CHAPTER 3

ENVIRONMENTAL REPORTING

Introduction

3.1 The *Company Law Review Act 1998* among other things inserted s.299(1)(f) into the Corporations Law. The paragraph provides as follows:

> **Annual directors' report – general information**
>
> **299(1) [General information about operations and activities].** The directors' report for a financial year must:
>
> **…**
>
> (f) if the entity's operations are subject to any particular and significant environmental regulation under a law of the Commonwealth or of a State or Territory – details of the entity's performance in relation to environmental regulation.

3.2 The Government indicated that it opposed the amendment and referred the matter to the PJSC for inquiry.

3.3 The PJSC received 46 submissions which addressed this topic, of which 6 were in favour of the provision and 40 opposed to it.

Arguments against the submission

Environmental reporting is inappropriate for the directors' report

3.4 A number of submissions advised that the environmental reporting requirement was inappropriate. Mr R I Barrett submitted that the annual report contents, as mandated by the Corporations Law, concentrated on matters of clear relevance to an informed assessment of the company's financial position and performance. They were not designed to encourage conduct that is responsible according to some broader social criterion. If disclosure of certain conduct is seen as necessary or desirable from some public interest or social standpoint unrelated to a company's financial standing, that issue should be addressed quite separately from the Corporations Law. In this context the United States securities laws do not require disclosure on environmental compliance simply for the sake of disseminating information about a company's environmental practices. The emphasis is on financial effects for the information of creditors and shareholders, that being the proper province of corporate regulation. The matters which are disclosed are related clearly to proper reporting of a company's financial position. The Australian Law Reform Commission submitted that to the extent that environmental reporting is necessary and justified it should form part of the environmental law itself. It should also form part of

the technical benchmarks prescribed by that law. The Australian Society of Certified Public Accountants, the Institute of Chartered Accountants in Australia and the Chartered Institute of Company Secretaries (W.A.) submitted that such reporting may have some merit but should be in environmental legislation not the directors' report.

3.5 Freehill Hollingdale and Page (Perth) submitted that this is not a corporations issue and should not be in the Corporations Law. The degree of such reporting should be set by environmental agencies. The Australian Industry Group submitted that ASIC was being made a de facto environmental agency. The Australian Institute of Company Directors (AICD) submitted that the provision duplicated regulatory authorities; ASIC were a new environmental regulatory agency.

3.6 The AICD further submitted that the requirement lacked any clear objective. It would do little to provide either environmental or financial information to debt and equity investors or to the public and is unlikely to focus directors' attention on appropriate corporate environmental behaviour. The National Association of Forest Industries (NAFI) submitted that the requirement serves the interest of non-shareholders rather than shareholders. Mr J A Sutton submitted that the provision was unnecessary. The Australian Chamber of Commerce and Industry (ACCI) submitted that the legislative approval is too doctrinaire and disproportionate to the issue it seeks to address. Blakiston and Crabb submitted that the provision was prescriptive and contrary to the simplification thrust of the *Company Law Review Act 1998.* Mr Timothy Walshaw submitted that the Corporations Law was not the appropriate venue for this type of information. Companies' officers and auditors should not be used to enforce compliance in areas in which they are not qualified. Rio Tinto submitted that the provision was incongruous, given the mainly financial basis of the Corporations Law.

Environmental performance should not be singled out for mandatory reporting

3.7 A number of submissions advised that environmental performance should not be singled out for mandatory inclusion in the annual directors' report. The Australian Law Reform Commission questioned whether such sector specific obligations have a place in the Corporations Law, which is designed to be of general application. Arnold Bloch Leibler asked why environmental performance had this special status and whether this meant that everything else was of lesser importance. The Australian Industry Group (AIG) submitted that there was no other regulatory reporting in s.299. Mr John Wilkin (Corrs Chambers Westgarth) submitted that if it involved reporting breaches of the law why did it not include, for instance, breaches of tax and other regulation.

3.8 KPMG submitted that companies should not be required to report compliance with some laws but not others. The Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants in Australia asked why other categories of non-financial information were not included. Mr R I Barrett submitted that it was not logical to single out one particular cause of financial risk or burden to the exclusion of others. Mr Timothy Walshaw submitted that the provision could open

the door to numerous other reporting requirements which are the fashion from time to time, such as occupational health and safety or affirmative action. Ernst and Young (Melbourne) asked why this area of social responsibility should be different to any other. Six other submissions made the same general point.

Voluntary reporting is preferable

3.9 A number of submissions advised that the quality of disclosure under the provisions would not be high. Voluntary rather than mandatory environmental reporting would produce the best results. The Australian Law Reform Commission submitted that the breadth of language of the provision is such that the likely result is generalised reporting of little use or benefit to shareholders. Blakiston and Crabb submitted that reporting would likely become a standard format. The CPA/ICA/CICS (W.A.) submitted that the requirement would be honoured by good companies and avoided by the bad ones. The Australian Listed Companies Association Inc. submitted that reporting would become a meaningless but not onerous general statement. The Australian Institute of Petroleum (AIP) submitted that environmental reporting should be left to the board of each company, with the government and shareholders developing suitable guidelines. The Australian Business Chamber submitted that the voluntary approach is preferable. The Australian Petroleum Production and Exploration Association (APPEA) submitted that compulsion is inappropriate. Rio Tinto Limited submitted that it and other major companies produced good quality stand-alone environment reports without a legislative requirement.

3.10 The AIG submitted that the provision for mandatory reporting was introduced even though there was no evidence that voluntary reporting had been unsuccessful. The preference in Australia has been to encourage company environmental reporting along voluntary lines. The United States experience of mandatory reporting is that it leads to a minimum common standard. The NAFI submitted that the provision would result in a lowest common denominator, making it harder to distinguish between the companies with good and bad environmental records. It would become harder rather than easier to identify environmental performance from company reports. Under the previous voluntary arrangements there was an opportunity for companies to demonstrate best practice.

The provision is vague and unclear

3.11 A number of submissions advised that the provision was uncertain and not well drafted. Allen Allen and Hemsley submitted that the provision was unclear. For instance, did it apply to trivial and technical breaches and to compliance with all standards? The Henry Walker Group submitted that there was no appropriate threshold for the operation of the provision. The Chartered Institute of Company Secretaries submitted that it was too vague for any meaningful disclosure. The Australian Institute of Petroleum submitted that the provision was vague and unworkable. Esso Australia Resources Ltd submitted that the provision was impractical and bound to cause confusion. Ernst and Young, Sydney, submitted that it was far too broad. The Australian Business Chamber submitted that it lacked clarity and a minimum level of detail. The Association of Mining and Exploration

Companies Inc (AMEC) submitted that the application of the provision was a matter of speculation. The AICD submitted that it was subjective with no definitions. The AICD and the Business Council of Australia (BCA) both submitted that interpretation was an issue, both in determining when the reporting obligation was triggered and, if triggered, the nature of the requirement. The APPEA submitted that it was uncertain in scope and application. KPMG submitted that the provision was open to differences of interpretation. The CPA submitted that it was subjective and thus could be unreliable; it was premature and needed more debate. The CPA/ICA/CICS (W.A.) submitted that the provision was subjective, leading to possible avoidance.

3.12 A number of submissions advised that the drafting of the provision was deficient. The AIG submitted that the provision had no verb, there were differences in the qualification of when an entity must report and that it came under the general reporting provision when it should have been included in the specific reporting provisions. The AICD and the BCA both criticised the grammar of the provision.

3.13 Arthur Anderson submitted that the provision did not require reporting in relation to overseas environmental performance.

Absence of appropriate safeguards

3.14 A number of submissions advised that the provision did not include appropriate safeguards in relation to its exercise. Allen Allen and Hemsley submitted that s.299(3) provided that prejudicial information about other aspects of s.299 need not be disclosed, but that there was no such safeguard for environmental reporting. There was no protection against self-incrimination, which the High Court has held to be absolutely fundamental. Also disclosure under the provision may prejudice the company in any civil proceedings in which it is engaged. The Victorian Minister for Fair Trading, Ms Jan Wade MP, also submitted that the provision might infringe the privilege against self-incrimination. Siddons Ramset Limited submitted that the provision implies an assumption of guilt with the onus on the company to disprove this.

3.15 Freehill Hollingdale and Page (Perth) submitted that Listing Rule 3.1, which requires a listed company to disclose any information material to the value of its securities, is subject to safeguards. There are no such safeguards, however, for this provision, which could force a company to make admissions which could be used against it in litigation or for environmental liability claims. Also, lobby groups could make harmful use of immaterial breaches.

Listed companies must already disclose material information

3.16 A number of submissions advised that companies must under the ASX listing rules already report material information, which included environmental performance. Freehill Hollingdale and Page (W.A.) submitted that Listing Rule 3.1 requires companies to disclose immediately any information which would have a material effect on the price or value of their securities. Bristile Ltd submitted that material events must be reported under the continuous disclosure rules and it is not justified to

report on immaterial events. The AMEC submitted that given the listing rules the provision is an unnecessary duplication and complication of the process. There were problems with extending the process to non-material issues. Blakiston and Crabb submitted that the listing rules were adequate. Four other submissions made the same general point.

The provision does not apply to all legal structures

3.17 A number of submissions advised that environmental reporting should not depend on legal structure. Freehill Hollingdale and Page (W.A.) submitted that environmental law applies to all legal structures, not just companies. Mr R I Barrett submitted that if such disclosure was thought necessary then it should not apply only to companies formed under the Corporations Law.

3.18 The APPEA submitted that the effect of the provision on joint venture arrangements was unclear. Virtually all exploration and production of oil and gas is undertaken by unincorporated joint ventures; one participant usually reports to the appropriate authorities on environmental performance. All joint participants are jointly and severally liable for actions of the joint venture. Some participants have an interest of less than 1%. Esso Australia Resources Ltd submitted that in the upstream petroleum industry operations are usually owned by a number of unrelated legal entities via joint ventures. Environmental reporting has been done on an operations basis not an entity basis. If relevant information is apportioned and separately reported it will be less transparent. Rio Tinto Limited submitted that in the case of a large listed group of companies, which prepares financial statements on a consolidated basis, it is an unnecessary administrative burden to require subsidiary companies in the group to report separately.

The provision adds an unnecessary cost

3.19 A number of submissions advised that the requirement imposes an additional and unnecessary cost. Mr Ian Cochrane submitted that reporting obligations are extensive enough already without adding to the burden. The Henry Walker Group submitted that there was a vast amount of environmental legislation with which companies must comply. Mr John Wilkin submitted that if companies were complying with environmental regulations then reporting this was a burden and expense with no benefit to anyone. The Australian Institute of Petroleum submitted that costs are high for extensive reports. The Australian Industry Group submitted that costs could be high. The Australian Business Chamber submitted that there could be high costs for such open ended mandatory reporting. The Victorian Minister for Fair Trading, Ms Jan Wade MP, submitted that the provision could impose significant additional costs on small and medium business enterprises. Mr Timothy Walshaw submitted that the provision raised significantly the cost of reports; the aim of business law reform should be to reduce, not increase the cost of doing business. The AMEC submitted that the provision was unnecessary and flew in the face of company law simplification.

3.20 A number of submissions advised that the provision duplicated other requirements. The AIP submitted that compliance was already reported to environmental agencies. Gunns Ltd submitted that there were existing processes for reporting to government agencies. Esso Australia Resources Ltd submitted that the provision duplicated State requirements. The ACCI submitted that it was an additional regulatory burden on business, which duplicated Commonwealth and State legislation. The AICD submitted that it duplicated existing and future requirements. The APPEA submitted that it duplicated other reporting requirements, which resulted in cost but little benefit.

Arguments in favour of the provision

3.21 The PJSC received submissions from two environmental organisations.

Greenpeace Australia

3.22 Greenpeace Australia submitted that there is little dispute that environmental issues are the most significant challenge that humanity faces. One common theme to the solution of these problems is the role of the corporate sector in changing the practices which have produced them. The provision is a positive proactive step which has the potential to produce significant environmental and economic benefits. There may be some teething difficulties but this is not an excuse to abolish the provision.

3.23 There are potential benefits in the provision for business, the environment and government;

- business benefits in two main ways; through potential cost savings in better environmental behaviour and through goodwill with the community. A number of business groups have referred publicly to these benefits.

- the environmental benefits are mostly self-evident. Public interest and concern about environmental issues remains high.

- the government benefits because agencies do not have enough resources to police environmental laws. Mandatory reporting can assist here and make environmental regulation more effective.

3.24 Environmental reporting should be compulsory because the voluntary system is clearly not adequate. The level of reporting in Australia is unsatisfactory and lags behind other countries. Enforcement of the provision should be through an enhanced ASIC practice note, which would include guidelines and minimum standards.

3.25 There are adequate responses to criticisms of the provision;

- as noted above, the voluntary system is not sufficient. The majority of companies have not done the right thing and must now be compelled. There will be no extra costs for the better companies and the rest will now be on a level playing field.

- there will always be some confusion and misunderstanding when a new system is introduced, but other provisions are also imprecise. The only companies that will have a problem are those with something to hide.

- while there may be a problem with the volume of environmental laws this is not an argument for voluntary reporting. Instead, the environment laws may need to be rationalised, with one set of Federal laws.

- there may be high potential costs for directors who sign off on compliance, but this is a positive feature of the new provision. The potential for penalties will focus the minds of directors.

3.26 This positive new provision should be given a chance to work. ASIC should take immediate steps to clarify its operation.

The Environmental Defender's Office Ltd

3.27 The EDO submitted that the provision is a progressive move which is both welcome and necessary. Before the provision the public had little, if any, information about company compliance with environmental law. There are a number of reasons for company environmental disclosure;

- it provides information to economically motivated investors. This information is important for shareholders to make informed investment decisions.

- it provides information to environmentally motivated investors. An increasing number of investors, both institutional and private, are making non-economic decisions when making investment decisions. In this context, financial concepts of materiality should not apply.

- it provides information to environmental regulators. Limited liability may sometimes be an incentive for socially irresponsible conduct by some companies. Therefore there is a need to regulate corporate environmental conduct and regulators must be informed to be effective.

- it provides information to the general public. Community right to know laws shift the focus of environmental law from a reactive crisis-by-crisis approach towards citizen and government monitoring of existing and potential hazards.

3.28 Australian company environmental reporting has been poor. The provision attempts to reverse this trend and make environmental disclosure meaningful. There have been concerns about the provision but these can be met largely by the existing ASIC Practice Note 68, which could be further refined.

Other submissions in favour of the provision

3.29 MAI Services Pty Ltd submitted that the provision was essential as a step for environmental stakeholders to replace government regulators. Corporations must prepare this information in any event and it would cost little to distribute

electronically to their shareholders. Mr Stan Rodgers submitted that companies are already required to report to State authorities so it would not cost more to report again. Shareholders need to know about weaknesses in a company's control systems, which could affect the share price. Mr R Furlonger agreed with the provision, on the principle of maximum disclosure. Mr Jack Tilburn agreed with the provision.

Conclusions

3.30 The PJSC concluded that it was inappropriate for the Corporation Law to require inclusion in the annual directors' report of details of performance in relation to environmental regulation. The PJSC noted and accepted the almost total unanimity of view on this point of submissions from the Australian financial and legal communities.

3.31 Environmental reporting is not a matter which relates to the Corporations Law. Environmental performance may be an important issue but it should be addressed through avenues other than the Corporations Law. The proper place for such reporting is the environment law itself.

3.32 The PJSC asks why the provision singled out environmental performance to the exclusion of other presumably worthwhile performance indicators. There is no other regulatory reporting in s.299. Presumably this means that, for instance, performance in taxation regulation or occupational health and safety regulation are less important for sector specific purposes of the Corporations Law than environmental performance.

3.33 Mandatory reporting of environmental performance may be unproductive. Compulsion may lead to mediocrity and blandness in environmental reporting, with companies using a standardised form of general words as the lowest common denominator. The voluntary system would encourage better companies to achieve best practice in this area, while the market will deal adversely with those companies which lag.

3.34 The provision is vague and uncertain, which could lead to subjective interpretation. These deficiencies are basic and, in the opinion of the PJSC, cannot be solved by simply asking ASIC to refine a practice note. The PJSC is grateful for the oral evidence given to it on this point by Ms Jillian Segal, Commissioner, ASIC.

3.35 The provision is significantly deficient in that it lacks any of the usual safeguards, even those included for other provisions of s.299. There is no protection against self-incrimination or in relation to civil proceedings or other liability claims. It also lacks the safeguards provided by Listing Rule 3.1. These deficiencies appear to be fundamental.

3.36 There is an existing obligation on listed companies to disclose immediately all events which would have a material effect on the price or value of its securities. Any additional information required by s.299(1)(f) would be non-material and up to a year after the event. The practical effect of the provision would therefore appear limited.

3.37 There are significant legal or economic structures to which the provision does not apply. For instance, it does not apply to overseas operations of entities formed under the Corporations Law. It is ironic that the express environmental reporting requirement does not include overseas performance, whereas the Listing Rules do include such material events overseas. Also the provision requires entity rather than project reporting for mining and exploration joint ventures. These matters have the potential to limit and distort the use of such environmental performance reporting.

3.38 The provision requires companies to duplicate existing Commonwealth and State environmental reporting requirements, with resulting additional costs.

3.39 The two submissions from environmental groups put different views to the above conclusions. These views, however, were not as persuasive as those from the business community.

Recommendation

3.40 The Committee recommends that s.299(1)(f) of the Corporations Law be deleted.