



Australasian
Compliance
Institute

The Secretary
Senate Economics Legislation Committee
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By Email – economics.sen@aph.gov.au

14 July 2009

Submission on Corporations Amendment (Improving Accountability on Termination Payments) Bill 2009

The Australian Compliance Institute (ACI) would like to take the opportunity to thank the Senate's Economics Legislation Committee for providing an opportunity for ACI to respond to your request for public comment on the proposed Corporations Amendment (Improving Accountability on Termination Payments) Bill 2009.

ACI is the peak industry body for the practice of compliance in Australasia. Our members are compliance, risk and governance professionals actively engaged in the private, professional services and Government sectors within Australia, New Zealand, Singapore, Thailand and Hong Kong.

For the benefit of Senators we have attached a copy of our original submission that was sent to Treasury as part of the public consultation that occurred in respect to the exposure bill.

We would like to take this opportunity to bring to the attention of the Committee one aspect of our previous submission that has not been taken up in the finalisation of the bill in its current form and that is the consideration of the circumstances surrounding the termination of an employee and whether, in light of performance or behavior issues, they should qualify for a termination payment.

Although, obviously, the general poor performance of an individual should be taken into consideration, in particular ACI advocates that in circumstances where an employee's employment is terminated as a result of undertaking an activity that is deemed to be either a significant breach of the organisation's compliance or governance plan and/or also in breach of the law, then that employee should forfeit any claim to a termination payout.

Principal Members





Although entities have the opportunity to negotiate these conditions in the contract with an employee at the time of appointment, there will be many organisations who may not have the foresight to consider such inclusions and without making these measures mandatory, or providing an opportunity for recourse through regulatory prosecution, there could be a significant gap in the amendments in relation to termination payments that could result in the finalised Corporations Act simply not achieving the objectives of Treasury.

Additionally, including considerations around expectations of compliant behaviour within the amendments clearly sends a message from government and the regulator as to the types of behaviour that is expected from executives and employees in Australia.

Most notably, without the inclusion of this kind of consideration, the opportunity for another occurrence of a situation similar to the termination payments made to departing James Hardie executives, CEO Peter Macdonald and CFO Peter Sharfon could occur.

In this case, both were able to resign and still receive their entitlements even though there were concurrent discussions by several Australian regulators with regard to laying charges for engaging in misleading and deceptive conduct, breaches of the Corporations Act, Trade Practices Act and the Fair Trading Act as well as dereliction of their duties as officers of a company. In this particular instance James Hardie were bound by their contractual obligations to the departing employees in the face of the potential criminal proceedings and huge public outrage.

ACI anticipates that this is exactly the type of experience that the proposed amendments are attempting to avoid, however, without the inclusions suggested in ACI's original submission Treasury will again be providing potential loopholes for employees whose employers do not have the foresight to include these kinds of contractual obligations themselves.

Once again ACI would like to thank the Treasury for providing an opportunity of making submissions on this important topic and would be keen to develop these concepts further with you as required.

Yours sincerely

Martin Tolar
Chief Executive Officer



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1 June 2009

Submission on Corporations Amendment (Improving Accountability on Termination Payments) Bill 2009

The Australian Compliance Institute (**ACI**) would like to take the opportunity to thank the Treasury for providing an opportunity for the Institute to respond to your request for public comment on the proposed Corporations Amendment (Improving Accountability on Termination Payments) Bill 2009.

ACI is the peak industry body for the practice of compliance in Australasia. Our members are compliance, risk and governance professionals actively engaged in the private, professional services and Government sectors within Australia, New Zealand, Singapore, Thailand and Hong Kong.

We have addressed relevant sections of the Exposure Draft – Explanatory Memorandum as below as well as some additional comments.

1. Lowering the threshold for shareholder approval

ACI supports and encourages the *intent* of the proposed changes, however our members have expressed some concerns with lowering the threshold for the payment of termination benefits to the level of exceeding only one year's base salary to be subject to shareholder approval for two reasons:

Firstly, this level does appear to be too low, especially in comparison to potential earnings overseas and may mean Australian companies are unable to compete in off shore searches to fill executive and director vacancies. Reciprocally, Australia may also lose a lot of talent at this level to off-shore companies who are able to offer better incentives in this regard. In practice a **two** year base would make this sourcing more competitive.

We also refer Treasury to statements issued by the European Corporate Governance Forum on Director Remuneration, held in Brussels on 24 March 2009.

Principal Members





“Severance pay for executive directors should be restricted to two years of annual remuneration and should not be paid if the termination is for poor performance.”¹

2. Expanding the scope to executives

Whilst shareholders have always, to extent, had some say over benefits for directors, they traditionally do not intrude into operational matters associated with the actual running of the company. Shareholders delegate these aspects to the board of directors. Giving a binding vote on termination payments to non-director executives seems to go beyond this oversight function into operational management matters. It is also questionable whether shareholders would have access or exposure to the necessary information or history of performance to be able to assess the appropriateness of payment of termination payments due.

3. Timing of Shareholder vote

Whilst it may be the intention of Treasury to limit the potential compliance costs associated with requiring a shareholder vote, in practice, contractual notice periods for very senior executive roles are often substantial lengths of time in order to allow businesses adequate opportunity to undertake succession planning and perform recruitment searches. Expanding the definition of “termination benefits” to capture payments in lieu of notice will mean that businesses are more frequently over the statutory cap where the executive is paid in lieu of some or all of the notice period.

The proposed amendments also prohibit companies from calling a general meeting for the sole purposes of holding the vote on the termination benefit. It is possible then that shareholder judgement might be delayed for up to twelve months, depending on the timing of the termination, by which time their judgement could be clouded by any number of issues beyond the control of the departing executive. In addition, in certain circumstances of separation, such as ill health, undue delay in obtaining approval could be unreasonable.

General observations

ACI notes that the proposed amendments do not indicate any consideration by Treasury of the circumstances surrounding the termination of the individual and would again refer to the statement issued by the European Corporate Governance Forum, included at the top of the page, indicating their preference that termination payments should not be made in circumstances where termination is a result of poor performance.

We would support such a position and add that consideration should perhaps also be given to the withholding of termination payments in circumstances where the termination has arisen due to compliance and governance breaches by the **individual** concerned. Breaches by the entity may arise due to a number of factors so we would restrict this condition only to the proven behaviours or actions of the director(s) and/or executive(s) concerned.

We understand that these conditions in regard to termination payments could also be negotiated by the entity at the contract and recruitment phase, however we wished to draw these considerations to the attention of Treasury for consideration at this stage of consultation as it is consistent with the intent of the amendment to improve accountability at this level.

ACI would also welcome further guidance or information from Treasury in regard to what criteria shareholders would be considering their votes against in regard to the

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<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/459&format=HTML&aged=0&language=EN&guiLanguage=en>

appropriateness of allowing the payment of Termination benefits, and what information the entity would be required to provide for the purposes of the vote. We would note that there is the potential for confidentiality and other implications depending on the requirements.



Conclusion

In summary then we would like to make the suggestion that:

The threshold of one year's base salary will be too low in practice to be able to recruit appropriately experienced talent at this level to Australian companies and to retain talent on-shore and that a more suitable threshold would be two years' base salary.

The expansion of the scope to executives is inconsistent with usual delegation by shareholder to directors for the management of operational matters, with corresponding accountabilities.

The holding over of the vote to the next scheduled general meeting could cause a potentially impractical delay that could have a number of impacts on the running of the business. Additionally it could impact the fairness with which the issue of the termination payments may be considered by shareholders.

A number of issues have not been included in the exposure draft that may contribute meaningfully to achieving the intent of the proposed changes, including guidance around criteria against which shareholders should assess whether it is appropriate to make termination payments and indications of what considerations should be taken into account, including aspects of performance, behaviour and actions of the individual.

Once again ACI would like to thank the Treasury for providing an opportunity of making submissions on this important topic and would be keen to develop these concepts further with you as required.

Yours sincerely

Martin Tolar
Chief Executive Officer