



Insight

Commercial Dispute Resolution

7 September 2011

The Centro Sentence – Does it go far enough?

Following on from the decision of Justice Middleton on 27 June 2011, the ASIC and the legal representatives for the eight Centro board members found to have failed to have performed their duties with the level of care and diligence required pursuant to the Corporations Act, 2001 recently made submissions to the court in relation to the appropriate penalty to be imposed.

On 31 August 2011, Justice Middleton handed down non-pecuniary penalties in the form of court declarations against the six non-executive directors, fined Andrew Scott (then Chief Executive Officer) \$30,000 and barred Romano Nenna (then Chief Financial Officer) from serving as a manager or director of any company for a two year period.

In respect of the non-executive directors, Justice Middleton stated that whilst they *“could have gone further in the way they expressed their remorse...to levy anything more would be unfair”*.

The claim

By way of background, the case proven against the eight defendant directors (two executive and six non-executive) centred on the approval of consolidated financial statements of three Centro entities for the financial year ending June 2007. All directors, save for one, defended the allegations.

The claim related specifically to the annual reports of the Centro entities and a failure by the members of the board to detect the non-disclosure of significant matters; namely millions of dollars worth of short term liabilities and the guarantees of the short-term liabilities of an associated company.

The penalty hearing

At the penalty hearing on 1 August 2011, the ASIC sought to distinguish between the culpability of the executive and non-executive directors. ASIC contended that the penalty for the CEO (Andrew Scott) should be *“substantially greater”* than that imposed on the other directors and that the CFO's role (Romano Nenna) was *“significantly different from and more serious”* than the non-executive directors.

ASIC's submissions

Specifically, the ASIC submitted that:

- The two executive directors be barred from acting as directors for up to three years and be fined \$100,000 each for failing to detect the error in the Centro entities' annual reports.
- The six non-executive directors be barred from acting as directors for between six and eighteen months and be fined at least \$30,000 and up to \$60,000.
- The actions of the directors had caused serious damage to other companies in the property sector and *“it had a major effect on the market”*.
- The handing down of penalties would act as a form of general deterrence and impress on directors the consequences to themselves and to the companies they oversee if they fail to apply due care and diligence to their duties.

In addition to distinguishing between the executive and non-executive directors, ASIC also submitted that the court could differentiate between the non-executive directors *“on the basis of their differing responsibilities within the group”*.

The defendants' submissions

Supported by character evidence from a wide range of prominent business figures, Counsel for the non-executive directors submitted that the ASIC's proposed penalties were *“extreme”* and *“harsh”*.

On behalf of the defendants, it was variously submitted that Justice Middleton should rely on the provision in the legislation that enables him to waive any penalty on the basis that the defendants were acting honestly. It was also submitted that:



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- The defendants had been sufficiently “humiliated” and had already endured the “trauma” of the case and the pending shareholder class actions.
- The publicity generated by the case was sufficient punishment, including the impact it had on their employment prospects (especially that of Nenna and Scott).
- The conduct of the defendants amounted to a form of “reasonable negligence” and to penalise them with a declaration would be akin to “*punishing a child when they don’t know they have done something wrong*”.
- The handing down of penalties would dissuade others from accepting director roles and would be “utterly out of step” with the community’s expectations.

The sentences

Whilst it is clear that Justice Middleton’s penalties are well below the bar submitted by the ASIC the case has certainly generated much interest in the corporate community and highlighted the repercussions that may ensue if directors do not properly scrutinise company reports and financial records.

Whether the level of public embarrassment that the eight defendant directors suffered will be sufficient deterrence to others is yet to be proven. However, what is certain is that corporate boards in Australia are closely monitoring board room procedures and processes to ensure that their members do not suffer the same fate.

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Our team

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