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28 November 2003

The General Manager
Corporations and
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Department of the Treasury
Langton Crescent
PARKES ACT 2600

The Secretary
Parliamentary Joint Committee
on Corporations and Financial
Services
Suite SG-64
Parliament House
CANBERRA ACT 2600

Dear Sirs

**CLERP (AUDIT REFORM & CORPORATE DISCLOSURE) BILL 2003
("CLERP 9")**

Three reforms, proposed to be introduced by CLERP 9 are, in the submission of the Task Force, flawed to such a degree that they ought not to proceed. They are:

- the grant to the ASIC of a power to impose financial penalties and issue infringement notices for contraventions of the ASX's continuous disclosure regime
- the establishment of a financial reporting panel to resolve disputes between the ASIC and companies in the application of accounting standards to financial reports, and
- the requirement for a listed company to submit their annual remuneration package to a non-binding vote at the company's annual general meeting.

Each of the first two proposed reforms seeks to attract to, respectively, the Commonwealth and a panel of Commonwealth appointees, particular functions presently placed in the Judiciary.

Each of the first two reforms marks a preference for a less expensive, less effective, regulatory and enforcement regime.

The third reform contemplates an unwieldy middle ground that is at odds with the organic theory of companies and the law applying to permit holders of fiduciary office to derive benefits from their office.

Each of the proposed reforms is further discussed below.

1. *ASX and continuous disclosure*: Matters of continuous disclosure involve difficult questions of degree. They are not straightforward, like the determination of a parking fine or a speeding ticket. They usually also involve the weighing of other laws, in a complex factual matrix.

It is submitted that the ASIC is neither well placed nor well skilled to undertake this function. The fines and penalties in contemplation are also not insignificant.

Nor is it seized of jurisdiction to consider matters of State and common law that will invariably also apply – eg. *Fair Trading Act* breaches and negligent misstatements.

The ASIC will also be acting as both prosecutor and the determiner of a matter.

2. *Financial Reporting Panel*: The replacement of Court functions by Panel determination is also not supported in this context. Panel members are not judicially trained, and many, if not most, are unlikely to be legally trained. Nor are they seized of the jurisdiction, the power or the competence to effectively consider and decide upon matters beyond the bounds of the accountancy standards. For example, underlying fraud, witness credibility, or other applicable State or Commonwealth laws will not be best appreciated and determined upon.

It is also submitted that the degree of scrutiny of those who are appointed to Panel membership, and their existing relationships and continuing direct and indirect pecuniary and other interests, is not considered or monitored in the depth and detail as operates for Judicial appointments. Could Panel decisions be influenced in any way by a desire to not stray outside accounting standard competency? Or a willingness to maintain the Panel member's reputation or his or her firm's client base, corporate opportunities or investments in any way? These are live issues.

3. *Non-binding remuneration vote*: Subject to contrary provision in statute or the ASX's Listing Rules, organic corporate theory vests, respectively, powers of a company's members in general meeting and powers of a company's Board in those two organs, as those powers may be specified in the particular company's Constitution.

As to remuneration of directors or employees, the power to determine these matters is generally placed in the hands of the Company's Board,

generally as a matter of management, with an express permission allowing the Company's Board to act notwithstanding their interest in the matter. Under this modern arrangement, however, and subject to contrary provision in statute or the ASX Listing Rules, the Board alone would determine matters of remuneration.

Under a traditional fiduciary regime, the persons to whom the fiduciary duties are owed will determine upon whether or not those who owe the duty may derive a benefit in the course of the exercise of their fiduciary powers. In this instance, generally, subject to contrary provision in any contract or deemed statutory contract (such as a company constitution) the members alone would determine the remuneration of those who owe them the fiduciary duty.

Where statute or the ASX Listing Rules divert from the modern position described above, to require matters to be dealt with by members, rather than the Board, notwithstanding provision to the contrary in the company's Constitution, the members are afforded a determinative, binding, vote. Two examples of this situation are:

- Chapter 2E, *Corporations Act 2001* – related party benefits, and
- Chapter 10, *ASX Listing Rules*.

The reform proposal, in providing for a non-binding vote, neuters the power of the members in general meeting. It seems to rely on "shame" and "reputation" motives, without providing for a resolution of the matter. A Board may, notwithstanding the passage of a non-binding members' vote against a remuneration package, ignore the members' resolution and proceed to implement the submitted remuneration package. Conflict in this situation is heightened. The matter in conflict is not resolved.

Rather than a measure that is designed to protect shareholders, the Task Force is of the view that in time the members' position will be weakened. They become a collective toothless tiger.

The reform would be better couched as either a binding vote in all cases, or a binding vote in specified cases. A non-binding vote is not a matter previously known in company law. It is an unwelcome development. The present provision in s 211 of the *Corporations Act 2001* is preferred to the reform proposal.



The Task Force invites you to carefully consider these submissions and not proceed with the proposed reforms discussed.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Daren Armstrong', written over the printed name.

Daren Armstrong

Secretary

Legislative Review Task Force

Commercial Law Association of Australia Limited