

The Boardroom Practice Limited

◆ Building Governance Best Practice ◆

To jump or not to jump

Directors are sometimes faced with situations where they must weigh up the prospect of “alarming investors and spooking the market” with their own discomfort regarding the financial state of a company. On the face of it this looks like a clear enough decision – if a director is unhappy with internal goings on and is unable to do much – at least in the here and now – about it, then surely resigning is the obvious course.

Things are rarely this clear. A surprising resignation is likely to lead to difficult market conditions under which investors might feel they have to sell, with subsequent price dips and losses to investors – outcomes which, should the company survive and go on to prosper might well be seen as inappropriate. Clarity is only apparent after the event.

Justice Miller in *Davidson v Registrar of Companies* (High Court, Wellington CIV 2010 – 485-76, 27 August 2010) as reported in NZ Lawyer 145 September 2010, has thrown some light on the issue in dealing with the matter of resignation and Bridgecorp Holdings Limited. His Honour accepted that the motivation in not resigning was an honourable one but noted that the long term health (and wealth) of shareholders would have been better served in this case by resignation.

In other words, resignation can be a signal – albeit an unwelcome one – to investors that trouble is afoot. Moreover because resignation is a serious matter its occurrence signals the strong probability that matters cannot be out to rights. Helpfully the Judge notes that where there are potential problems one might expect to see a review having been initiated by the board, of both the company’s cash resources and its ability to pay its debts as they fell due.

The detail of the Bridgecorp case is of no great import here and it might – indeed we would hope – it represents an extreme case but the message is clear. Regardless of the honest hopes and aspirations which directors may have, when the probabilities shift materially to the likelihood that collapse is imminent or likely then investors deserve the benefit of that signal which resignation provides.

The caveat of course, is that the signal is not always as strong as might be hoped for. Two directors of South Canterbury Finance resigned well before there was general knowledge of the true state of affairs at the company underlining the fact that resignation is an important but last ditch measure.

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