

# **CORPORATIONS AMENDMENT (CORPORATE REPORTING REFORM) BILL 2010**

## **DRAFT REGULATORY IMPACT STATEMENT**

### **BACKGROUND**

A robust financial reporting framework is an essential component of an efficient market. Appropriate financial reporting and auditing requirements enhance the accuracy of financial information, ensure transparency and comparability and promote confidence.

The proposed reforms seek to reduce red-tape, improve accountability and transparency of disclosures, and implement a number of other important refinements to the corporate regulatory framework. This work would also ensure that Australia's financial reporting framework remains strong and in line with or ahead of world's best practice. An overview of each of the recommended options is set out below.

#### **Reducing red-tape**

The proposals that are designed to cut red-tape in financial reporting with a view to reducing the regulatory burden on business include:

- simplifying financial reporting requirements for smaller companies limited by guarantee (which predominantly have a not-for-profit focus);
- relieving companies that are parent entities of the requirement to prepare financial statements for both the parent entity and the consolidated group;
- relaxing the statutory requirement that companies may only pay dividends from profits; and
- facilitating a change of balance date by a company.

#### **Improving accountability**

The proposals enhance the transparency and utility of disclosures contained in the directors' report include extending the requirement to disclose a review of operations and financial condition to all listed entities (currently, these requirements apply to listed public companies).

#### **Refining the framework**

The proposals for refining aspects of the financial reporting framework include:

- protecting solicitors' representation letters from disclosure, in response to the decision in *Westpac Banking Corporation v 789 Ten Pty Ltd* [2005] NSWCA 321, which held that such correspondence is not protected by client legal privilege; and
- amending the directors' declaration to refer to compliance with International Financial Reporting Standards (IFRS).

## IDENTIFICATION OF OPTIONS, IMPACT ANALYSIS, CONCLUSIONS AND RECOMMENDATIONS

### Impact assessment methodology

Impacts can be divided between three impact groups (consumers, business and government). Typical impacts of an option on consumers might be changes in access to a market, the level of information and disclosure provided, or prices of goods or services. Typical impacts of an option on business would be the changes in the costs of compliance with a regulatory requirement. Typical impacts on government might be the costs of administering a regulatory requirement. Some impacts, such as changes in overall confidence in a market, may impact on more than one impact group.

The assessment of impacts in this regulation statement is based on a seven-point scale (-3 to +3). The impacts of each option are compared with the equivalent impact of the 'do nothing' option. If an impact on the impact group would, relative to doing nothing, be beneficial, the impact is allocated a positive rating of +1 to +3, depending on the magnitude of the relative benefit. On the other hand, if the impact imposes an additional cost on the impact group relative to the status quo, the impact is allocated a negative rating of -1 to -3, depending on the magnitude of the relative cost. If the impact is the same as that imposed under the current situation, a zero score would be given, although usually the impact would not be listed in such a case.

The magnitude of the rating of a particular impact associated with an option has been assigned taking into account the overall potential impact on the impact group. The reference point is always the status quo (or 'do nothing' option). Whether the cost or benefit is one-off or recurring, and whether it would fall on a small or large proportion of the impact group (in the case of business and consumers), is factored into the rating. For example, a cost or benefit, even though large for the persons concerned, may not result in the maximum rating (+/-3) if it is a one-off event that only falls on a few individuals. Conversely, a small increase in costs or benefits might be given a moderate or high rating if it would be likely to recur or if it falls on a large proportion of the impact group. The rating scale for individual impacts is explained in the table below.

#### Rating an individual impact

+3	+2	+1	0	-1	-2	-3
Large benefit/ advantage compared to 'do nothing'	Moderate benefit/ advantage compared to 'do nothing'	Small benefit/ advantage compared to 'do nothing'	No substantial change from 'do nothing'	Small cost/ disadvantage compared to 'do nothing'	Moderate cost/ disadvantage compared to 'do nothing'	Large cost/ disadvantage compared to 'do nothing'

The ratings for the individual impacts compared to the status quo are then tallied to produce an overall outcome for the option. If it is positive, it indicates that the option is likely to produce a more favourable cost/benefit ratio than the status quo. If it is zero there would be no overall benefit from adopting the option, and if negative the option

would provide overall a less favourable cost/benefit ratio than the ‘do nothing’ option. Ordinarily, options that have the highest positive score would be the favoured courses of action.

What is classed as a ‘large’, ‘moderate’ or ‘small’ cost or benefit depends on the nature of the problem and options being considered. Of course, the costs and benefits associated with options to address a problem costing billions of dollars per year are likely to be of a much greater absolute magnitude than the costs and benefits of options for dealing with a rather modest issue that affects only a handful of persons. However, as all the ratings are made relative to the status quo/ do nothing option for a particular problem, the absolute value of ‘large’ or ‘moderate’ or ‘small’ is not really important. All that matters is that within a problem assessment, the impacts of each option are given appropriate ratings relative to the status quo and each other. If that occurs, it will be sufficient for the methodology to yield an overall rating that assists in assessing the relative merits of options, from a cost/benefit perspective, to address the particular problem.

An example of the rating calculation for an option, using the seven-point scale ratings of impacts, is in the table below. The example is based on a purely hypothetical scenario that a new type of long-wearing vehicle tyre is being sold and marketed, but it has become apparent that the new style of tyres have a higher risk of exploding while in motion than conventional tyres. The example is designed merely to illustrate how the rating scale might be used to compare a proposal’s costs and benefits option to the ‘do nothing’ option — it is not intended to be a comprehensive or realistic assessment of options to address such a problem.

### **Illustrative rating for the problem of a long-wearing tyre that may fail**

#### **Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Consumers	Access to a cheaper solution for vehicle tyres	Risk of tyre failure that can result in personal and property damage as a result of collision. Damage can be severe but cases are rare
Industry		Some compensation payments to persons as a result of collisions caused by the tyre
Government	Advantages for waste management perspective	

#### **Option B: Ban on sale of the new tyre**

	<b>Benefits</b>	<b>Costs</b>
Consumers	No persons will be affected by tyre failure and resultant damage (+3)	Lack of access by consumers to long-wearing vehicle tyres, increasing the cost of vehicle maintenance [-2]
Industry	No compensation payments for accident victims [+1]	Transitional costs involved with switching back all manufacturing/marketing operations to

Government		conventional tyres [-3]	Conventional tyres produce more waste which is costly to deal with [-1]
Sub-rating	+4		-6
Overall rating		-2	

**Option C: Industry-developed quality control standards**

	Benefits	Costs
Consumers	Much lower risk of tyre failure and resultant damage than status quo [+2]	
Industry	Significantly less compensation payments for accident victims [+1]	Developing and monitoring industry-wide quality control standards [-2]
Government		
Sub-rating	+3	-2
Overall rating		+1

In the above hypothetical example, Option C appears to have a better impact for consumers and a better overall cost/benefit rating than Option B.

## **SIMPLIFYING THE REPORTING AND AUDITING REQUIREMENTS OF COMPANIES LIMITED BY GUARANTEE**

### **Problem**

Currently, all public companies, disclosing entities, large proprietary companies and registered schemes are required to prepare a full audited annual report in accordance with Australian accounting standards. As a result, the requirement to prepare a full audited annual report also applies to all public companies limited by guarantee, regardless of their size. Consequently, companies limited by guarantee are required to comply with the same level of reporting and auditing requirements as a large listed company.

The company limited by guarantee structure is used predominantly by not-for-profit entities to incorporate their operations. There are approximately 11,000 companies limited by guarantee, the majority of which are relatively small. Research conducted by The University of Melbourne found that 21 per cent of companies limited by guarantee were sports and recreation related organisations, 19 per cent were community service organisations, 15 per cent were education-related institutions and 10 per cent were religious organisations.

Given that companies limited by guarantee are mostly small not-for-profit entities, the current financial reporting requirements can impose onerous costs and regulatory burden in the form of preparation costs, audit costs, printing and distribution costs. Quantifying such costs can be difficult, as they vary significantly depending the size and complexity of the report. It is estimated that the average cost of preparing and auditing an annual report is \$60,000 per company. This figure is based on approximate costs obtained in relation to large proprietary companies.

The table below outlines the relative size of companies limited by guarantee based on a sample of companies that lodged financial reports with the Australian Securities and Investments Commission (ASIC). The small size of companies limited by guarantee means that the costs of extensive reporting requirements are disproportionate to the size of the entity. However, reporting by such companies is also an important governance and transparency mechanism, particularly for larger companies or companies that seek donations from the public, as it provides users with information on how their donations have been spent, how the company is performing and how it is being managed.

**Table 1: Size of companies limited by guarantee<sup>1</sup>**

	Revenue (%)	Cumulative Total: Revenue (%)	Assets (%)	Cumulative Total: Assets (%)
<b>Less than \$20,000</b>	14	14	12	12
<b>Between \$20,000 and \$50,000</b>	9	23	9	21
<b>Between \$50,001 and \$250,000</b>	24	47	16	37
<b>Between \$250,001 and \$500,000</b>	7	54	8	45
<b>Between \$500,001 and \$1,000,000</b>	14	68	18	63
<b>Between \$1,000,000 and \$12,500,000</b>	28	96	30	93
<b>Greater than \$12,500,000</b>	4	100	5	100

## Objective

The objective is to reduce the regulatory burden and administration costs for small companies limited by guarantee to allow greater resources to be devoted to their not-for-profit work, whilst ensuring that large companies limited by guarantee or companies that seek tax deductible donations from the public remain accountable and transparent.

## Options

### Option A: Do nothing

Under this option, all companies limited by guarantee would continue to prepare a full audited annual report in accordance with Australian accounting standards regardless of their size.

This would require a company limited by guarantee to provide the same level of annual reporting as companies listed on the Australian Stock Exchange. As noted above, it is estimated that the average cost of preparing and auditing an annual report is \$60,000 per company, although this would vary depending on the size and complexity of the report.

A significant proportion of companies limited by guarantee (almost half) have consolidated revenue of less than \$250,000, resulting in the compliance costs that are disproportionate to the size of the organisation.

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<sup>1</sup> Based on sample data provided by ASIC on 3 November 2006.

**Option B: Establish a differential reporting and auditing framework and streamline requirements**

Under this option, small companies limited by guarantee would be exempt from preparing audited financial reports and directors' reports under Chapter 2M of the Corporations Act. Large companies limited by guarantee, or companies that seek tax deductible donations from the public, will continue to prepare financial reports with simplified auditing and directors' report requirements.

It is proposed that the threshold be determined by reference to the company's consolidated revenue. Tests based on assets or number of employees may not be accurate indicators of the "size" of the company. For example, a company limited by guarantee may have a large number of assets, but there may be restrictions on the company disposing of these assets. In addition, indicators based on employee numbers are likely to be distorted by the large number of volunteers that generally participate in not-for-profit entities. This is also consistent with the recommendations of the recent Senate Economics Committee report on the disclosure regimes for not-for-profit organisations, which recommended the introduction of a tiered reporting system based on revenue thresholds.

In addition, it is proposed that the threshold be set at \$250,000 of consolidated revenue. Companies below this threshold would be exempt from the reporting and auditing requirements of Chapter 2M of the Corporations Act, unless they are a deductible gift recipient. As indicated in Table 1 above, 47 per cent (or approximately one half) of companies limited by guarantee would fall below the \$250,000 threshold. On balance, this is considered to be an appropriate threshold, as it would ensure that the remaining half is still required to prepare financial reports. Appropriate safeguards will be put in place by requiring companies below this threshold to prepare a financial report if they are directed to by ASIC or by 5 per cent of members (similar to the requirements applying to small proprietary companies in sections 293 and 294 of the Corporations Act).

Some types of companies limited by guarantee will have a higher level of public interest due to the nature of their activities. Charities, for instance, generally fall within this category because of their public fundraising activities (for example, donation drives) and significant community involvement. In contrast, member-focused companies limited by guarantee (for example, sporting clubs) may have a significantly lower level of public interest. Such factors need to be considered when differentiating between companies limited by guarantee for reporting purposes. As such, it is proposed that all deductible gift recipients (that is, companies which seek tax deductible donations from the public) continue to prepare a financial report, irrespective of whether they fall above or below the threshold.

Companies above the threshold, or companies that seek tax deductible donations from the public, would continue to prepare financial reports in accordance with Australian Accounting Standards. However, these companies will have simplified directors' report requirements, as they will prepare a summarised directors' report containing approximately five key qualitative disclosures (rather than a full directors' report which would typically require compliance with sections 299 and 300). The existing directors' report disclosure requirements for companies include a large number of provisions that are not relevant for not-for-profit companies. These include disclosures relating to the payment of dividends and options issued to directors as remuneration. In addition, it is noted that not-for-profit companies are generally purpose or objective driven. As such, stakeholders in not-for-profit companies are likely to be particularly interested in the objectives of the organisation and how the activities conducted during the period contributed achieving those objectives. By creating a set of tailored, non-financial

disclosure requirements for companies limited by guarantee that recognises the not-for-profit nature of these entities, the proposal will result in more relevant information being provided to stakeholders whilst reducing the range of reporting requirements currently imposed on companies limited by guarantee.

Companies above the threshold will also have simplified auditing requirements if their consolidated revenue is below \$1 million. Such companies would have the option of having either a full audit or a review of the financial report conducted by a registered company auditor or by a member of a professional accounting body with a practising certificate. This will streamline the auditing requirements for a further 21 per cent of companies limited by guarantee. Companies with a consolidated revenue greater than \$1 million will continue to be required to undertake a full audit of the financial report by a registered company auditor.

In addition, other minor and technical amendments would be implemented, such as providing streamlined methods for companies limited by guarantee to distribute the annual report to their members and removing the ability of companies limited by guarantee to pay dividends as their corporate structure means they are not suited for conducting for-profit activities which could legitimately warrant the payment of dividends to members.

### **Option C: Exempt all companies limited by guarantee from reporting and auditing requirements irrespective of size**

Under this option, all companies limited by guarantee, regardless of their size, would be exempt from preparing audited financial reports under Chapter 2M of the Corporations Act.

This option is not considered ideal, as it would diminish accountability and transparency for companies which ought to be subject to reporting requirements given the public nature of the company and the fact that it seeks donations from the public.

## **Impact analysis**

### **Impact group identification**

Affected groups:

- users of financial reports (such as employees, donators) etc;
- companies limited by guarantee; and
- Government and regulators.

### **Assessment of costs and benefits**

#### **Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Users	Financial details of all companies limited by guarantee are available to users All financial reports are required to	

	be audited resulting in confidence that the figures are transparent and accurate	
Companies limited by guarantee		There are significant compliance costs for small companies limited by guarantee associated with producing financial reports  Compliance costs in the form of preparation costs, audit fees, printing costs and distribution costs can be significant for small companies limited by guarantee
Government/regulators		

**Option B: Establish a differential reporting and auditing framework and streamline requirements**

	Benefits	Costs
Users	Users will have access to more tailored disclosures, which are better suited to the not-for-profit nature of the company [+3]	Decrease in availability of financial information in relation to small companies limited by guarantee [-1]
Companies limited by guarantee	Significantly reduced compliance costs for small companies limited by guarantee [+2]	
Government/regulators		
Sub-rating	+5	-1
Overall rating	+4	

**Option C: Exempt all companies limited by guarantee from reporting and auditing requirements**

	Benefits	Costs
Users		Decrease in transparency and accountability for <u>all</u> companies limited by guarantee [-3]
Companies limited by guarantee	Significantly reduced compliance costs relating to reporting and auditing [+3]	
Government/regulators		
Sub-rating	+3	-3
Overall rating	0	

## Consultation

In June 2007, Treasury released a discussion paper on financial reporting by unlisted public companies. The paper sought comments on whether the existing reporting framework was appropriate for the 11,000 companies limited by guarantee and the 7,000 unlisted public companies limited by shares preparing financial reports under the Corporations Act.

The discussion paper elicited submissions from a broad range of stakeholders including preparers and auditors of unlisted public company financial reports as well as industry groups and other interested parties.

As part of the consultation process, there was broad support for the introduction of a differential reporting framework for companies limited by guarantee, consistent with Option B above.

## Conclusion and recommended option

Option A is not preferred, as it requires a company limited by guarantee to provide the same level of annual reporting as companies listed on the Australian Stock Exchange. A significant proportion of companies limited by guarantee are relatively small, resulting in the compliance costs that are disproportionate to the size of the organisation.

Option B is the preferred option as the introduction of a differential reporting and auditing framework will ease the regulatory burden on smaller companies limited by guarantee, while ensuring that the larger companies limited by guarantee remain transparent and accountable. Also, by creating a set of tailored, non-financial disclosure requirements for companies limited by guarantee that recognises the not-for-profit nature of these entities, this option will result in more relevant information being provided to stakeholders whilst reducing the range of unnecessary reporting requirements currently imposed on companies limited by guarantee. The costs of this approach are expected to be minimal and outweighed by the benefits to users and companies limited by guarantee. In addition, this option is consistent with the recommendations of the recent Senate Economics Committee report on the disclosure regimes for not-for-profit organisations. The committee recommended the introduction of a tiered reporting system based on revenue thresholds.

Option C is not preferred, as it would weaken the existing framework for companies limited by guarantee that ought to be subject to greater accountability given their size or public fundraising activities. This option would weaken existing corporate governance arrangements and would result in users (such as donators) no longer having access to information about the financial performance and position of the company. The costs to users are likely to outweigh the benefits to companies as a result of this approach.

## PARENT ENTITY FINANCIAL STATEMENTS

### ***Problem***

The Corporations Act requires companies to prepare audited financial statements for both the consolidated entity and the parent entity. This results in companies having to include a minimum of four columns in their financial statements ie figures for the current financial year and the preceding financial year for both the parent entity and the consolidated entity.

The presentation of full parent entity financial statements together with the consolidated financial statements clutters the annual report with unnecessary detail and is potentially confusing to users. The Group of 100 (comprising the Chief Financial Officers of Australia's largest entities) in a submission to Treasury noted 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.

The issue of the usefulness and value of separate parent entity financial statements has been debated in Australia for a number of years. In 2003, the Australian Accounting Standards Board (AASB) commissioned a research project on the relevance of parent entity financial reports and issued a discussion paper titled *The Relevance of Parent Entity Financial Reports*. The AASB believes that there is a need for revision in respect of parent entity reporting.

The costs associated with the preparation and audit of full parent entity financial statements will be dependent on the size and complexity of the entity and relativities around the size of the parent as opposed to the consolidated entity. The Group of 100 have indicated that the removal of the requirement to prepare parent entity financial statements would result in significant cost savings in external audit alone with the incremental audit costs for parent entity financial statements being in the vicinity of \$20,000 to \$25,000 for the top 150 ASX companies.

While a number of stakeholders have indicated that full parent entity financial statements do not provide useful and relevant information to most users of financial information, they have noted that there would be value in the presentation of key financial information on the parent entity in a summarised form.

### ***Objective***

The objectives are: to ensure that all stakeholders have access to an appropriate level of parent entity financial information; and, at the same time, to reduce the compliance burden on entities that produce full parent entity financial statements.

### ***Options***

#### **Option A: Do nothing**

The current requirement to prepare and have audited full parent entity financial statements would be retained under this option.

**Option B: Allow companies to prepare summary financial information in relation to the parent entity**

Under this option, full parent entity financial statements would be replaced by summary data for the parent entity consisting of: the parent entity’s current and total assets; current and total liabilities and total shareholders’ equity; the parent entity’s net profit after tax and total retained earnings; details of any guarantees entered into by the parent entity in relation to the debts of its subsidiaries; and details of any contingent liabilities applicable to the parent entity and the parent entity’s capital commitments.

**Option C: Allow companies to not report any financial information in relation to the parent entity**

This option proposes that the parent entity would not include any separate parent entity financial information in its financial statements.

**Impact analysis**

**Impact group identification**

Affected groups:

- users of financial statements;
- preparers of financial statements; and
- regulatory Government agencies that rely on financial statements to conduct their supervisory duties.

**Assessment of costs and benefits**

**Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Users	Users of company financial statements would continue to have the access to a full range of information on the parent entity and the consolidated entity	Retains an added level of complexity in the presentation of the financial reports for those users who may not understand the correlation, if any, between the operations of the company and the parent entity
Preparers		Significant resource and time costs would continue to be incurred in preparing and auditing parent entity information
Government/regulators		

**Option B: Allow companies to prepare summary financial information in relation to the parent entity**

	<b>Benefits</b>	<b>Costs</b>
Users	Reduced complexity for users of company financial statements [+1]	Decrease in the level of information available to users of company

		financial statements [-1]
Preparers	Substantial decrease in compliance costs resulting from a reduction in the level of resources needed to prepare and audit parent entity data [+2]	A reduction in potential savings through having to maintain separate parent entity financial statements for prudential purposes [-1]
Government/regulators		
Sub-rating	+3	-2
Overall rating	+1	

### **Option C: Allow companies to not report any financial information in relation to the parent entity**

	<b>Benefits</b>	<b>Costs</b>
Users	Reduced complexity for users of company financial reports [+1]	Decrease in the level of information available to users of company financial reports [-3]
Preparers	Significant decrease in compliance costs resulting from a reduction in the level of resources needed to prepare and audit parent entity data [+3]	A reduction in potential savings through having to produce parent entity financial statements on request for specific shareholders and creditors as well as APRA [-2]
Government/regulators		
Sub-rating	+4	-5
Overall rating	-1	

### **Consultation**

Targeted consultation occurred on this proposal in August 2008.

A number of stakeholders have called for the removal of the requirement to prepare (and audit) separate parent entity financial statements to be replaced by summarised information. Stakeholders include the Group of 100, the professional accounting bodies (The Institute of Chartered Accountants Australia, CPA Australia and the National Institute of Accountants), a number of audit firms and individual companies.

### **Conclusion and recommended option**

Option A is not preferred. While the current requirements provide significant information to stakeholders, questions have been raised as to whether stakeholders require or understand the financial statements as presented. As compliance costs associated with preparing and auditing parent entity financial statements are significant, the value of this information appears to be disproportionate to its cost.

Option B is the preferred option. This option strikes a more effective balance between the needs of users of parent entity financial information and the cost of preparing such information. Users of parent entity financial statements, including shareholders would still retain access to relevant financial information relating to the parent entity through the

summary report. While some information on the parent entity would no longer be reported, stakeholders have indicated that this information is not widely used and only adds to the complexity of the financial statements. The costs to prepare and audit of summary financial information will be significantly lower than the costs to prepare and audit separate parent entity financial statements – the extent of these costs 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. The Group of 100 estimates that the incremental savings from audit alone would be in the vicinity of \$20,000 to \$25,000 for large listed companies.

Option C is not preferred because the trade-off in reduced preparation expenses for industry is likely to be offset by the need to produce parent entity financial statements, or some form of summary parent entity information, on request for specific stakeholders. The impact of producing this information may be compounded by the fact that different data would be requested by different stakeholders, meaning that information may need to be customised. The impact on those stakeholders who do not have the capacity to request this information is also increased, as these users would then have no way of accessing financial information on the parent entity.

## DIVIDENDS FROM PROFITS

### *Problem*

The Corporations Act provides that dividends can only be paid from profits. There are a number of difficulties with this requirement, including:

- the fact that the Corporations Act does not provide guidance or a definition for the term ‘profits’, making the legal requirements of dividend distribution unclear. In addition, the legal precedents on this issue are outdated, complex and not in line with current accounting principles. This makes it difficult for directors to understand the legal requirements when paying dividends;
- the nature of accounting principles for the calculation of profits has changed over time. Australian accounting standards, particularly following the adoption of IFRS, are increasingly linked to the fair value of the company’s assets with changes in the fair value (whether realised or unrealised) impacting on the profitability of the company. This makes the profitability of Australian companies increasingly volatile with a larger number of non-cash expenses being included in the net result. In these circumstances a company may have sufficient cash to pay a dividend to shareholders but is unable to do so because the accounting profits of the company have been eliminated by non-cash expenses; and
- the requirement for companies to pay dividends only out of profits is inconsistent with the trend to lessen the outdated capital maintenance doctrine in Australia. The capital maintenance doctrine is no longer supported by other provisions of the Corporations Act, such as the requirements relating to capital reconstructions and share buy-backs.

The concerns support recommendations made in a discussion paper by the Australian Accounting Research Foundation in 2002 that Australia move away from the current profits test for the payment of dividends.

### *Objective*

The objective is to ensure that companies have the ability to distribute dividends if they have the ability to do so without causing detriment to ongoing operation. Given the current reporting framework focusing on fair valuation, this will allow companies to distribute a dividend even though profit may be impacted by non-cash revaluations.

### *Options*

#### **Option A: Do nothing**

Under this option companies would still be limited in the amount of dividend that can be distributed to accounting profit; known as the profits test.

**Option B: Broaden the ability of companies to pay dividends ensuring safeguards to protect shareholders and creditors are in place**

Under this option companies would be allowed to pay a dividend if it:

- is fair and reasonable to the company’s shareholders as a whole;
- does not materially prejudice the company’s ability to pay its creditors; and
- has sufficient assets in excess of its liabilities to make the dividend payment.

This would replace the existing profits test.

If a company is not required to prepare an audited financial report (for example, because it is a small proprietary company), then the last component of the test which requires the company to be balance sheet solvent will be determined by reference to the accounting records which are required to be kept under section 286 of the *Corporations Act 2001*.

Share buy-backs would continue to be governed by the requirements in Part 2J of the Corporations Act. Some consequential amendments may be required to the income tax law to ensure that there is no change in taxing arrangements as a result of this reform.

**Option C: Broaden the ability of companies to pay dividends without ensuring safeguards to protect shareholders and creditors are in place**

This option allows companies to distribute dividends without applying any safeguards such as the balance sheet test.

**Impact analysis**

**Impact group identification**

Affected groups:

- shareholders;
- companies paying dividends; and
- regulatory Government agencies responsible for corporations and taxation.

**Assessment of costs and benefits**

**Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Shareholders	Prevents companies from distributing amounts that would be detrimental to the share value	Shareholders of solvent companies that have mark downs to profit resulting from valuation changes are limited in their ability to receive dividends. Shareholders who have a preference for cash flow but cannot receive dividends will need to sell their shares which will incur transaction costs and may have tax

		implications.
Companies	Prevents companies from distributing amounts that would be detrimental to the share value.	Solvent companies that have mark downs to profit resulting from valuation changes are limited in their ability to distribute dividends
Government/regulators		

**Option B: Broaden the ability of companies to pay dividends ensuring safeguards to protect shareholders and creditors are in place**

	Benefits	Costs
Shareholders / creditors	Shareholders of solvent companies that have mark downs to profit resulting from valuation changes can receive dividends which will facilitate cash flow to the investor and potentially make the investment more attractive[+2] Greater protection for shareholders arising from the introduction of the balance sheet test [+1]	
Companies	Solvent companies that have mark downs to profit resulting from valuation changes can pay dividends if not detrimental to the creditors and shareholders. This provides greater flexibility to pay dividends which may increase their attractiveness as an investment and provide greater ability to attract and raise capital [+2].	Potential increase in monitoring costs for companies that are not required to prepare a financial report (in assessing whether they satisfy the balance sheet test) [-1]
Government/regulators		
Sub-rating	+5	-1
Overall rating	+4	

**Option C: Broaden the ability of companies to pay dividends without ensuring safeguards to protect shareholders and creditors are in place**

	Benefits	Costs
Shareholders / creditors	Shareholders of solvent companies that have mark downs to profit resulting from valuation changes can receive dividends [+2]	Shareholders could have the value of their shares significantly reduced if the ongoing operation of the company are damaged by a dividend payment [-3] Creditors of companies could have their debts reneged on if the company distributes a dividend that results in default [-3]

Companies	Solvent companies that have mark downs to profit resulting from valuation changes can pay dividends if not detrimental to the creditors and shareholders [+2]	
Government/regulators		
Sub-rating	+4	-6
Overall rating	-2	

## ***Consultation***

In August 2008, Treasury undertook targeted consultation on this issue with key stakeholders including representatives of industry, business, professional accounting bodies and other interested parties.

Overall, stakeholders were generally supportive of providing greater flexibility for paying dividends while maintaining appropriate safeguards, consistent with Option B above.

## ***Conclusion and recommended option***

Option A is not preferred as the environment that companies operate in has significantly changed since the creation of the 'profit test'. The adoption of IFRS has resulted in accounting practices that involve significant movements in the income statement that affect profit, but have no impact on the liquidity or ongoing operations of the company. This results in instances where a company is unable to distribute a dividend when it has the ability to do so.

Option B is the preferred option as it provides companies with the ability to distribute dividends greater than accounting profit, whilst ensuring that appropriate safeguards are in place to protect the shareholders and creditors of the company. The proposed new safeguards will also significantly improve the existing safeguards contained in the Corporations Act. The benefits of this approach are expected to outweigh the costs.

Option C is not preferred because of the significant risk to shareholders and creditors that would be exist if there were no safeguards in place relating to the payment of a dividend. Under this option a company would be able to distribute a dividend that could result in the company not being able to pay it's debts as and when they fall due. These are large and unacceptable risks.

## CHANGING REPORTING PERIODS

### ***Problem***

In Australia, close to 33,000 companies, registered schemes and disclosing entities have financial reporting obligations as outlined in Chapter 2M of the Corporations Act. Under the provisions of the Act, a financial year is 12 months long (plus or minus seven days). The balance date can normally only be changed by up to seven days each year to accommodate entities with week-based internal reporting. The restrictions on changing financial years were introduced by the *Company Law Review Act 1998*, which came into effect on 1 July 1998.

The existing arrangements in Australia make it difficult for companies to change their year-end date for reasons other than those contained in the Corporations Act. In this regard, the Australian requirements are more stringent than the requirements of comparable jurisdictions. This inflexibility has the potential to unnecessarily burden companies and their auditors, particularly during peak reporting periods.

An added issue that could arise through the adoption by companies of a new financial reporting period is an increase in compliance costs as it could result in a lack of alignment between a company's income years for financial reporting and tax purposes. While a taxpayer can apply to the Commissioner of Taxation to adopt a substituted accounting period for income tax purposes, the Commissioner will not allow the adoption of a substituted accounting period merely for convenience, such as to align with a taxpayer's financial reporting obligations.

### ***Objective***

In principle, there is no reason why a company should not be free to change its year-end date, provided that any change is made in good faith, investors and other users of company information are not disadvantaged and the change does not conflict with the requirements of other legislation. However, entities may need to be made aware that such a change could result in increased compliance costs in respect of their taxation and other reporting obligations.

### ***Options***

#### **Option A: Do nothing**

Under this option the requirement that an entity's reporting date be within seven days of its current reporting date would remain. In practical terms, this would mean that the majority of entities would have a reporting date of 30 June.

#### **Option B: Allow companies flexibility to change their reporting periods**

Under this option the restrictions on reporting date for a company would be eased to allow reasonable movement. Any changes would have to be made in good faith in the best interests of the company to ensure that companies are not changing their reporting date to alter the

appearance of their financial information. Companies would also face potential compliance costs as they would still be required to lodge figures with the Australian Taxation Office, for taxation purposes, under the current timeframe.

## **Impact analysis**

### **Impact group identification**

Affected groups:

- users;
- companies;
- preparers and auditors of financial statements; and
- Government agencies.

### **Assessment of costs and benefits**

#### **Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Users		
Companies		Significant impact on availability of accounting and auditing resources for the preparation of financial reports due to companies and other members of the community being required to prepare and submit taxation returns at the same time
Preparers and auditors		
Government/regulators	Annual reporting timeframes for most companies align with the ATO cycle	

#### **Option B: Allow companies flexibility to change their reporting periods**

	<b>Benefits</b>	<b>Costs</b>
Users		Users could face slight delays in accessing financial information about the company [-1]
Companies	Companies would have greater access to accounting and auditing services [+2]	Companies could face additional costs in complying with the ATO tax cycle if a reporting date other than 30 June is chosen [-2]
Preparers and auditors	Accounting and auditing firms would have the ability to spread their work more evenly throughout the year [+2]	
Government/regulators		

Sub-rating	+4	-3
Overall rating	+1	

## **Consultation**

Targeted consultation on this proposal occurred in August 2008.

A number of stakeholders have called for additional flexibility in this area. Stakeholders include audit firms and preparers, the Group of 100 and the professional accounting bodies (The Institute of Chartered Accountants Australia, CPA Australia and the National Institute of Accountants).

## **Conclusion and recommended option**

Option A is not preferred, primarily because of the restrictions it places on an entity's ability to program accounting and auditing work to minimise the cost and resource pressures on the entity. Maintaining the status quo will also result in the potentially inefficient use of resources within accounting and other professional firms being continued.

Option B is the preferred option. Greater flexibility around year-end reporting dates, would result in benefits to auditing and accounting firms which would in-turn flow through to cost savings for companies. With protections in place to ensure that changes are made in good faith in the best interests of the company there should be minimal costs for users of reports. There would be some costs to companies that have different reporting and taxation years but this would be optional and it is expected that companies would weigh up these costs when choosing alternative reporting dates. This option achieves an appropriate balance between minimising the costs incurred by entities for accounting and auditing work (including more efficient use of resources by professional accounting and auditing firms) and any additional compliance costs incurred in complying with the taxation reporting requirements.

## **EXTEND THE REQUIREMENT TO DISCLOSE A REVIEW OF OPERATIONS AND FINANCIAL CONDITION TO ALL LISTED ENTITIES**

### **Problem**

Under section 299A of the Corporations Act, a listed public company is required to provide, in its director's report, all information reasonably required to allow an informed assessment of its operations, financial condition and business strategies and prospects for future financial years. Guidance on this requirement refers to it as a review of operations and financial condition.

The requirement for companies to disclose a review of operations and financial condition was introduced as a result of the recommendations of the HIH Royal Commission. The rationale for its introduction was to address a lack of contextual information which explained the results set out in a company's financial statements. Accordingly, the review of operations and financial condition was introduced to provide stakeholders with an overview which would enable users to understand a business' performance and the factors underlying its results and financial position.

However, the requirement to disclose a review of operations and financial condition only applies to listed public companies (of which there are approximately 2200) does not apply to listed managed investment schemes (of which there are approximately 200).

Managed investment schemes were not involvement in the HIH Collapse and as such were not considered in Commission's recommendations. Nonetheless, the size and degree of public investment in these listed managed is analogous to the degree of public investment in listed companies. The complexity and potential for confusion in the financial statements of managed investment schemes is also similar to that of companies.

As such, the same reasons which suggested a need to introduce additional narrative reporting for listed companies also suggest a need to introduce additional narrative reporting for listed managed investment schemes.

Extending 299A to all listed entities was a recommendation of the Corporations and Markets Advisory Committee (CAMAC) in 2006.

### **Objective**

To improve decision making by investors and oversight by regulators in relation listed managed investment schemes.

### **Options**

#### **Option A: Do nothing**

Under this option listed entities would continue to have different reporting requirements, depending on whether they were companies or managed investment schemes.

**Option B: Consistent requirements**

Under this option, all listed entities would have consistent reporting requirements in relation to disclosure of a review of the entity’s operations and financial condition.

**Impact analysis**

**Impact group identification**

Affected groups:

- investors and other users of annual reports;
- listed managed investment schemes; and
- Government/regulators.

**Assessment of costs and benefits**

**Option A: Do nothing**

	<b>Benefits</b>	<b>Costs</b>
Investors and other users of annual reports		Users of listed managed investment schemes’ annual reports do not have access to a narrative discussion which would help them understand a business’ performance and the factors underlying its results and financial position.
Listed managed investment schemes	Preparers of listed managed investment schemes do not have to expend resources preparing a review of operations and financial condition.	
Government/regulators		

**Option B: Consistent requirements**

	<b>Benefits</b>	<b>Costs</b>
Investors and other users of annual reports	The information which listed managed investment schemes would be required to disclose would allow investors and other users of financial reports to make better decisions. In particular, this should mean fewer losses as a result of poor information and more efficient allocation of capital. [+2]	
Listed managed investment schemes		There would be some compliance costs for listed managed investment schemes associated with preparing the additional disclosures.

		However, these costs are expected to be minimal. Much of the information required under section 299A is similar to the information already required under section 299. Additionally, the disclosures required by section 299 rarely constitute more than a few pages; even BHP only devoted 1000 words to these disclosures in its 2008 Annual Report. Further, these disclosures do not need to be audited. The issues which must be reported on are also those which the responsible entity of a managed investment scheme (or any entity) should be aware of in any case. [-1]
Sub-rating	+2	-1
Overall rating	+1	

## Consultation

Consultation was undertaken as part of the CAMAC review and was taken into account by CAMAC in forming its recommendation. Groups who made submissions to the CAMAC inquiry included major businesses and business associations, accounting firms and shareholder representative.

Submissions which dealt with the issue of who should report generally focused on size and/or ownership. One submission which did deal with reporting obligations for companies other than corporations commented that any entity with a significant impact on society should be required to report.

## Conclusion and recommended option

Option B is the preferred option. It is difficult to quantify the costs and benefits of requiring companies to disclose a review of operations and financial condition. However, the costs appear likely to be minimal for the reasons outlined above. The disclosure of this information is also generally viewed as beneficial for listed companies and was considered by the HIH Royal Commission to be important in helping users understand the issues underlying the figures reported in a company’s financial statements.

As the benefits of providing this information are generally considered to outweigh the costs when this information is provided by listed companies, it seems likely that the benefits will also outweigh the costs when this information is prepared by listed managed investment schemes.

## SOLICITORS REPRESENTATION LETTERS AND LEGAL PROFESSIONAL PRIVILEGE

### Problem

In preparing their financial statements, entities are required to make provisions for, or disclose in the notes, probable or possible liabilities in accordance with Accounting Standard AASB 137 Provisions, Contingent Liabilities and Contingent Assets. Such disclosure should include liabilities which may arise from pending or current litigation. In auditing this information, auditors are required to obtain appropriate audit evidence of the director's assessments of any litigation, by obtaining a solicitor's representation letter from the entity's lawyers.

The solicitor's representation letter requests the entity's lawyers to confirm, among other things, whether the director's view of the description and estimates of the amounts of financial settlement which might arise in the litigation are reasonable. Auditing Standard ASA 508 Enquiry Regarding Litigation and Claims provides that the auditor must request management to obtain the solicitor's representation letter from the entity's lawyers, with a request that the lawyers respond directly to the auditor. The solicitor's representation letter must be sent from the lawyer directly to the auditor to maintain the integrity and independence of the lawyer's corroboration.

#### The Westpac Decision

In September 2005, the NSW Court of Appeal in *Westpac Banking Corporation v 789 Ten Pty Ltd* [2005] NSWCA 321 held that solicitor's representation letters are not subject to legal professional privilege because they do not satisfy the "dominant purpose" test in sections 118 and 119 of the Evidence Act 1995. In other words, the solicitor's representation letters are not prepared for the dominant purpose of providing legal advice to a client, or for an anticipated or pending proceeding; they are prepared instead for the purpose of conducting an audit.

In the first instance, the judgment explored whether this issue could be resolved by the lawyer providing the letter directly to the client, who would then provide it to the auditor. However, on appeal, the court held that the communication would not be privileged even if the lawyer or the client provided the communication to the auditor. In any event, if this information is not independently communicated by the lawyer directly to the auditor, it would significantly diminish the reliability of the audit evidence.

The Westpac judgment noted that 'there is obviously a problem which may require legislative intervention...for instance, by amendment to the Evidence Act or the Corporations Act...'. The decision is authoritative, as the High Court refused special leave to appeal the decision in December 2005.

#### Implications of the Westpac decision

The audit function represents the principal external check on the integrity of financial statements. The obligation to advise auditors of all contingent liabilities is an essential requirement to ensure auditors are aware of all matters relevant to an entity's financial position, and are in a position to corroborate management's assertions concerning contingent liabilities. However, as a result of the Westpac decision, this may result in an

entity risking further liability by granting their opponent a strategic advantage in the legal proceedings.

Entities that do not request their solicitors to prepare a solicitor's representation letter may receive a qualified audit opinion if the auditor believes there is insufficient audit evidence to verify the contingent liabilities. Alternatively, an auditor may limit the scope of the audit to exclude an audit of any potential liabilities arising from litigation.

The solicitor's representation letter may contain additional information that is not already disclosed in the financial report. Potential liabilities arising from legal proceedings may be aggregated into a single class in the financial report, so that the amount reported in the financial report may not be discernable to any particular proceedings. In addition, an entity is not required to disclose in its financial report information required by AASB 137 if it could be expected to prejudice seriously the position of the entity in a dispute with other parties. In such cases, an entity must disclose the general nature of the dispute and explain why the information has not been disclosed. In confirming whether the director's view on the description and financial estimates of the legal matter are reasonable, a lawyer may need to reveal the contents of sensitive legal advice or legal opinions in the solicitor's representation letter, which are unlikely to have been disclosed in the entity's financial report, and therefore, would not be publicly available.

As a result, entities may be placed at a disadvantage in current or pending litigation if they are required to disclose the directors' view of the entity's prospects in the litigation, and the view of its solicitors, without such correspondence being privileged. If solicitors' representation letters were protected by client legal privilege, lawyers would be able to provide full and frank advice in the solicitor's representation letter without prejudicing their client's prospects of success in the litigation, or their ability to negotiate a settlement.

## Objective

To ensure that lawyers can provide full and frank advice in the solicitors' representation letter to enable the auditors to conduct a proper audit of the company and its contingent liabilities.

## Options

### Option A: Do nothing

Under this option, no action would be taken in response to the *Westpac* decision.

### Option B: To provide, by legislation, that solicitors' representation letters are protected by some form of privilege, similar to legal professional privilege

Under this option, the *Corporations Act 2001* would be amended to provide that solicitors' representation letters and associated correspondence are protected from disclosure to another person or to a court.

Exceptions will exist to ensure that the Australian Securities Investments Commission (ASIC), the Australian Prudential Regulation Authority (APRA) and the Companies Auditors and Liquidators Board (CALDB) can continue to access these communications for the purpose of performing their functions.

It is noted that any potential amendment to the Corporations Act would not extend to unincorporated entities and public sector entities, and that further amendments to Australian, State and Territory legislation would be required to capture these entities.

### Option C: Remove the requirement to obtain a solicitor's representation letter

Under this option, the requirement to obtain a solicitors' representation letter, which is contained in the auditing standards, would be removed by the Auditing and Assurance Standards Board.

## Impact analysis

### Impact group identification

Affected groups:

- Auditors;
- Entities that prepare financial statements and are a party to litigation;
- Lawyers; and
- Government/regulators.

### Assessment of costs and benefits

#### Option A: Do nothing

	Benefits	Costs
Auditors		Unlikely to obtain appropriate audit evidence to verify contingent liabilities.
Entities that prepare financial statements and are a party to litigation		May be placed at disadvantage in litigation if the letter is not protected from disclosure.
Lawyers		Unable to provide full and frank advice in the letter if it is not protected from disclosure.
Government/ regulators		

#### Option B: To provide, by legislation, that solicitors' representation letters are protected by some form of privilege, similar to legal professional privilege

	Benefits	Costs
Auditors	Auditors are more likely to obtain appropriate audit evidence to verify contingent liabilities [+3]	
Entities that prepare financial statements and are a party to	Less likely to have their prospects of success in the litigation	

litigation	adversely affected due to disclosure of sensitive information [+3]	
Lawyers	Greater ability to provide full and frank advice to the auditor without impacting on their client's prospects of success in the litigation [+2]	
Government/ regulators		
Sub-rating	+8	0
Overall rating	+8	

### Option C: Remove the requirement to obtain a solicitor's representation letter

	Benefits	Costs
Auditors		Unable to conduct a proper audit of entity's contingent liabilities [-3].
Entities that prepare financial statements and are a party to litigation		
Lawyers	Less compliance costs, as the relevant information will no longer need to be prepared [+1].	
Government/ regulators		
Sub-rating	+1	-3
Overall rating	-2	

## Consultation

In August 2008, Treasury undertook targeted consultation on this issue with key stakeholders. Stakeholders were generally supportive of providing solicitors' representation letters with a privilege similar to legal professional privilege, consistent with Option B above.

## Conclusion and recommended option

Option A is not preferred, as auditors require appropriate audit evidence to verify an entity's contingent liabilities. If solicitors' representation letters are not protected, lawyers may be reluctant to disclose such information as it may disadvantage their client or adversely affect their prospects in the litigation. If auditors obtain such audit evidence 'off the record' then the auditor is likely to be in breach of their legal obligation to keep appropriate documentation.

Option B is the preferred option, as it will allow lawyers to provide full and frank advice in the solicitors' representation letter, which will enable the auditors to conduct a proper

audit of the company and its contingent liabilities. There are no costs expected with the change while there are expected to be benefits in the form of enhanced communication between lawyers and auditors, which would lead to more accurate audit reports.

Option C is not preferred as auditors will be unable to conduct a proper audit of the entity's contingent liabilities, without obtaining independent corroboration from the entity's lawyers.

## **OTHER MINOR AND TECHNICAL AMENDMENTS**

### **DECLARATION OF IFRS COMPLIANCE**

#### **Problem**

Some feedback from foreign jurisdictions has suggested there is a lack of awareness that the financial statements of Australian companies are compliant with IFRS. In particular, as accounting standards in Australia are commonly referred to as ‘Australian-equivalent International Financial Reporting Standards (AIFRS)’, there is a perception that they are not identical to IFRS.

Lack of international recognition of Australia’s IFRS adoption prevents Australia from realising the full benefits of IFRS in relation to the facilitation of foreign investment.

Auditing Standards also require an auditor to make a declaration of IFRS compliance in the audit report, but there is no corresponding requirement in the directors’ declaration and this may create some confusion.

#### **Conclusion**

A statement of IFRS compliance should be required in the directors’ declaration. This will provide benefits to companies by creating consistency between the auditor’s report and directors’ declaration and will help ensure international recognition of Australia’s adoption of IFRS. This amendment would not generate any additional costs as an analogous statement is already required in the notes to a company’s financial statement. It would merely ensure that IFRS compliance is stated more prominently.

## **LOST CAPITAL REDUCTIONS**

### **Problem**

Under section 258F of the Corporations Act, companies are allowed to cancel paid-up capital that is lost or not represented by available assets of the company. The provision is intended to allow companies to write down the value of the company's capital in situations where a company incurs certain types of losses. This is done by writing-off past accumulated losses against the share capital of the company.

Concerns have been expressed that companies may be able to use section 258F to overstate the profitability of the company by taking expenses directly to share capital rather than recognising them in the statement of financial performance. Such action would be in breach of Australian accounting standards.

### **Conclusion**

Section 258F should be amended to make it clear that a company can only cancel share capital in circumstances where it is not inconsistent with the requirements in Australian accounting standards. The proposed amendment will still allow companies to write off accumulated losses to share capital but will not allow companies to take expenses directly to share capital.

The proposed amendment is of a technical nature and is designed to clarify the manner in which section 258F is intended to operate. There is no evidence that there is, or has been, widespread misuse of the section and, as a consequence, the proposed amendment will have minimal, if any, impact on companies that are required to prepare financial statements.

## **IMPROVEMENTS TO THE FINANCIAL REPORTING COUNCIL'S FUNCTIONS AND FUNDING ARRANGEMENTS**

### **Problem**

Prior to the enactment of the *Governance Review Implementation (AASB and AUASB) Act 2008* (the GRI Act), the Australian Accounting Standards Board (AASB) and the Australian Accounting Standards Board (AUASB) were statutory bodies governed by the *Commonwealth Authorities and Companies Act 1997* (CAC Act). The GRI Act has transferred the AASB and the AUASB from the CAC Act to the *Financial Management and Accountability Act 1997* (FMA Act) framework.

As a consequence of the enactment of the GRI Act, the specific accounting and auditing standards functions given to the FRC under s.225(2)(i) and (j) and s 225A(2)(i) and (j) of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) are now obsolete and unnecessary. These provisions require the FRC to:

- : seek contributions towards the costs of the Australian accounting standard and auditing standard setting processes; and
- : monitor the level of funding, and the funding arrangements, for those processes.

### **Conclusion and recommended option**

Paragraphs 225(2)(i) and (j) and 225(2A)(2)(i) and(j) of the ASIC Act should be repealed as they are no longer necessary or appropriate having regard to the fact that the AASB and the AUASB are now FMA agencies for purpose of the FMA Act.

## IMPROVEMENTS TO THE COMPANIES AUDITORS AND LIQUIDATORS DISCIPLINARY BOARD'S (CALDB) PROCESSES INCLUDING IMMUNITIES AND APPOINTMENTS

### Problem

The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (CLERP 9) amended CALDB's structure. As a result of the CLERP 9 changes, CALDB's membership was increased from three to 14 members, all of whom are appointed by the Minister on a part-time basis. Membership consists of:

- : a Chairperson and a Deputy Chairperson, each of whom must be enrolled as a barrister and/or a solicitor or a legal practitioner in Australia;
- : three members selected from a panel of seven nominated by the Board of the ICAA;
- : three members selected from a panel of seven nominated by the Board of CPAA; and
- : six business members. Business members need not be nominated by any particular body. The Minister must be satisfied that a business representative has knowledge or qualifications in a business or law-related discipline.

There are problems with this approach. There are three professional accounting bodies in Australia, the ICAA, CPAA and the National Institute of Accountants (NIA). Additionally, there is also a recognised professional body representing insolvency practitioners, the Insolvency Practitioners Association of Australia (IPAA). Under the current framework, the NIA and other professional and interested parties are unable to nominate members for CALDB.

Under s 221 of the ASIC Act, immunity consistent with that of a Justice of the High Court is conferred on Panel Members of the CALDB when exercising powers in relation to a hearing. Witness and legal and other representatives receive immunity equivalent to that which they would receive if appearing before the High Court.

However, s 1294A of the Corporations Act also allows the Chairperson to conduct pre-conference hearings. This was introduced to streamline the hearing process. Immunity under s 211 is not available for pre-conference hearings conducted by the Chairperson.

### Conclusion and recommended option

The requirement for the two professional accounting bodies to directly nominate members to the CALDB should be replaced with a new approach whereby accounting members would be drawn from nominations received from all relevant professional bodies and other interested parties, with the Minister retaining responsibility for selecting the most appropriate accounting member once the list is compiled. This is similar to the current arrangements for the appointment of business members to CALDB.

The immunity under s 221 of the ASIC Act should be extended to include pre-conference hearings conducted under s 1294A of the Corporations Act.

## IMPLEMENTATION

The preferred options identified above will be progressed through the Corporations Act Amendment (Corporate Reporting Reform) Bill 2010.

Several of the issues identified above are long standing issues, which are the result of extensive previous review processes. These issues include reporting by companies limited by guarantee, parent-entity financial reports, and the requirement to pay dividends from profit.

In August 2008, several of the preferred options identified above were included as part of a targeted consultation process with key stakeholders. Feedback from the targeted consultation process suggests that there is broad support for the proposed reforms among stakeholders, and that the measures would be well received by the wider corporate community.

In addition, Treasury proposes to undertake further public consultation on the exposure draft of the amendments. Any changes to the proposals arising out of the future consultation process would be reflected in a revised Regulatory Impact Statement.