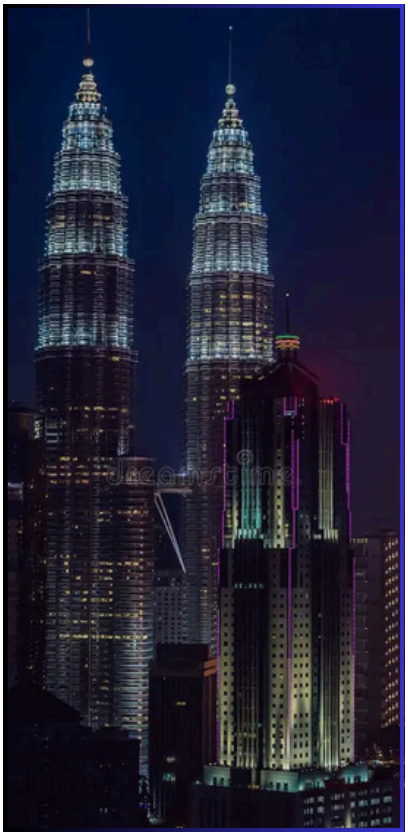
PRACTICALLY SPEAKING SERIES:

HAS THE BUSINESS JUDGMENT RULE (BJR) AS CLARIFIED IN IRIS CORPORATION CASE EASED THE DECISION-MAKING PROCESS FOR COMPANIES?



The Malaysian courts, recently in the case of Iris Corporation**[1]** and earlier in the case of Petra Perdana**[2]**, affirmed that directors should not be exposed to personal liability for every unsuccessful business decision.

These decisions have forged a coherent and modern articulation of the business judgment rule (BJR) which is embodied in Section 214 Companies Act 2016 ("CA 2016") with the courts saying:-

"There is no appeal on merits from management decisions to courts of law: nor will courts of law assume to act as a kind of supervisory board over decisions within the powers of management honestly arrived at."**[3]**

The Iris Corporation decision has definitely comforted the director community. Attributing personal liability for unsuccessful business decisions will serve to deter qualified individuals from accepting directorship in addition to stifling business innovation and growth.

On the flip side, the risk of courts being "dismissive" of all such actions, may result in directors being less vigilant in scrutinising business proposals or in exercising their duty of care, knowing that the courts are unlikely to intervene unless there is clear evidence of bad faith. This could lead to a culture of complacency at the board level.

Aside from the general duties and responsibilities of directors under the CA 2016, let's examine the BJR from a practical standpoint of a director in office.

We know that the four (4) limbs of the BJR must be satisfied. The BJR as embodied in Section 214 CA 2016 stipulates that in the exercise of business judgment one must:-

1. act for a proper purpose and in good faith;
2. no material personal interest in the subject matter;
3. being informed about the subject matter to the extent one reasonably believes to be appropriate under the circumstances; and
4. reasonably believe that the business judgment is in in the best interest of the company.

Looks easy enough.

On the assumption that limbs 1) and 2) are not an issue, how does one satisfy limbs 3) and 4)? Where do you draw the line that you are reasonably informed and believe that it is the best interest of the company? How much due diligence do you exercise? When must you do more? Throw in the complication that one does not usually have much time vis-à-vis business opportunities adds more subjectivity in the equation.

The simple answer may be that it all depends inter alia on the facts and circumstances of each business proposal, the skill sets of the board members and the capital to be invested.

Against these broad parameters, the practical reality as directors in office, these questions will remain:-

- how informed should the board be?
- how much reliance can the board place on the management's review and proposal?
- when should external advisors be brought in to assess the business proposal?

Some aspects were clarified in the Iris case in that the Court clarified that "independent assessment" does not require exhaustive due diligence, but rather an unbiased evaluation consistent with the directors' experience and the information before them. "Independent" also does not translate to engaging external parties.

We also know the Singapore courts have recently pronounced that directors must be sentinels and not sleuths suggesting that forensic level due diligence from a director is unreasonable.**[4]**

It all sounds clear enough but is it really?

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[1] Iris Corporation Bhd v Tan Sri Razali & Ors [2025] MLRAU 300
[2] Tengku Dato' Ibrahim Petra Tengku Indra Petra v Petra Perdana Berhad & Another case [2018] 2 MLJ 177
[3] Howard Smith Ltd v Ampol Petroleum [1974] AC 821
[4] Inter Pacific Petroleum Pte Ltd (in liquidation) V Goh Jin Hian [2024] SGHC 178

Anyone serving or having served as a non-executive director ("NED") knows that the reality of the situation on the ground is that you will only be given as much information as the management sees fit to render. As a director, you can ask for more information but this may then transgress to micro-managing. On the flip side, some management will inundate directors with copious amount of information and this is dangerous as NED then may transgress into making executive decisions when their job requires them to exercise an oversight function.

Another consideration is how much reliance can one place on the management? As pronounced in the Iris case, "the information need not be comprehensive or conducted from a position of scepticism"**[5]**. I disagree as the primary purpose of serving as an NED is to render input from oversight angle and not "assessment angle".

If a certain degree of scepticism is not exercised and information from management is relied on without probing further and asking the right questions, the "oversight" function of NED is surely not discharged. Interesting that the auditing space requires an auditor to view management's information with "healthy scepticism". Some advocate "professional scepticism" which requires one to not accept information at face value, probe deeper, seek corroborative evidence and challenge assumptions**[6]**. I opine that by doing this, the NED is discharging their "oversight" function. Another question following from the Iris case**[7]** would be whether the "assessment function" is a sub-set of "oversight" or "assessment" should be done wholly by the management?

In the whole scheme of things, where does that leave the NED vis-à-vis their discharge of fiduciary duties in respect of business proposals? Review the supporting documents, make due inquiry without too much scepticism? How much is too much will depend on the directors own skill and knowledge. What if some board members fail to demonstrate sufficient level of inquiry with regard their own skill and knowledge?

No one simple answer. All I can say is hold true to the guiding mantra which is "always acting in the best interest of the company".

One certainty from the Iris Corporation case and other cases**[8]** is the importance of contemporaneous documents including the minutes of meeting. From a practical angle, we know that how much reliance can be placed on documents and minutes is dependant on the management more so when an individual has left the board! That is a topic for another day...

KEY PRACTICAL TAKE-AWAYS are:-

1. All directors must discharge their fiduciary duties in the best interest of the company in good faith with no material interest;
2. NED and executive director have differing functions, the former an "oversight" and latter "assessment" function;
3. Following from Point 2 above, should management inundate the board with overload of information?;
4. The board's composition must consist of competent individuals with varied skill sets to assist the board as a collective decision-making entity to be informed about the subject matter to the extent one reasonably believes to be appropriate under the circumstances;
5. Following from Point 4 above, understandably external advisors should be engaged if the business proposal involves a subject matter not within the area of skill and knowledge of the board members as a collective body;
6. Contemporaneous documents used in making such decisions must be retained to corroborate board decisions; and
7. If some directors on the board fall short of the skill and expertise reasonably expected from such director, honest assessment of such director must be undertaken. "Automatic" re-election may in the worst case scenario, result in of the board being held liable as a whole due to an "incompetent" director. By the same token, incompetent management may result in the same consequence, and the defence of "reliance" in CA 2016**[9]** may not avail the board.

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The Writer's bio is available on our website.

[5] See note 1
[6] Devanesan Evanson NST 27 March 2025
[7] Court clarified that "independent assessment" does not require exhaustive due diligence, but rather an unbiased evaluation consistent with the directors' experience and the information before them
[8] Dato' Azizan Bin Abdul Rahman & others v Concrete Parade [2024] 3MLJ 223 wherein the minutes of meeting had assisted the court in arriving at its decision
[9] Section 215 Companies Act 2016