of a particular sect or group. For example we may refer to Christian or Jewish ethics. In another sense reference is often made to "ethics" in the context of the standards of a group as a whole. Hence, the accusation that Australians

³ Owen J (2003), *The failure of HIH Insurance*, Volume 1 at xvii

⁴ (1993) 3 ASC Digest, SPCH 55

have lost the "work ethic" refers to the alleged decline in Australia in the moral value placed upon work and the possession of secure employment.

There is obviously a close connection between ethics and morality. An "ethical" businessman is one whose honesty and integrity may be relied upon. That is because those who deal with him or her do so with trust and confidence. People do not want to do business with a con-man or a con-woman. It is ironic that the use of "con" in this connection is short for "confidence" as in "confidence trick". There will always be confidence tricksters, but their task is made harder in a context where there is a high level of ethical conduct in business.

"Ethics" is a branch of philosophical knowledge which involves a study of the principles of morality, of right and wrong conduct, and of good and bad, virtue and vice as they relate to behaviour of men and women or even groups or whole societies. In this context things begin to get complicated because we make distinctions between public and private morality.

One thing is clear, however. Morality is concerned with standards of conduct and values. Honesty is good, fraud is bad. The concept of the sanctity of human life is a value reflected in the biblical commandment "Thou shalt not kill". Respect for the property rights of others is a value reflected in the commandment "Thou shalt not steal".

How important is the adherence of the members of society to common standards and values? Anthropologists would say that any group of people who share common beliefs and values about what is right and what is wrong can, in general, live in peace and harmony with one another. A group of people who do not share such common beliefs and values will have difficulty in living in peace and harmony with one another. The existence of a cohesive society requires a community of ideas. Thirty years ago Lord Devlin, an English Judge, said:

“I return to the statement that I have already made, that society means a community of ideas; without shared ideas on politics, morals, and ethics no society can exist. Each one of us has ideas about what is good and what is evil; they cannot be kept private from the society in which we live. If men and women try to create a society in which there is no fundamental agreement about good and evil they will fail; if having based it on common agreement, the agreement goes, the society will disintegrate. For society is not something that is kept together physically; it is held by the invisible bonds of common thought. If the bonds were too far relaxed the members would drift apart. A common morality is part of the bondage. The bondage is part of the price of society; and mankind, which needs society, must pay its price.”

This is not to say that a common morality must be accepted by every member of society and that there is no room for legitimate differences. The degree of cohesion, however, must necessarily be related to the degree of agreement about morals. A recognised morality is as necessary to society as a recognised government. This recognised morality may be regarded as public morality. Thus the criminal law by prohibiting murder, rape (now called sexual assault), robbery, burglary, fraud and car theft on pain of punishment enforces adherence to the standards the community requires. These are the cases where society asserts the right to pass judgment on matters of morals and to use the weapons of the law to enforce that judgment.

It is difficult to divorce morality from religion, but it must be recognised that while Western Society derives much of its moral standards from the Christian and Jewish religions, morality has an existence apart from religion. What is important, however, is that morals and values do not have an independent existence. We are not born with a set of morals and values. They are things which have to be learned. This means that they have to be taught. In times past they were taught in churches and schools and what was learned by parents in this way was also passed on to their children.

In Australia, statistics show that church attendance and religious observance and contact has tended to steadily decline. Hence, less and less

children have been exposed to morals and values as taught by the churches. Religious instruction is no longer included in the curriculum of government schools. I have no clear picture of the extent to which teachers in government schools already teach morals and values. My suspicions incline me to be pessimistic. The anti-judgmental movement in education in government schools has led to a great reluctance on the part of many educators to get involved in the consideration of ethical issues or criticise behaviour on purely ethical or moral grounds. Successive generations of parents have passed on less and less in terms of moral values to their children.

These are of course broad generalisations. As such they may be misleading. There are many exceptions. The reality must be faced, however, that in the last thirty years there has been a rise in the acceptance of wide variances in private morality and the assertion of individual freedom of action. This is particularly so in relation to books, films and videos for example. There has been a much greater emphasis on the rights of the individual with correspondingly less emphasis on the obligations of the individuals to others or to society as a whole. At the same time, public morality remains as a necessary element in the preservation of society in terms of law and order. For the purposes of the law the standard remains the standard of the reasonable person. Immorality is that which a reasonable person would consider to be wrong. In making the necessary judgment it is necessary to strike a balance between the public interest of society as a whole and the private interest of an individual.

Education in ethics is vital. It is as vital for directors and managers of public companies as it is for doctors, lawyers and accountants. Organisations such as the Australian Institute of Directors have recognised this. Unlike the medical and legal professions, however, directors' professional qualifications and standards of professional behaviour are not subject to review by a professional disciplinary body which polices a professional code of conduct.

The activities of company directors are subject to review by auditors and by the Australian Securities Commission (ASC), formerly the National Companies and Securities Commission (NCSC).

In 1990 there was a significant development in the educational area in Western Australia. There was introduced into the business management course at Curtin University an optional unit in ethics. One third of the students enrolled. The course is now compulsory.

Education in the appropriate standards to be observed and the establishment of an appropriate regulatory body modelled on those of other professions, to monitor and supervise the observance of those standards by public company directors and managers, are positive steps required in this field. Due to recent company collapses, coupled with demand for greater scrutiny and transparency from shareholders and investors, the need for a graduate course in corporate governance and directors' duties has grown significantly.

Leadership and education alone are not enough. They must be backed up by appropriate laws and properly funded and resourced law enforcement. The law is a powerful instrument for regulating behaviour in society. The mere existence of a law, however, is not enough. A law which simply declares that it is an offence to be dishonest, or not to take reasonable care of the money or property of others will be no more effective than a law which declares that good behaviour is compulsory.

It has long been a part of company law that directors are required to be honest and diligent in the performance of their duties as company directors. These obligations are spelled out in s.180, of the *Corporations Act 2001* (Cth). Directors who breach these duties are liable for any loss or damage caused to the company and liable to account to the company for any profits earned by them as a result of the breach.

As part of the Federal Government's Corporate Law and Economic Reform Program, commonly referred to as CLERP, many of the lessons learnt from past corporate failure were incorporated into the new *Corporations Act*, including many of the 61 policy recommendations made by Owen J in the HIH Report. In specific relation to directors' duties and responsibilities, CLERP 9 sets the scene for a new corporate governance framework. The draft Corporate Law Economic Reform program (Audit Reform & Corporate Disclosure) Bill was released on 8 October 2003 and is expected to commence from 1 July 2004. CLERP 9 represents a concerted effort towards reforms, namely to avoid conflicts of interest, by addressing the recent problems with auditors who also hold positions on various boards, and encouraging executives to maintain an open dialogue with shareholders to promote transparency.

In the wake of recent spectacular corporate collapses, a new catchphrase has become associated with ethical responsibilities in the corporate world – "Corporate Governance". Corporate Governance is all about accountability and stewardship. One critical objective of a system of corporate governance is to ensure that those in whom responsibility is vested to control and direct the business of a corporation hold the confidence of those having a stake in the success of the business. In the HIH Report, Owen J referred to a *Code of Best Practice*, derived from a UK model, which enunciated the principles clearly:

"The principles on which the Code is based are those of openness, integrity and accountability. They go together. Openness on the part of companies, within the limits set by their competitive position, is the basis for the confidence which needs to exist between business and all those who have a stake in its success. An open approach to the disclosure of information contributes to the efficient working of the market economy, prompts boards to take effective action and allows shareholders and others to scrutinise companies more thoroughly.

Integrity means both straightforward dealing and completeness. What is required of financial reporting is that it should be honest and that it should present a balanced picture of the state of the company's affairs. The integrity of the reports depends on the integrity of those who prepare and present them.

Boards of directors are accountable to their shareholders and both have to play their part in making that accountability effective. Boards of directors need to do so through the quality of information which they provide to shareholders, and the shareholders through their willingness to exercise their responsibilities as owners"⁵

The need for transparency at the highest level of the business chain has never been more critical, and this is reflected in the mounting public outcry over what is being perceived as "golden handshake" deals for outgoing CEOs. To put it into perspective, at the same time that the Australian Council of Trade Unions ("ACTU") campaigned for the minimum wage to be increased by an extra \$10 per week for Australia's lowest-income earners, tens of millions of dollars were being paid to outgoing top executives who were already paid a handsome salary. In the last financial year, the annual average salary for the top 100 Australian CEOs had increased from \$1.45 million to \$2 million, a 38% increase.

The justifiable reason for the outrage behind the "golden handshake" deals is that at least some of the CEOs were actually leaving companies because of their lack of success, sometimes leaving the company in a much worse state than when they arrived. During 2002, few of Australia's highest-paid executives actually increased shareholder wealth, yet CEOs and boards of a number of large corporations still received large financial rewards and incentives. Some companies' share prices decreased during the reign of the incumbent CEO, and increased upon their departure. It is easy to perceive the perverse assumption that they were being *rewarded* for their failure! This is

⁵ Owen J (2003), *The failure of HIH Insurance*, Volume 1, p.102

not the position our society should be in, nor an image which big businesses should wish to project.

The HIH Royal Commission Report is littered with references to shady accounting practices, and instances of the board not running sufficient checks and balances on risky projects. In one instance, from time to time the chief executive intermingled his own personal funds with corporate funds in the company's bank account. This was done with no reasonable explanation and no disclosure to shareholders. Another ethical anomaly revealed was the adoption of accounting and auditing practices by the company and its accountants, which managed to disguise the true situation when the company had massive debts and was basically trading whilst insolvent. From an outside perspective, and as was ruled by Owen J, it did not appear to be appropriate that there were members of the board who were also current or former partners of the company's designated auditors.

Unfortunately, in many instances, unless the unethical or illegal activities of company officers come to the attention of external authorities, the decision whether to take action in any case rests with the board of directors themselves. The lack of resources and personnel of the NCSC made detection, exposure and successful legal proceedings by the NCSC unlikely. In some instances this led the Commission to attempt public exposure by the release of information to the media. The frustrations which led to this were understandable, but the attempts were misguided for two reasons. First, they represented a departure from the fundamental principles of our criminal law relating to the presumption of innocence, the right to a fair trial and the undesirability of trial by media rather than trial by jury. Secondly and, perhaps, more importantly, such attempts made it widely known that the NCSC did not have the funds or resources to successfully enforce the relevant provisions of the *Companies Code* and that others were encouraged to believe

that they might also get away with breaching them. Hence, it is essential that the ASC is able to demonstrate that it has been adequately resourced and funded in the area of supervision, detection, enforcement and prevention of breaches of the *Corporations Law*. Certainly the level of funding of the ASC has to date been higher than that of the NCSC.

Although there have been criticisms levelled at the ASC, its programmes of prosecutions and civil litigation have generally been successful, though not without flaws. It appears that the ASC is increasingly turning its attention to the prevention of corporate crime. The balance is shifting from punishment to surveillance. It is hoped that the increased surveillance will act as a deterrent to corporate crime.

Section 180 of the *Corporations Act 2001* (Cth) provides that:

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

It has been said repeatedly that the duty to act honestly involves a duty to act in good faith. Directors are required to act in good faith in the interests of the company. The duty of honesty or good faith has a number of aspects under the general law. First, the directors must exercise their powers in the interests of the company; they must not misuse their powers. Secondly, they must avoid conflicts between their personal interests and those of the company. Thirdly, they should not take advantage of their position to make secret profits. Fourthly, they should not misappropriate the company's assets for themselves.

All powers and duties of directors were said to be fiduciary because the directors are agents of the company⁶. This means that a power may be exercised only for the purpose for which it has been conferred and not for any collateral, improper or unauthorised purpose. Where the exercise of a power is abused by exercising it for some collateral, improper or unauthorised purpose, such abuse is said to involve a "fraud on the power". The amendments proposed to the *Corporations Law* in 1993, in my view, did not change this aspect of the law in any respect. Even though it was amended to reinforce the officer's duty of care as an objective one, it was acknowledged by the Attorney General at the time that this would not effect any significant change in the law which the Western Australia Courts had been following. It was accepted that directors and officers should not be liable for honest errors of judgment or business judgments taken in good faith.

The CLERP Act introduced a new statutory business judgment rule. From a business perspective, this offers directors protection from personal liability in relation to honest, informed and rational judgments, within its actual sphere of legal operation. Under section 180(2), a director or other officer of a corporation will be taken to have met the requirements of the duty of care and diligence in respect of making a business judgment if:

- The judgment was made in good faith for a proper purpose;
- The director or other officer did not have a material personal interest in the subject matter of the judgment;
- The director or other officer informed themselves about the subject matter of the judgment to the extent they reasonably believed to be appropriate; and
- The director or other officer rationally believed that the judgment was in the best interests of the corporation.

⁶ *Richard Brady Franks Ltd v Price* (1937) 58 CLR 112 at 142

It is interesting to note the test relating to “best interests of the corporation”. It is presumed that a director’s belief, that the relevant business judgment is in the best interests of the corporation, is a rational one unless the belief is one that no reasonable person in the position of the director would hold. Given the recent past performances of some high-flying corporate cowboys, one may query if we would be able to find the “reasonable person in their position” with which to draw a comparison.

The duties I have referred to have long been the duties of directors and senior management of companies. The re-enactment of the legislation, even with increased penalties under Part 9.4B is not enough. In their essentials, these provisions have been part of the law for many, many years. The mere existence of the prohibitions and the provisions for recovery of loss and damage, such as those now found in Part 9.4B of the *Corporations Law* have proved inadequate in changing the attitudes of some company directors.

A combination of leadership, education and law enforcement can change attitudes. In the 1970s what was seen as a repressive and inequitable tax regime in Australia led to the proliferation of tax minimisation, avoidance and evasion. The artificiality of many of the schemes which were packaged and marketed over these years, and the enthusiasm with which they were embraced, indicated a significant decline in the standards of "tax morality" of the community. The introduction of what many perceived as draconian anti-avoidance legislation, much of it having retrospective operation, caused an outcry. The devotion of substantial resources to enforcement and the erection of a policy based upon assess and pay and ask questions later was also criticised. This tough approach did much to change the "tax morality" of many Australians. It might be going too far to say that people now believe that it is part of their civic duty to pay their fair share of tax and that tax avoidance is undesirable, but it is a view commonly expressed.

As in the case of the tax avoidance legislation, the law may sometimes impose a standard of behaviour higher than that currently being observed in the community. That is a function of democratic government achieved by Parliament enacting the legislation. There may be areas where the legal obligation falls short of the related moral obligation. The law and morality do not necessarily coincide in content. As Professor Paul Finn has said:

“...the law, including commercial law, does not track systematically even at a distance the imperatives of morality, conventional and otherwise. Moral values (and contentious ones at that) can and do manifestly inform the law. They are not its master. Illustrative of this is the very obvious truism that legal censure does not as of course parallel moral censure.”⁷

No doubt there are many cases in which the legal obligation falls short of the moral imperative. In the context of commercial and company law, however, the courts have recognised the need for a closer parallel between moral or ethical values and the content of the law. As the former Chief Justice of the High Court, Sir Anthony Mason, has pointed out⁸ there has been a growing awareness, particularly in appellate courts, of the need to develop the common law to meet "Australian circumstances, needs and values". At the same time, there has been a change in the attitude of the courts to the standards of conduct expected of parties in their business and commercial dealings. This has been demonstrated in a series of decisions in the High Court of Australia since 1983. I was prompted by some of those to write a paper in 1987 titled *The Penetration of Equitable Principles into Modern Commercial Law*, which was published in the Australian Bar Review⁹. In

⁷ Finn, (1989), *Commerce, the Common Law and Morality* 17 MULR 87

⁸ Mason, (1988), *Australian Contract Law*, *Journal of Contract Law* 1

⁹ Malcolm, (1987), *The Penetration of Equitable Principles into Modern Commercial Law* 3 Aust Bar Rev 1 185

retrospect the title might well have been *The Penetration of Ethical Principles into Modern Commercial Law*.

Professor Paul Finn has traced the origins and assessed the significance of this development in the article *Commerce, the Common Law and Morality*, above, from which I have already quoted. In the nineteenth century the doctrine of freedom of contract rode high, wide and handsome and permitted the pursuit of self-interest, subject only to fraud, duress and a limited degree of equitable intervention. Superior knowledge and superior power were simply advantages to be exploited. *Caveat emptor* or "let the buyer beware" reflected an idea that was pervasive. In the law of tort fraudulent misrepresentation attracted a remedy in damages but not negligent misrepresentation. Non-disclosure rarely attracted a remedy. The scope of actions for damages for nuisance and negligence was relatively narrow.

The twentieth century has seen accelerating change leading to an entirely new approach. In *Nicholson v Permakraft (NZ) Ltd*¹⁰, Cooke P (Sir Robin Cooke, President of the New Zealand Court of Appeal) said that legal obligations are being asked to match "the now pervasive concepts of duty to a neighbour and the linking of power with obligation". This is a reflection of the decision in *Donoghue v Stephenson*¹¹, which was until recently the basis of the modern law of negligence. In that case Lord Atkin said at 580:

“The rule that you are to love your neighbour becomes in law you must not injure your neighbour; and, the lawyers question, 'Who is my neighbour?' receives a restricted reply. You must take care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour.”

The moral and ethical foundation for Lord Atkin's formulation of the test for the existence of a duty of care is clear.

¹⁰ (1985) ACLC 453 at 459

¹¹ (1932) AC 562

The decisions of the High Court in the last twenty years dealing with unconscionable conduct, equitable estoppel, relief from forfeiture, unconscionable reliance on contractual rights, penalties and other matters suggest that a requirement of good faith and fair dealing may have replaced the moral abstinence of the legal doctrines of the nineteenth century. This may reflect the fact that the nineteenth century approach rested on an assumption of community observance of general standards of behaviour making legal intervention unnecessary and a realisation that the assumption is no longer valid. Thus, to quote Professor Finn again, (*op cit* at 92):

“As a legal idea 'good faith and fair dealing' (or neighbourhood if you like) is rich in moral connotation. Its emphatic concern is regard for others. And its contemporary effects are many. First, and a superficial point: it is having a very direct impact upon the language of the law itself. One need only note the growing currency of terms such as 'unconscionable conduct', 'basic fairness', 'the fair and reasonable man', 'reasonable expectations', 'reasonable reliance', 'the protection of legitimate interests', 'unfair detriment', 'unjust enrichment' and the like. The evocative, and morally judgmental, adjective is with us.

Secondly, more substantially, we are witnessing new and heightened standards of conduct being imposed as commonplace.”

It may well be argued that as general standards of the observance of moral imperatives have declined, so the common and commercial law has developed in order to counteract that decline. In the United States, for example, *The Restatement (Second) of Torts*¹² states that is an actionable wrong for a party to a "business transaction" to fail to disclose:

“...facts basic to the transaction, if he knows that the other is about to enter into it under a mistake as to them and that other, because of the relationship between them the customs of the trade or other objective circumstances, may reasonably expect him to disclose.”

¹² (1977), s.551(2)(e)

The justification of this is that "the continuing development of modern business ethics has... limited to some extent (the) privilege to take advantage of ignorance"¹³. Duties of disclosure have been held in Australia to arise in contract formation, equitable and common law estoppel, deceit and negligence. A dramatic example in the case of estoppel was *Waltons' Stores (Interstate) Ltd v Maher*¹⁴. Section 52 of the *Trade Practices Act 1974 (Cth)* is probably the most powerful of the potential weapons in this area.

As the decision of the High Court in *Commercial Bank of Australia Ltd v Amadio*¹⁵ demonstrates, circumstances may give rise to a duty on the part of a businessman to recommend that a party with whom he is in negotiation obtain independent advice, or at least to a duty to give a full explanation of the implications of a transaction. If the duty is not fulfilled the transaction may be set aside as unconscionable. Similarly, circumstances may give rise to a duty to have regard to the legitimate interests and reasonable expectations of others. These can occur in relation to a mortgagee exercising a power of sale, the treatment of minority shareholders by the majority and the exercise by a franchisor of discretionary powers regarding a distributorship or franchise. The law seems to have set its face against unconscionable conduct, so that there may be circumstances where it would be unfair or unjust for one party to a contract to insist on his or her legal rights. This has been demonstrated in the cases against relief against forfeiture and the exercise of rights of contractual termination as in *Legione v Hately*¹⁶ and *Stern v McArthur*¹⁷.

In all of these cases there has been a close analysis of the relationship between the parties, the extent to which one of them has reasonably relied on the other, or the extent to which one of them has created a reasonable

¹³ *Ibid*, comment 1 at p.124

¹⁴ (1988) 164 CLR 387

¹⁵ (1983) 151 CLR 447

¹⁶ (1983) 152 CLR 406

¹⁷ (1988) 165 CLR 489

expectation in the mind of the other. This approach is similar to that adopted in the context of the law of negligence in determining whether there was a duty of care: *Sutherland Shire Council v Heyman*¹⁸; and *San Sebastian Pty Ltd v Minister Administering Environmental Planning and Assessment Act 1979*¹⁹. The thrust of the change is to place curbs on the exploitation of superior knowledge or superior bargaining power to the disadvantage of the vulnerable.

At a symposium on *The High Court: A Reflective View* held at the University of Western Australia in 1993, Associate Professors Carter and Stewart commented, in their paper *Commerce and Conscience: The High Court's Developing View of Contract*²⁰:

“The particular concern of the [High] Court over the past decade in contract litigation has been to promote the concept of unconscionability. It has been made clear that unconscionable conduct is the pivot on which the concepts of estoppel and relief against forfeiture turn. Similar considerations have been used to justify the adoption of unjust enrichment as a unifying legal concept which both explains why the law recognises, in a variety of contexts, an obligation on the part of a defendant to make fair and just restitution for a benefit derived at the expense of a plaintiff, and also assists in determining whether the law should, in justice, recognise such an obligation in a new or developing category of case...”

Associate Professors Carter and Stewart also refer to Article 27 of the Victorian Law Reform Commission's proposed *Australian Contract Code*, which provides:

“A person may not assert a right or deny an obligation to the extent that it would be unconscionable to do so.”

Unconscionability is to be judged "by reference both to the values of the wider community and to the accepted morality of the particular environment in which

¹⁸ (1985) 157 CLR 424

¹⁹ (1986) 162 CLR 340

²⁰ at p.54

it occurs". Although this has not become law, it is an indication of the way in which legal thinking is changing.

An article in the University of New South Wales Law Journal²¹ raised the issue of "corporate social responsibility", which brings the issue of ethics into the realm of the artificial entities which are controlled by persons. The concept may require corporate managers to consider non-profit, non-shareholder or broader social interests in decision making. Such interests include, typically, consumer and environmental interests. This brings to mind the new corporate accountability system known as "the Triple Bottom Line". The three bottom lines refer to economic, environmental and social performance, and forces the board of a company to take accountability beyond finance and consider the wider implications of the impact of their activities on the environment, the community and human rights. Dealing with companies who do not support child labour is one example of an ethical consideration which will benefit the company in the long-term, by way of improving it's image in the eyes of the community, but is not directly reflected in the financial statements.

Arguments about corporate social responsibility have been continuing in the United States since 1932. An example of the operation of corporate social responsibility is provided by the American Central Maine Power Company, which works to reduce demand for electricity rather than provide more. To industry and commerce, the largest users of electricity, it offers rebates to encourage the installation of energy efficient lights and motors and it provides energy efficiency design advice and energy audits, among other things. As a result of the decreased demand for electricity its profits were reduced but, after convincing local regulatory authorities to remove disincentives to energy efficiency, it began to make money from its programmes. As well as ethical

²¹ Tolmie, J, [1992], *Corporate Social Responsibility*, 1 UNSW Law Journal 268

issues, the concept of corporate social responsibility involves many policy and philosophical issues which time does not permit of consideration in this lecture.

These developments in the law and in legal thinking are a reaction to an identified need. The necessity for them will only be reduced by a sea change in the general approach to business ethics through inspirational leadership by example, education, professional development and self-regulation by public company directors and managers, backed up by comprehensive and comprehensible laws which are enforced by competent, properly funded and resourced administrators.

In Australia we have developed ideas of freedom based upon the concepts of rights. The focus on rights tends to overlook the relationship between freedom and responsibility and between rights and duties. This has led to less emphasis on the obligations of individuals to others or to society as a whole. It seems to me that we have an enormous task in lifting the level of awareness and respect, not only for moral values but also for the obligations of a citizen to other members of the community and to the community as a whole. Charles Williams, Deputy Chairman of the ASC, in closing an address some 10 years ago²² had the following message for industry, professional bodies, regulators and individuals. He quoted from Dietrich Bonhoeffer's *Ethics*²³, which summed up the characteristics of the responsible person who:

“...acts in the freedom of his own self, without the support of men, circumstances or principles, but with a due consideration for the given human and general conditions and for the relevant questions of principle. The proof of his freedom is the fact that nothing can answer for him, nothing can exonerate him except his own deed and his own self. It is he himself who must observe, judge, weigh up, decide and act. It is man himself who must examine the motives, the prospects, the value and the purpose of his action. But neither the purity of the

²² (1993) 3 ASC Digest, SPCH 62

²³ Macmillan, New York, 1955

motivation, nor the opportune circumstances, nor the value, nor the significant purpose of an intended undertaking can become the governing law of his action, a law to which he can withdraw, to which he can appeal as an authority, and by which he can be exculpated and acquitted. For in that case he would indeed no longer be truly free.”

In the field of business, as in so many other fields, it is also important to develop a broad consensus about moral and ethical standards of behaviour. The interests of society as a whole require limitations upon the pursuit of purely private interests. Striking the balance between private interests and the interests of society as a whole requires an exercise of judgment. In government, judgments of this kind must be made by Cabinet and Parliament on questions of policy when considering calls for a law to be passed regulating some activity. Debates about prostitution, homosexuality, abortion, imprisonment, in vitro fertilisation and other issues involving the interaction between law and morality, all involve the making of moral judgments. Because we live in a democracy we insist that no great decisions should be made in these areas without debate. The law should only be required to enforce morality where it is necessary for the protection of society. We must not forget that in a modern democracy sensitive to individual civil liberties, there should be toleration of the maximum individual freedom that is consistent with the integrity of society. The law should only be used to enforce those standards where the departure from them is beyond the limits of tolerance. It is not enough to say that a majority dislike a certain activity. The activity must be one deserving of condemnation and productive of indignation, or even disgust, before society should make a judgment of prohibition on pain of punishment.

In the context of business ethics, however, what is important is to promote codes of behaviour or conduct which will encourage the development of relationships built on trust, confidence, reliability and integrity. In short we are seeking to develop relationships built on good faith and fair dealing. The

search for improvement in business ethics should now be on the agenda of every business looking for quality in management.