



Corporations Amendment (Corporate Reporting Reform) Bill 2010

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Law and Bills Digest Section

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Corporations Amendment (Corporate Reporting Reform) Bill 2010

Date introduced: 26 May 2010

House: House of Representatives

Portfolio: Financial Services, Superannuation and Corporate Law

Commencement: Almost all of the provisions commence on Royal Assent. However, Parts 2 and 3 of Schedule 1 do not commence at all if the proposed Act receives Royal Assent before item 34 of Schedule 1 to the *Corporations Amendment (Financial Market Supervision) Act 2010* commences.¹

Links: The [links](#) to the Bill, its Explanatory Memorandum and second reading speech can be found on the Bills page, which is at <http://www.aph.gov.au/bills/>. When Bills have been passed they can be found at ComLaw, which is at <http://www.comlaw.gov.au/>.

Purpose

The Bill amends the *Corporations Act 2001* (Corporations Act) for a variety of purposes, including:

- to reduce the regulatory burden on small companies limited by guarantee² by establishing a specific financial reporting regime (and requiring such companies to provide a copy of their annual reports only to members who request a copy)
- to prohibit companies limited by guarantee from paying dividends to members
- to allow companies to disclose summary parent-entity financial information on behalf of both the parent entity and its associated consolidated group (instead of providing audited financial statements for both the consolidated entity and the parent entity)

1. Item 34 of Schedule 1 to the *Corporations Amendment (Financial Market Supervision) Act 2010* inserts **Part 10.14—Transitional provisions relating to the Corporations Amendment (Financial Market Supervision) Act 2010** into the Corporations Act. Schedule 1 to that Act commences on a single day to be fixed by Proclamation (which is yet to occur). However, if any of the provisions in Schedule 1 do not commence within 12 months of the Act receiving Royal Assent (which occurred on 25 March 2010), then those provisions in Schedule 1 are repealed. A copy of the *Corporations Amendment (Financial Market Supervision) Act 2010* (being Act No. 26 of 2010) is available electronically at http://www.austlii.edu.au/au/legis/cth/num_act/camsa2010530/, viewed 31 May 2010.
2. The term ‘*small company limited by guarantee*’ (in the context of a particular financial year) is defined in **proposed section 45B** of the Corporations Act. See the discussion of **item 4 of Schedule 1** to the current Bill in the Main Provisions section of this Digest.

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- to modify the requirement that companies may only pay dividends from profits, by replacing the current ‘profits test’ with a solvency-based test
- to allow companies to vary the length of a financial year in certain circumstances³
- to require all listed entities to disclose a ‘review of operations and financial condition’⁴, and
- to clarify when a company can cancel its share capital.⁵

The Bill also amends the *Australian Securities and Investments Commission Act 2001* (ASIC Act):

- to remove obsolete provisions, and
- to improve the processes of the Companies Auditors and Liquidators Disciplinary Board (CALDB).

Background

Key issues and basis of policy commitment

Small companies limited by guarantee: modified reporting framework

In part, the Bill gives effect to recommendations made by the Treasury following its recent inquiry into financial reporting by unlisted public companies. On 6 June 2007, the Treasury issued a discussion paper on the issue for public comment.⁶ Primarily, it wished

3. **Proposed subsection 323D(2A)** of the Corporations Act (which is to be inserted by **item 44** of **Schedule 1** to the Bill).
4. See discussion of section 299A of the Corporations Act at pp. 10–12 of this Digest. The text of section 299A is available electronically at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s299a.html (viewed 1 June 2010). In addition, section 299 of the Corporations Act provides that the directors’ report for certain entities for a financial year must include certain general information about the company’s operations and activities, including a ‘review of operations during the year of the entity reported on and the results of those operations’ and various financial information. Currently the provision really only applies to companies, registered schemes and ‘disclosing entities’. Section 299A does not apply to individuals, partnerships or trusts. See http://www.austlii.edu.au/cgi-bin/sinodisp/au/legis/cth/consol_act/ca2001172/s299.html (viewed 1 June 2010).
5. The Bill makes minor, technical amendments to existing section 258F of the Corporations Act to make it clear that a company can only cancel share capital in circumstances where it is not inconsistent with Australian accounting standards to do so. For example, a company can write off accumulated losses against share capital, but it cannot take expenses directly to share capital. See **items 8–10** of **Schedule 1** to the Bill.
6. The Treasury, *Financial reporting by unlisted public companies—Discussion Paper*, (inquiry homepage), Treasury website, 7 June 2007, viewed 7 June 2010, <http://www.treasury.gov.au/contentitem.asp?ContentID=1269&NavId=037>

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to examine whether ‘some type of differential reporting framework should be introduced for [unlisted public companies] based on the existing differential requirements for proprietary companies’.⁷ On 21 September 2007, it made some 47 submissions available to the public, with most submissions suggesting that for reporting purposes, companies limited by guarantee could be differentiated on the basis of the size of their operating revenue (rather than less straightforward criteria such as amount of assets or number of employees).⁸

There are currently some 11 000 companies limited by guarantee in Australia.⁹ According to research by the University of Melbourne, approximately 21 per cent of these companies are sports and recreation-related organisations; 19 per cent are community service organisations; 15 per cent are education-related institutions; and 10 per cent are religious organisations.¹⁰ The research also shows that ‘almost all companies limited by guarantee have a not-for-profit motive’.¹¹ According to the Treasury, the not-for-profit focus of a company limited by guarantee is:

... likely to significantly impact upon the demand for comprehensive financial reports by members. This is because members generally invest only nominal amounts of capital into the company. In addition, members do not receive direct financial returns in the form of dividends or capital gains. For example, in the case of a small sporting club, members receive returns in the form of access to facilities and discounted goods and services.¹²

The Bill recognises (among other things) that, by virtue of their size, the smaller of these companies find it difficult to comply with the current auditing and reporting requirements in the Corporations Act. According to sample data provided by ASIC on 3 November 2006, 47 per cent of companies limited by guarantee have revenue of less than \$250 000, but the average cost to a company of preparing an auditing an annual report is estimated to be \$60 000.¹³ Nonetheless, the Bill also recognises that some requirements are necessary

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7. The Treasury, *Financial reporting by unlisted public companies—Discussion paper*, Treasury website, 6 June 2007, p. iii, viewed 7 June 2010, http://www.treasury.gov.au/documents/1269/PDF/Discussion_paper_Financial_Reporting_by_Unlisted_Public_Companies.pdf
 8. The Treasury, *Submissions: Financial reporting by unlisted public companies—Discussion paper*, 21 September 2007, viewed 7 June 2010, <http://www.treasury.gov.au/contentitem.asp?ContentID=1316&NavID=037>
 9. Explanatory Memorandum, op. cit., pp. 5–6. See also Treasury, *Financial reporting by unlisted public companies—Discussion paper*, op. cit., p. 2.
 10. Ibid.
 11. Treasury, *Financial reporting by unlisted public companies—Discussion paper*, op. cit., p. 2.
 12. Ibid., pp. 2 and 4.
 13. Explanatory Memorandum, op. cit., pp. 46–48, particularly Table 10.1 (‘Size of companies limited by guarantee’).

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as an ‘important governance and transparency mechanism’.¹⁴ Thus, in place of the current regime, the Bill introduces a three-tiered, differential reporting framework for companies limited by guarantee, with the particular requirements being determined by the amount of the company’s annual consolidated revenue.¹⁵

In summary, the Bill exempts the first tier of small companies limited by guarantee (being those with an annual revenue of less than \$250 000) from the reporting and auditing requirements set out in Chapter 2M of the Corporations Act¹⁶—however, there are a number of exceptions:

- where the company is a deductible gift recipient¹⁷
- where members with at least five per cent of the votes in the company (or ASIC) direct the company to prepare a financial report and directors’ report for a financial year¹⁸
- where the company is a Commonwealth company, a subsidiary of a Commonwealth company (or a subsidiary of a Commonwealth authority)¹⁹, and
- where the company is a transferring financial institution of a State or Territory, or a company that is permitted to use the expression ‘*building society*’, ‘*credit society*’ or ‘*credit union*’ under section 66 of the *Banking Act 1959*.²⁰

14. Ibid., pp. 5–6.

15. See **proposed section 285A** of the Corporations Act (which is to be inserted by **item 14** of **Schedule 1** to the Bill). The *first tier* applies to companies limited by guarantee which have an annual revenue of less than \$250 000 and do not have deductible gift recipient status. The *second tier* applies to companies limited by guarantee which (a) have an annual revenue of less than \$250 000 and have deductible gift recipient status or (b) have an annual revenue of between \$250 000 and \$1 million, regardless of whether the company has deductible gift recipient status. The *third tier* applies to companies limited by guarantee which have an annual revenue of \$1 million or more, regardless of whether the company has deductible gift recipient status.

16. Chapter 2M of the Corporations Act deals with financial reports and audit.

17. The term ‘*deductible gift recipient*’ is generally defined in section 30-227 of the *Income Tax Assessment Act 1997* to mean an entity or government entity that is a fund, authority or institution described in the table in section 30-15 of that Act, and is either endorsed under Subdivision 30-BA as a deductible gift recipient or is mentioned by name in that table or in Subdivision 30-B. A taxpayer can claim a deduction in his or her income tax return for any gift or donation made to a ‘deductible gift recipient’.

18. See **proposed sections 294A and 294B** of the Corporations Act (which are to be inserted by **item 16** of **Schedule 1** to the Bill).

19. See **proposed paragraphs 45B(1)(d) and 301(3)(a)** of the Corporations Act (which are to be inserted by **items 4 and 30** of **Schedule 1** to the Bill). The directors of a Commonwealth company must continue to comply with the annual reporting requirements set out in the *Commonwealth Authorities and Companies Act 1997* (CAC Act).

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The Bill also streamlines assurance (or auditing) requirements for companies in the second tier (being those with annual revenue of between \$250 000 and \$1 million), by giving them the option of having their annual reports subject to a review (rather than a more expensive and time consuming audit).²¹ In this regard, the Auditing and Assurance Standards Board (AUASB) has issued an exposure draft of a proposed Auditing Standard (titled ‘Proposed Auditing Standard on Review Engagements ASRE 2415: *Review of a Financial Report—Company Limited by Guarantee*’).²² The proposed Auditing Standard will apply in relation to companies limited by guarantee following the passage of the Bill (and associated regulations). It does not replace any existing Auditing Standard but rather sets out the specific requirements that an auditor must observe when conducting a review of a financial report for a financial year ending on or after 30 June 2010 for a small company limited by guarantee. It also sets out the form and content of the review report.

Finally, in the context of amendments that modify the financial reporting framework for small companies limited by guarantee, it is noted that the Bill also:

- exempts companies in the second and third tiers of the proposed three-tier differential framework from complying with the existing directors’ report disclosure requirements, but requires them to prepare a simplified directors’ report instead²³
- revises the way companies limited by guarantee can distribute annual reports to members²⁴, and

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20. **Proposed subsection 45B(1)** of the Corporations Act (which is to be inserted by **item 4** of **Schedule 1** to the Bill). These companies will continue to be subject to the financial reporting regime in Part 12.6 of the Corporations Regulations 2001.
 21. **Proposed subsection 301(3)** of the Corporations Act (which is to be inserted by **item 30** of **Schedule 1** to the Bill).
 22. The AUASB is an independent statutory board established under section 227A of the ASIC Act. Its functions include making auditing standards under section 336 of the Corporations Act 2001; formulating auditing and assurance standards for other purposes; and formulating guidance on auditing and assurance matters. See AUASB, *Standards and Guidance*, AUASB website, no date, viewed 3 June 2010, <http://www.auasb.gov.au/Standards-and-Guidance.aspx>. The proposed Auditing Standard was issued in draft form on 28 May 2010. See AUASB, *News: The AUASB has issued exposure draft 02/10*, AUASB website, 28 May 2010, viewed 3 June 2010, <http://www.auasb.gov.au/News.aspx?newsID=3956> The proposed Auditing Standard is available electronically at http://www.auasb.gov.au/admin/file/content102/c3/ED_02_10_ASRE%202415.pdf and an explanatory guide is also available at http://www.auasb.gov.au/admin/file/content102/c3/Explanatory_Guide_to_ED_02_10.pdf (viewed 3 June 2010).
 23. **Proposed section 285A** of the Corporations Act (which is to be inserted by **item 6** of **Schedule 1** to the Bill). The specific requirements of the simplified directors’ report are set out in **proposed subsections 300B(1) and (2)** of the Corporations Act (which are to be inserted by **item 29** of **Schedule 1** to the Bill).

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- prohibits all companies limited by guarantee from paying a dividend to members.²⁵

Parent-entity financial statements

Currently, the Corporations Act requires each public company, large proprietary company, registered scheme and ‘disclosing entity’ to prepare an annual financial statement.²⁶ Where any of these entities is a parent entity, it must also prepare financial statements in relation to the consolidated entity if required to do so by the accounting standards. Further, a disclosing entity must also provide half-yearly statements.

In 2003, the Australian Accounting Standards Board (AASB) investigated the relevance of presenting parent-entity financial reports in addition to consolidated reports.²⁷ As part of a discussion paper, it set out the requirements in a number of other jurisdictions (namely France, Germany, Japan, New Zealand, Canada, United Kingdom and the United States of America) before recommending (among other things) that the Australian requirement for parent entity financial reports to be published in the annual report should be removed. It also recommended that the requirement for full audited parent entity general purpose financial reports to be lodged with ASIC should be retained, except for parent entities that:

- (a) do not conduct substantive operations, including treasury operations;
- (b) are not borrowing entities;
- (c) are not single guarantors for the debt of one or more subsidiaries.²⁸

On 7 April 2006, the Treasury released a consultation paper titled ‘Corporate and Financial Services Regulation Review’.²⁹ The paper covered a number of areas of financial services regulation, company reporting obligations, auditor independence, corporate governance, fundraising, takeovers, collective investments and dealing with

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24. **Proposed section 316A** of the Corporations Act (which is to be inserted by **item 40** of **Schedule 1** to the Bill).
 25. **Proposed section 254SA** of the Corporations Act (to be inserted by **item 6** of **Schedule 1** to the Bill).
 26. See section 292 of the Corporations Act at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s292.html (viewed 10 June 2010).
 27. Dr J Cotter (Associate Professor of Accounting, University of Southern Queensland), *Relevance of parent entity financial reports*, Discussion paper, 2003, viewed 7 June 2010, http://www.aasb.com.au/admin/file/content102/c3/Parent_entity_discussion_paper.pdf
 28. *Ibid.*, p. 29.
 29. Treasury, *Corporate and Financial Services Regulation Review: Consultation paper*, 7 April 2006, viewed 7 June 2010, <http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=1068>

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regulators. Specifically in relation to parent entity financial statements, comments were sought on whether only summary financial information should be required in relation to the parent entity, and the type of information that should be required to be disclosed.³⁰

In November 2006, the Treasury announced that the Government would not proceed with this proposal, saying:

The consultation paper raised whether to allow lodgment of only summary financial information relating to the parent entity when a corporate group lodges consolidated financial statements.

The Government will not proceed with this proposal because the consultation process did not identify that the costs of preparing this information outweighed the existing benefits to users.³¹

However, in August 2008, the Rudd Government undertook targeted consultation with key stakeholders, including the Group of 100 (being an ‘association of senior finance executives from the nation’s business enterprises’), professional accounting bodies and a number of audit firms.³² The Explanatory Memorandum states that a number of these stakeholders ‘have called for the removal of the requirement to prepare (and audit) separate parent entity financial statements to be replaced by summarised information’.³³ It also notes that the Group of 100, in supporting the proposed amendment, said that ‘the replacement of full parent entity financial statements with summary information would reduce the burden of regulation on business, reduce business costs and remove unnecessary disclosures from an entity’s annual report’.³⁴ The Group of 100 estimates that the ‘incremental [external] audit costs’ for parent-entity financial statements are about \$20 000 to \$25 000 for the top 100 ASX companies.³⁵

Under the proposed law, an entity will be required to prepare only one set of financial statements—either financial statements solely in relation to the particular entity or (if the accounting standards require the preparation of consolidated financial statements) financial statements in relation to the consolidated entity.³⁶ If the entity is required to

30. Ibid.

31. Treasury, *Corporate and Financial Services Regulation Review: Proposals paper*, November 2006, p. 54, viewed 7 June 2010, http://www.treasury.gov.au/documents/1189/PDF/CFSRR_Proposals_Paper.pdf

32. Explanatory Memorandum, op. cit., p. 57.

33. Ibid.

34. Ibid., p. 15.

35. Ibid., p. 54.

36. **Proposed subsection 295(2)** of the Corporations Act (which will replace current subsection 295(2)). See **item 17 of Schedule 1** to the Bill. Similar amendments are made to requirements for half-year financial statements: see **proposed subsection 303(2)** of the

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prepare consolidated financial statements, the Corporations Regulations 2001 will specify supplementary information about the parent entity that is to be included in a note to the consolidated financial statements.³⁷

Modifying the requirement that companies may only pay dividends from profits, by replacing the current 'profits test' with a solvency-based test

Currently, a company may only pay a dividend to shareholders out of company profits.³⁸ While this is commonly known as the 'profits test', the Corporations Act does not define the term '*profits*' nor provide any guidance about the operation of the test. Further, as the Explanatory Memorandum notes, existing legal interpretations by the courts (known as 'precedents') are 'outdated and complex' and are out of step with changing accounting principles.³⁹ Since the adoption of International Financial Reporting Standards (IFRS), Australian accounting standards are 'increasingly linked to the fair value (whether realised or unrealised) impacting on the profitability of the company'.⁴⁰ This means that accounting profits are neutralised by non-cash expenses—even where companies otherwise have sufficient cash resources to pay a dividend.

In December 2002, the Australian Accounting Research Foundation released a discussion paper recommending that a solvency-based test be adopted in place of the profits test.⁴¹ The proposal received widespread industry and legal support.⁴² However, it was not until

Corporations Act (which will replace current subsection 303(2)). See **item 31** of **Schedule 1** to the Bill.

37. Existing paragraphs 295(3)(a) and 303(3)(a) of the Corporations Act.
38. Section 254T of the Corporations Act (which is to be repealed and substituted by **item 7** of **Schedule 1** to the Bill). Note that under **proposed section 254SA** of the Corporations Act (which is to be inserted by **item 6** of **Schedule 1** to the Bill), all companies limited by guarantee will be prohibited from paying a dividend. Note also that a taxpayer must include a dividend in his/her (or its) assessable income.
39. Explanatory Memorandum, op. cit., p. 19.
40. Ibid.
41. Ibid. See also Legislation Review Board of the Australian Accounting Research Foundation, *Payment of dividends under the Corporations Act 2001*, Discussion paper No. 5, December 2002.
42. See, for example, Group of 100, *Payment of dividends under the Corporations Act 2001*, Submission to the Australian Accounting Research Foundation, 12 June 2002, viewed 10 June 2010, http://group100.com.au/submissions/sub_20020612_aasb_div-corpact.htm ; Australian Institute of Company Directors (AICD), *Law reform: payment of dividends*, Submission to Treasury, 5 August 2004 (annexed to a letter from AICD to Chris Pearce MP dated 12 January 2006), viewed 10 June 2010, <http://www.companydirectors.com.au/NR/rdonlyres/A3C02E91-5F21-4283-9355-DDE258435E4A/0/LettertoChrisPearceonIFRSanddistributabledivid.pdf> and Law Council of Australia, *Proposal for reform of section 254T of the Corporations Act*, Submission to

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August 2008 that the Treasury consulted with key stakeholders, ‘including representatives of industry, business, professional accounting bodies and other interested parties’, most of whom were ‘generally supportive of providing great flexibility for paying dividends while maintaining appropriate safeguards’.⁴³

The Bill repeals the profits test and replaces it with a more flexible, solvency-based test which allows a company to pay a dividend where:

- the company’s assets exceed its liabilities immediately before the dividend is declared
- the excess is sufficient to meet the payment of the dividend
- the payment of the dividend is fair and reasonable to the company’s shareholders as a whole, and
- the payment of the dividend does not ‘materially prejudice’ the company’s ability to pay its creditors.⁴⁴

The company’s assets and liabilities are to be calculated in accordance with accounting standards in force at the relevant time.⁴⁵ If the company is not required to prepare an audited financial report (for example, where the company is a small proprietary company), its solvency can be determined by reference to the accounting records it is required to keep under section 286 of the Corporations Act.⁴⁶

Treasury, September 2004, viewed 10 June 2010,
http://www.lawcouncil.asn.au/shadomx/apps/fms/fmsdownload.cfm?file_uid=8C732D5B-1C23-CACD-2243-22F30938DA55&siteName=lca

43. Explanatory Memorandum, op. cit., p. 63.
44. **Proposed section 254T** of the Corporations Act (which is to be inserted by **item 7** of **Schedule 1** to the Bill). It will replace current section 254T. As explained in Note 1 to the proposed provision, the payment of a dividend would ‘materially prejudice the company’s ability to pay its creditors’ if the company would become insolvent as a result of the payment. It should be noted that directors have a duty to prevent insolvent trading under existing section 588G of the Corporations Act. (The text of section 588G is available at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s588g.html, viewed 10 June 2010.) The requirement that the company’s assets exceed its liabilities immediately before the dividend is declared is similar to the ‘balance sheet’ tests used in New Zealand and Canada.
45. **Proposed subsection 254T(2)** of the Corporations Act.
46. The text of section 286 of the Corporations Act is available at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s286.html (viewed 10 June 2010).

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All listed entities to provide information about their operations and financial position

In part, the Bill also gives effect to a recommendation by the Corporations and Markets Advisory Committee (CAMAC) in 2006. CAMAC is an ongoing committee established in 1989 ‘to provide a source of independent advice to the Australian Government on issues that arise in corporations and financial markets law and practice’.⁴⁷ In March 2005, the then Parliamentary Secretary to the Treasurer, Chris Pearce MP, requested CAMAC to inquire into ‘the extent to which the duties of directors under the *Corporations Act 2001* (the Corporations Act) should include corporate social responsibilities or explicit obligations to take account of the interests of certain classes of stakeholders other than shareholders’.⁴⁸ In November 2005, CAMAC issued a discussion paper for public comment. It received a ‘large’ number of submissions. Then on 1 December 2006, CAMAC published its report, focussing on directors’ duties; corporate disclosure; and the promotion of responsible corporate practices.⁴⁹

Among other things, CAMAC recommended that section 299A of the Corporations Act should be extended to apply not only to listed public companies (as is the case at present) but to all listed entities.⁵⁰ Currently section 299A of the Corporations Act states that the directors’ report for a financial year for a company (or disclosing entity) that is a listed public company must also contain information that members of the company would reasonably require to make an informed assessment of the company’s:

- operations and financial position, and
- business strategies and prospects for future financial years.

The directors’ report may omit material that would otherwise relate to business strategies and prospects for future financial years if it is likely to result in unreasonable prejudice to the company (or disclosing entity) or a related consolidated entity. However, if material is omitted, the report must say so.

In recommending that section 299A be extended to apply to all listed entities (and not just listed public companies as is the case at present), CAMAC noted that non-corporate listed entities (including listed managed investment funds) make up over 10 per cent of all listed entities and suggested it is therefore ‘anomalous’ that these other listed entities are not

47. CAMAC, *Welcome to CAMAC*, website, viewed 28 April 2010, <http://www.camac.gov.au/camac/camac.nsf>

48. CAMAC, *The social responsibility of corporations: Report*, 1 December 2006, pp. 2–3, viewed 31 May 2010, [http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/\\$file/CSR_Report.pdf](http://www.camac.gov.au/camac/camac.nsf/byHeadline/PDFFinal+Reports+2006/$file/CSR_Report.pdf)

49. Ibid.

50. See footnote 4 above.

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covered by section 299A.⁵¹ However, CAMAC drew the line at extending section 299A to cover all existing categories of entities or companies under the Corporations Act, saying that it was ‘not persuaded that the potential interest of other elements of the community in particular aspects of the activities of some non-listed companies is sufficient justification for a wholesale expansion of the category of reporting entities’.⁵²

Approval of proposed amendments to the corporations law by the Ministerial Council for Corporations

Finally, by way of background to the Bill, it is noted that the Ministerial Council for Corporations (MINCO) was apparently consulted about the amendments to the laws in the national corporate regulation scheme, and has approved them (as it is required to do under the Corporations Agreement 2002 as amended).⁵³

Committee consideration

On 13 May 2010, the Senate resolved to refer the provisions of ‘time-critical Bills’ to various legislative and general purpose standing committees for inquiry and report by 15 June 2010.⁵⁴ On 1 June 2010, the Senate Economics Legislation Committee reported that there are no substantive matters that require examination in the current Bill.⁵⁵

Financial implications

The Explanatory Memorandum contains no clear statement about the financial impact of the Bill. However, the Regulation Impact Statement (RIS) notes that:

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51. CAMAC, *The social responsibility of corporations: Report*, op. cit., p. 146.
 52. Ibid.
 53. C Bowen MP (Minister for Financial Services, Superannuation and Corporate Law and Human Services), ‘Second reading speech: Corporations Amendment (Corporate Reporting Reform) Bill 2010’, House of Representatives, *Debates*, 26 May 2010, p. 20, viewed 1 June 2010, <http://www.aph.gov.au/hansard/rep/dailys/dr260510.pdf>. See particularly clauses 501 and 502 of the Corporations Agreement 2002 (as amended in 2005) at <http://www.treasury.gov.au/contentitem.asp?pageId=035&ContentID=495> (viewed 1 June 2010).
 54. Senator P Wong, ‘References to committees’, Senate, *Debates*, 13 May 2010, p. 2839, viewed 7 June 2010, <http://www.aph.gov.au/hansard/senate/dailys/ds130510.pdf>. Here the phrase ‘time-critical Bills’ refers to all Bills introduced into the House of Representatives after 13 May 2010 and before 3 June 2010 that contain provisions commencing on or before 1 July 2010.
 55. Senate Economics Legislation Committee, ‘Consideration of time critical Bills’, *Report*, 1 June 2010, viewed 7 June 2010, http://www.aph.gov.au/Senate/committee/economics_ctte/timecritical_bills/report/report.pdf

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- the costs of introducing a three-tiered financial reporting system for small companies limited by guarantee is expected to be ‘minimal and outweighed by the benefits to users and companies limited by guarantee’⁵⁶
- the costs to prepare and audit parent-entity summary data will be ‘significantly lower’ than the costs to prepare and audit separate parent-entity financial statements), but the extent of the savings ‘will be dependent on the size and complexity of the entity and the relativities around the size of the parent as opposed to the consolidated entity’⁵⁷,
- the benefits of replacing the ‘profits test’ with a more flexible, solvency-based test for the payment of dividends ‘are expected to outweigh the costs’⁵⁸, and
- the costs of requiring all listed entities to disclose a review of operations and financial condition are difficult to quantify but appear to be ‘minimal’—mainly because there are only approximately 200 listed managed investment schemes which will need to comply with the revised requirement (in addition to the 2200 or so listed public companies to which the requirement already applies).⁵⁹

Main provisions

Many of the main provisions of the Bill are discussed (or highlighted) in the ‘Background’ section to this Digest above. However, for completeness, some provisions are discussed more fully below.

Schedule 1—Amendments relating to the *Corporations Act 2001*

Item 4 of Schedule 1 inserts **proposed section 45B** into the Corporations Act. It defines the term ‘*small company limited by guarantee*’ (in the context of a particular financial year) to mean a company which:

- is a company limited by guarantee for the whole of the year
- is not a deductible gift recipient at any time during the year
- has revenue (or consolidated revenue) less than the \$250 000 (or such other amount prescribed by the regulations as the relevant threshold amount) for the relevant year⁶⁰

56. Explanatory Memorandum, op. cit., p. 53.

57. Ibid., p. 58.

58. Ibid., p. 64.

59. Ibid., p. 68 (noting the odd syntax in paragraph 10.75).

60. **Proposed subsection 45B(2)** states that for the purposes of **proposed section 45B**, the threshold amount is \$250 000 ‘or any other amount prescribed by the regulations’. **Proposed subsection 45B(3)** states that revenue and consolidated revenue are to be calculated for the purposes of the section ‘in accordance with accounting standards in force

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- is not a company for the purposes of the *Commonwealth Authorities and Companies Act 1997* (CAC Act) or a subsidiary of such a company (or a Commonwealth authority)⁶¹
- has not been a ‘*transferring financial institution*’ of a State or Territory (as defined in **Schedule 4** to the Corporations Act),⁶² and
- is not a company that is permitted to use the expression ‘*building society*’, ‘*credit society*’ or ‘*credit union*’ under section 66 of the *Banking Act 1959*.⁶³

Item 6 inserts **proposed section 254SA** to prohibit a company limited by guarantee from paying a dividend to its members. Although not stated in the provision itself, **proposed section 254SA** is an offence provision. It attracts a maximum penalty of 100 penalty units (that is, \$11 000) or imprisonment for two years, or both.⁶⁴ The fact the penalty may involve imprisonment raises an interesting issue, because the language of the provision refers to a ‘company limited by guarantee’ rather than ‘an officer’ of such a company (or

at the relevant time’ (even if the standard does not apply to the particular financial year, or some or all of the companies concerned).

61. The text of the CAC Act is available electronically at: http://www.austlii.edu.au/au/legis/cth/consol_act/caaca1997387/ (viewed 1 June 2010).
62. Schedule 4 to the Corporations Act deals with the transfer of financial institutions and friendly societies, and is available electronically at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/sch4.html (viewed 1 June 2010).
63. The text of section 66 of the *Banking Act 1959*, which sets out restrictions on the use of certain words and expressions, is available electronically at: http://www.austlii.edu.au/au/legis/cth/consol_act/ba195972/s66.html (viewed 1 June 2010).
64. **Proposed table item 82A** in Schedule 3 to the Corporations Act (which is to be inserted by **item 48** of **Schedule 1** to the Bill). The term ‘*penalty unit*’ is defined in section 4AA of the *Crimes Act 1914* as \$110. However, section 4B of that Act provides that where the offence is committed by a body corporate (that is, a company), a court may impose a maximum penalty up to five times that which can be imposed on an individual—unless a contrary intention is shown in the relevant legislation. In this regard, it should be noted that section 1312 of the Corporations Act also states that ‘Where a body corporate is convicted of an offence against this Act, the penalty that the court may impose is a fine not exceeding 5 times the maximum amount that, but for this section, the court could impose as a pecuniary penalty for that offence’. It could be argued that because **proposed section 254SA** is expressed in terms of a ‘company limited by guarantee’ rather than by reference to the individual directors of such a company, the offence carries only the penalty as stated in **proposed table item 82A** in Schedule 3 to the Corporations Act (rather than a penalty of up to five times that amount). On the other hand, however, the fact that the penalty could involve imprisonment tends to support the proposition that the penalty as stated is simply that which would apply to an individual (with the possibility that a court could impose a fine of up to \$55 000 on the company).

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indeed, even a ‘person’). It has long been established at common law⁶⁵ that a company has a separate legal personality, quite distinct from that of its members or officers, including directors. In this regard, for example, section 188 of the Corporations Act sets out the responsibilities of secretaries and directors of a company if the company contravenes certain named provisions of that Act⁶⁶—but no provision in the Bill amends section 188 to include reference to **proposed section 254SA**. It may therefore need to be made clear on the face of the provision (even if only by the insertion of a note):

- that it is an offence provision
- in what circumstances directors (or other officers of the company) will be liable, and/or
- what defences (if any) may be available to such persons.

Item 7 repeals existing section 254T and inserts **proposed section 254T** in its place. It sets out the circumstances in which a company (other than a company limited by guarantee) may pay a dividend. As noted in the ‘Background’ section to this Digest, under the revised provision, a company must not pay a dividend unless:

- (a) the company’s assets exceed its liabilities immediately before the dividend is declared, and the excess is sufficient to meet the payment of the dividend
- (b) the payment of the dividend is fair and reasonable to the company’s shareholders as a whole, and
- (c) the payment of the dividend does not ‘materially prejudice’ the company’s ability to pay its creditors.⁶⁷

The company’s assets and liabilities are to be calculated in accordance with accounting standards in force at the relevant time.⁶⁸ A person commits an offence under **proposed**

65. See, for example, *Salomon v A Salomon & Co Ltd* [1897] AC 22, which is now enshrined as section 124 of the Corporations Act (which is available electronically at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s124.html, viewed 21 June 2010).

66. The text of section 188 of the Corporations Act is available electronically at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s188.html (viewed 21 June 2010).

67. As explained in Note 1 to the proposed provision, the payment of a dividend would ‘materially prejudice the company’s ability to pay its creditors’ if the company would become insolvent as a result of the payment. Directors have a duty to prevent insolvent trading under existing section 588G of the Corporations Act. (See footnote 69 below.)

68. **Proposed subsection 254T(2)** of the Corporations Act.

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section 254T if he or she is a director of a company which pays a dividend in contravention of the provision.⁶⁹

Items 8–10 amend section 258F to make it clear that while a company may reduce its share capital by cancelling any paid-up capital that is lost or not represented by available assets, it may not reduce its share capital:

- by cancelling shares, or
- where the cancellation of paid-up share capital is inconsistent with the requirements of any accounting standard.⁷⁰

Item 14 inserts **proposed section 285A**, which sets out an overview of the annual financial reporting obligations for companies limited by guarantee. It sets out, in tabular form, the three-tiered differential reporting framework that is based on the relevant company's annual revenue.

Item 15 inserts **proposed subsection 292(3)**, which states that a small company limited by guarantee is only required to prepare the financial report and directors' report if directed to do so by members of the company with at least five per cent of the votes (**proposed section 294A**) or by ASIC (**proposed section 294B**).⁷¹

In the case of a member direction given under **proposed section 294A**, the direction must be signed by the members giving the direction and be made no later than 12 months after the end of the relevant financial year.⁷² It may specify:

- that the financial report does not have to comply with some or all of the accounting standards
- that a directors' report (or part thereof) does not need to be prepared, and/or

69. Subsection 588G(3) of the Corporations Act states: 'A person commits an offence if: (a) a company incurs a debt at a particular time; and (aa) at that time, a person is a director of the company; and (b) the company is insolvent at that time, or becomes insolvent by incurring that debt, or by incurring at that time debts including that debt; and (c) the person suspected at the time when the company incurred the debt that the company was insolvent or would become insolvent as a result of incurring that debt or other debts (...); and (d) the person's failure to prevent the company incurring the debt was dishonest'. Under subsection 588G(1A), a company incurs a debt in relation to the payment of dividends at the time when the dividend is paid or, if the company has a constitution that provides for the declaration of dividends, when the dividend is declared. For the text of section 588G, see http://www.austlii.edu.au/cgi-bin/sinodisp/au/legis/cth/consol_act/ca2001172/s588g.html (viewed 18 June 2010).

70. **Proposed paragraphs 258F(2)(a) and (b)** are inserted by **item 10** of **Schedule 1** to the Bill.

71. **Proposed sections 294A and 294B** are inserted by **item 16** of **Schedule 1** to the Bill.

72. **Proposed subsection 294A(2)** of the Corporations Act.

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- whether the financial report is to be audited or reviewed.⁷³

A company limited by guarantee which fails to comply with a direction given by ASIC under **proposed section 294B** may be guilty of a strict liability offence that carries a maximum of 10 penalty units or imprisonment for three months or both.⁷⁴ The direction may be general or may specify the particular requirements with which the company must comply.⁷⁵ It must specify a ‘reasonable’ date for complying with the direction.⁷⁶ It must also be made in writing; specify the financial year concerned; and be made no later than six years after the end of that financial year.⁷⁷ A direction given by ASIC under **proposed section 294B** is not a legislative instrument and therefore cannot be subject to parliamentary scrutiny or disallowance.⁷⁸

Item 17 repeals existing subsection 295(2) of the Corporations Act and substitutes **proposed subsection 295(2)** in its place. The amendment replaces the current requirement for a parent entity to produce not only audited financial statements for itself but also any related consolidated entity, with a requirement to provide only financial statements in relation to the consolidated entity (if required to do so by the accounting standards).⁷⁹ If the entity is required to prepare consolidated financial statements, the Corporations Regulations 2001 will specify supplementary information about the parent entity that is to be included in a note to the consolidated financial statements.⁸⁰ **Item 31** makes a similar amendment in relation to financial statements for the half-year by

73. **Proposed subsection 294A(3)** of the Corporations Act.

74. **Proposed subsection 294B(2)** of the Corporations Act and **proposed table item 103AA** in Schedule 3 to the Corporations Act (which is to be inserted by **item 49** of **Schedule 1** to the Bill). See the discussion about penalty units in footnote 64. It could be argued that because the offence in **proposed subsection 294B(1)** is expressed in terms of a ‘small company limited by guarantee’ rather than by reference to the individual directors of such a company, the offence carries only the penalty as stated in **proposed table item 103AA** in Schedule 3 to the Corporations Act (rather than a penalty of up to five times that amount). On the other hand, however, the fact that the penalty could involve imprisonment tends to support the proposition that the penalty as stated is simply that which would apply to an individual (with the possibility that a court could impose a fine of up to \$5500 on the company).

75. **Proposed subsection 294B(3)** of the Corporations Act.

76. **Proposed subsection 294B(4)** of the Corporations Act.

77. **Proposed subsection 294B(5)** of the Corporations Act.

78. **Proposed subsection 294B(6)** of the Corporations Act.

79. **Proposed subsection 295(2)** of the Corporations Act (which will replace current subsection 295(2)). See **item 17** of **Schedule 1** to the Bill. Similar amendments are made to requirements for half-year financial statements: see **proposed subsection 303(2)** of the Corporations Act (which will replace current subsection 303(2)). See **item 31** of **Schedule 1** to the Bill.

80. Existing paragraphs 295(3)(a) and 303(3)(a) of the Corporations Act.

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repealing existing subsection 303(2) and substituting **proposed subsection 303(2)** in its place.

Item 29 inserts **proposed section 300B** into the Corporations Act. It sets out the matters which a company limited by guarantee must include in its annual directors' report, including:

- the short and long-term objectives of the company
- the company's strategy for achieving those objectives
- the company's principal activities during the year
- how those activities assisted in achieving the company's objectives, and
- how the company measures its performance.⁸¹

If the company is a consolidated entity, it is only required to report on the consolidated entity.⁸² The company's directors' report must also include:

- details of any person who has been a director at any time during or since the relevant financial year
- his or her qualifications, experience and special responsibilities
- the number of meetings of the board of directors during the financial year (and each director's attendance at those meetings)
- the amount which a member of each class of membership is liable to contribute if the company is wound up, and
- the total amount that members are liable to contribute if the company is wound up.⁸³

Item 30 inserts **proposed subsections 301(3) and (4)** into the Corporations Act. **Proposed subsection 301(3)** states that a company limited by guarantee may have its financial report for a financial year *reviewed* (rather than *audited*) if the company is not a Commonwealth company (or a subsidiary of a Commonwealth company or authority), and either:

- the company is not required by the accounting standards to be included in consolidated financial statements and the revenue of the company for the financial year is less than \$1 million, or
- the company is required by the accounting standards to be included in consolidated financial statements and the consolidated revenue of the consolidated entity for the financial year is less than \$1 million.

81. **Proposed subsection 300B(1)** of the Corporations Act.

82. **Proposed subsection 300B(2)** of the Corporations Act.

83. **Proposed subsection 300B(3)** of the Corporations Act.

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Proposed subsection 301(4) states that the financial report of a small company limited by guarantee does not have to be audited or reviewed if:

- the report is prepared in response to a member direction under **proposed section 294A**, and
- the direction does not ask for an audit or review.

Item 40 inserts **proposed section 316A** into the Corporations Act. **Proposed subsection 316(1)** provides that a member of a company limited by guarantee may, by written notice to the company, elect to receive a hard copy or an electronic copy of the company's financial reports, directors' reports or auditor's reports.⁸⁴ An election applies in the year in which it is made and then acts as a standing election for later years (until the member changes the election).⁸⁵ If the company prepares a financial report or a directors' report, or obtains an auditor's report, it must send a copy of the report to the member free of charge before the earlier of (a) 21 days before the company's next annual general meeting (AGM) after the end of the financial year or (b) four months after the end of the financial year.⁸⁶ However, if a member direction is given under **proposed section 294A**, the deadline for sending a copy of the reports is the later of (a) two months after the date on which the direction was given, or (b) four months after the end of the financial year.

A company limited by guarantee that fails to comply with the requirement to provide a copy of relevant reports to a member under **proposed subsections 316A(3) or (4)** may be guilty of a strict liability offence that carries a maximum of 10 penalty units or imprisonment for 3 months or both.⁸⁷ It is clear on the face of **proposed subsection 316A(5)** that any such offence is a strict liability offence.

Items 43 and 44 amend existing section 323D, which provides that a financial year is 12 months long (plus or minus seven days). **Item 44** inserts **proposed subsection 323D(2A)** which allows a financial year subsequent to the first year to last for a period other than 12 months provided that:

84. Note that **item 38** of **Schedule 1** to the Bill (which inserts **proposed subsection 314(1AAA)** into the Corporations Act) and **item 39** of **Schedule 1** to the Bill (which inserts **proposed subsection 316(5)**) provide that the ordinary requirements for the provision of annual reports to members do not apply in relation to a company limited by guarantee (on the assumption that **proposed section 316A** is enacted).

85. **Proposed subsection 316A(2)** of the Corporations Act.

86. **Proposed subsection 316A(3)** of the Corporations Act. Note that section 250N of the Corporations Act sets out the when a company must hold an AGM. See http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s250n.html (viewed 10 June 2010).

87. **Proposed subsection 316A(5)** of the Corporations Act, and **proposed table item 109A** in Schedule 3 to the Corporations Act (which is to be inserted by **item 51** of **Schedule 1** to the Bill). See also the discussion of penalty units in footnote 64.

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- the subsequent financial year starts at the end of the previous financial year
- there has not been a period during the previous five financial years in which there was a financial year of less than 12 months in reliance on this subsection, and
- the change to the financial year is made ‘in good faith in the best interests of the company, registered scheme or disclosing entity’.

Item 45 inserts **proposed section 324BE**, which provides that an individual is taken to be a registered company auditor for the purposes of a *review* (as compared with an *audit*) of a financial report of a company limited by guarantee if the individual:

- is a member of a professional accounting body, and
- holds a practising certificate of the kind specified in the Corporations Regulations 2001.

The Explanatory Memorandum notes that the amendment will expand the category of individuals that are permitted to undertake reviews, which ‘will provide greater flexibility and reduce unnecessary burden on companies limited by guarantee and their auditors, particularly during peak periods’.⁸⁸

The amendments made by **Schedule 1** generally apply to financial years ending on or after 30 June 2010.⁸⁹ However, the amendments in **items 24–28** (which extend the requirement in section 299A to disclose a review of operations and financial condition to all listed entities) only apply to financial years ending on or after 30 June 2011.⁹⁰

Schedule 2—Australian Securities and Investments Commission Act 2001

In summary, **Schedule 2** repeals a number of obsolete provisions in the ASIC Act and modifies the operation of other provisions.

Items 3–5 amend section 203 of the ASIC Act, which set out the conditions for membership of the Companies Auditors and Liquidators Disciplinary Board (CALDB). The CALDB is a disciplinary body which reviews applications made to it by ASIC or the Australian Prudential Regulation Authority (APRA) in relation to the conduct of registered company auditors or liquidators.

Item 3 repeals existing paragraphs 203(1)(c) and (d) and substitutes **proposed paragraph 203(1)(c)** in their place. It provides that the Minister may select six members

88. Explanatory Memorandum, op. cit., p. 12.

89. **Proposed Part 10.14** of the Corporations Act (which contains transitional provisions relating to the proposed amendments made by Part 1 of Schedule 1 to the Bill), which is to be inserted by **item 52** of **Schedule 1** to the Bill. See particularly **proposed section 1510B** of the Corporations Act.

90. **Proposed subsection 1510B(6)** of the Corporations Act.

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who are eligible for appointment as ‘*accounting members*’ of the CALDB. Under the Bill, ‘*accounting members*’ are to be appointed to the CALDB in a way that is similar to the way ‘*business members*’ are appointed to the Board under existing paragraph 203(1)(e).

A person is eligible to be appointed as an ‘*accounting member*’ if the person is an Australian resident and also a member of a professional accounting body (or such other body as is prescribed by the regulations for the purposes of the provision).⁹¹ There are three professional accounting bodies in Australia: the Institute of Chartered Accountants in Australia (ICAA); CPA Australia (CPAA) and the National Institute of Accountants (NIA). However, there are other professional bodies, such as the Insolvency Practitioners Association of Australia (IPAA), which are currently ineligible to nominate members of the CALDB. Under the Bill, such bodies could be prescribed for the purposes of **proposed subparagraph 203(1B)(b)(ii)**, which would mean that a member of such a body, who is also an Australian resident, would be eligible for the Minister to select him or her as an ‘*accounting member*’ of the CALDB under **proposed paragraph 203(1)(c)**.

Items 7 and 8 amend existing section 221 of the ASIC Act to insert **proposed subsections 221(1A) and (2A)**. Existing section 221 confers immunity consistent with that of a Justice of the High Court of Australia on panel members of the CALDB when exercising powers in relation to a hearing. Witnesses, legal and other representatives also receive a similar immunity. However, at present, the immunity does not extend to cover pre-hearing conferences convened by the Chairperson of the Board under section 1294A of the Corporations Act.⁹² **Item 7** extends the immunity to the Chairperson of the Board in the performance of his or her functions in relation to such a conference, and **item 8** extends the immunity to any barrister, solicitor or other person appearing on behalf of a person at a conference. The amendments made by **items 7 and 8** apply in relation to all pre-hearing conferences convened by the Chairperson of the Board, including conferences conducted before the commencement of **Schedule 2**.⁹³

Items 10 and 12 of **Schedule 2** repeal paragraphs 225(2)(i) and (j) and paragraphs 225(2A)(i) and (j) of the ASIC Act. Those provisions gave specific accounting and auditing standards functions to the Financial Reporting Council, but are no longer required following the enactment of the *Governance Review Implementation (AASB and AUASB) Act 2008*.

91. **Proposed subsection 203(1B)** of the ASIC Act, as repealed and substituted by **item 5** of **Schedule 2** to the Bill.

92. The text of section 1294A of the Corporations Act is available at http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/s1294a.html (viewed 10 June 2010).

93. **Proposed section 291** of the ASIC Act (which is inserted by **item 13** of **Schedule 2** to the Bill).

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