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JOINT COMMITTEE on the CORPORATIONS AND SECURITIES

Reference: Corporate Law Economic Reform Bill 1998

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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Friday, 26 June 1998

Members: Senator Chapman *(Chair)*, Senators Conroy, Cooney, Gibson and Murray and Mr Anthony, Mrs Johnston, Mrs De-Anne Kelly, Mr Leo McLeay and Mr Kelvin Thomson

Senators and members in attendance: Senators Chapman, Conroy, Cooney and Gibson, and Mr Kelvin Thomson

Terms of reference for the inquiry:

Corporate Law Economic Reform Bill 1998

WITNESSES

Committee met at 9.21 a.m.

BARRETT, Mr Patrick Joseph, Auditor-General, Australian National Audit Office, 19 National Circuit, Canberra, ACT 2600

O'BRIEN, Ms Lynne Maree, Executive Director, Financial Audit Business Unit, Australian National Audit Office, GPO Box 707, Canberra, ACT 2601

CHAIR—The purpose of this hearing is to take evidence on the exposure draft legislation under the corporate law economic reform program. The committee has already received eight written submissions, which it will consider along with today's evidence in preparing its report. The committee prefers to conduct its hearings in public. However, if there are any matters which witnesses wish to discuss with the committee in camera, we will consider any such request. This hearing will be held while the Senate is sitting, so some committee members may have to leave the hearing from time to time to vote in the Senate chamber if divisions are called. I hope that this will not unduly disrupt proceedings.

I now welcome Mr Pat Barrett, the Commonwealth Auditor-General, who is appearing today as a representative of the Australasian Council of Auditors-General. I also welcome Lynne O'Brien, his associate. The committee has before it your written submission. Are there any corrections or alterations that you need to make to that submission?

Mr Barrett—No.

CHAIR—Do you wish to make an opening statement to the committee?

Mr Barrett—I would like to make a few comments, if that is okay.

CHAIR—Yes, we invite you to do so. At the conclusion of your comments, we may have some questions.

Mr Barrett—I am here today to represent the Australasian Council of Auditors-General. As is the case with most of such submissions, they represent consensus views of Commonwealth and state auditors-general. What the submission is basically about is a plea for greater recognition of the public sector as part of the new legislation, particularly in the standards arena. In most instances, standards developed for private sector entities would be appropriate to the needs of public sector reporting entities. Therefore in the interests of ensuring greatest consistency possible in financial reports and the cost-effectiveness of the development of standards—if I can use an acronym—ACAG supports the application of common standards wherever appropriate.

What we are seeing at the Commonwealth level—and clearly at various state levels—is the growing convergence between the public and private sectors, which reinforces that ACAG view. However, it is important to recognise some of the essential differences between the two sectors, not least in the context of both performance and accountability—performance being the bottom line; and there are clearly distinctions between the public and private sectors on what reflects the bottom line—and, of course, accountability provisions, not least of which is the public interest. We consider that there could be variations to clauses

of the kinds that were put forward in the submission which would better facilitate that interest being expressed in those forums that are being proposed under the elements of the new standards legislation.

Just to give you some examples, we do recognise that separate or amended standards are needed to get, for example, clear recognition of the need for such standards, that is, public sector standards, and facilitate development of standards. Therefore, ACAG is supportive of the need for greater public sector representation within the proposed standards process. I might add that its members already extensively participate in many of the standard setting bodies and processes.

The auditing standards are not covered by this legislation, but we have a strong representation on that. I refer to the legislative review board, the Public Sector Accounting Standards Board, the urgent issues group, consultative groups, and both the Australian standards board and the Public Sector Accounting Standards Board.

In other words what I am saying is that ACAG is more than willing to pull its weight in this area. That is really a reflection of its suggestion about greater participation in the bodies concerned. I suppose that in essence—and not surprisingly, because the bill is oriented towards the private sector—the public sector does not get a mention. The word 'public' is very seldom used. It is called business, but not public. We feel that public, including not for profit entities, is something that should be expressly covered by any legislation.

I was going to give you a couple of examples of where separate amended standards have been required in the past—for instance, the standards which specify financial reporting requirements for governments and government bodies. Currently, separate standards exist outlining reporting requirements for local governments, government departments and governments themselves. The need for such standards arises because of the different nature and objectives of government activities as compared to commercial entities, of which this committee is all too well aware. For example, the standard on government departments requires that the departments clearly distinguish between those transactions that they incur in their own right and those which are incurred on behalf of the government. Just as an example, to make the point and no more, if the Australian Taxation Office reported under commercial standards, it would indicate that it would have made an operating profit in excess of $100 billion. Of course, reporting under departmental standards, that $100 billion is reported as revenue of the government rather than of the Taxation Office.

The standards which have been amended because commercially based tests are not appropriate to the government sector are another area. For example, the standard which deals with accounting for fixed assets contains a requirement that assets not be valued at amounts in excess of the recoverable amount. The recoverable amount is measured as the net cash inflows associated with the use and the subsequent disposal of the asset. Such a test is not relevant within the public sector, where assets are generally not used to derive cash flows but to provide services to the community. Similarly, the going concern standard has been amended to deal with the financial reporting consequences of the restructuring which occurs within government simply as a result of changes to the administrative orders. These are really pedestrian, everyday elements, and we consider that standards should reflect the conditions that exist in the public sector and that are not found in the private sector.

I could leave it on that basis, but if I could just make another comment in my capacity as Auditor-General, I strongly support the greater emphasis on corporate governance that is in this legislation. The reason I am doing that is not just because of better administration but because, you may be aware, the Australian National Audit Office has been active in trying to get acceptance from public sector entities of the need to take on board a lot of the practices in the private sector under the corporate governance heading. We have actually put out a paper on this as guidance for chief executives in budget dependent agencies—or core government, whatever you would like to describe it as—on the basis that we believe that the public sector, particularly in this greater convergence between the two sectors, would be advantaged in terms of its performance and accountability by adapting or adopting a lot of the good corporate governance practices that we see in the private sector that have actually come out of some turbulent times over the past decade. So we would be very strongly supportive of better corporate governance practices. In that way we would get the benefit of that if we applied those within the public sector.

I am in your hands. If there are any specific issues that you would like to raise with us about the submission, I am quite happy to respond.

CHAIR—Thank you very much. In your submission, you suggest that the membership of the Financial Reporting Council should be broader and could well include people with public sector accounting experience. I have just been looking at the draft bill. It seems to me that the membership in effect is open ended, because it is simply by appointment by the minister. There are no limitations or specifications as to who might be members of the council. So doesn't the legislation in fact give the minister direction to appoint such people?

Mr Barrett—We would like to think so, but all we are saying is that in the words of the bill the only categories that are specified do not make any reference to the public sector. So we are just simply putting our hands up and saying that in whatever documentation, whether it is part of the statement going with the bill, we would like to recognise—

CHAIR—In the explanatory notes?

Mr Barrett—Yes. We would like to recognise that there is a public sector out there at Commonwealth and state level that has a tremendous interest in this area, and we would like to be considered for membership of the FRC as well as the Accounting Standards Board.

CHAIR—I certainly know that the original papers that were published indicated the sort of people it was thought might make up the FRC. I notice in the bill no specific groups are identified, so certainly the breadth and the capacity is there to do as you ask.

Mr Barrett—I would like to think so. The fact is—

CHAIR—We might hope that your evidence this morning would lead to that outcome.

Mr Barrett—In relation to the focus on facilitation of business interests, we would like to think it is business and public sector interests. That is all. Point made.

CHAIR—With regard to the international accounting standards and the harmonisation of international accounting standards—I know this is a matter that has come under consideration by the International Organisation of Securities Corporations among others—what do you see as the prospects of actually getting an agreed international accounting standard?

Mr Barrett—At this stage I think it is much too early to say. I am not trying to duck out from answering your question; I will try to come about it another way. No doubt the secretariat would have known—at least you may have noted and you would not be surprised—that there is quite a lot of common ground between our submission and the submissions made by the professional accounting bodies, particularly in this area. You would be well aware that major countries, such as the United States, Japan and the United Kingdom, certainly are not proponents of harmonisation or adherence to international accounting standards. The accounting bodies refer specifically to the acceptance by the money market people of the standards as being a real test, although I think quite rightly they are not willing to leave it to, say, a body such as the Australian Stock Exchange to be the regulator, so to speak. Personally, I would agree with that; that is not their role, in my view.

The problem that we see is: if there are standards that are normally supposed to be international standards that are provided by the International Accounting Standards Committee, you have to wonder what sort of support and, therefore, what impact that is going to have on financial markets. The basic thing is that we want to get international recognition. So if we have not got that standard body recognised in major markets such as Japan, the United Kingdom and the United States, you have to ask yourself what the point is.

The other thing, too, which is exercising the professional bodies' minds is that there might be circumstances in which the international standard might not just be in Australia's interests. There may need to be some variation to it. The earlier language, if I could put it this way, of the documents seems to suggest that, once the standard was in, that was it, so to speak. As I read the document, the standards board, for instance, had to do the cost-benefit analysis prior to the standard being promulgated—but after the standard was promulgated, that would be the end of the matter; it would just get an automatic tick.

I think we need to be a bit more balanced than that. Quite clearly, national harmonisation in principle is a very fine idea. It is a fine idea, like a lot of ideas, provided it works, and I think it is in Australia's interests, particularly if we want to be part of the international community and we have aspirations, particularly in this region, to ensure that we do have such a role. Quite clearly, we should not be doing anything prematurely that puts us outside the bailiwick of other major money markets or the requirements thereof.

I think a little bit of discretion and, if I dare say, a little bit of commonsense needs to apply in this area. Frankly, from reading the legislation, I think it looks prescriptive and I do not think it gives enough room for the decision makers to make sensible decisions. Also, if the public sector at Commonwealth, state and local government levels had representatives in this area, at least the concerns of government would be reflected in the considerations by those bodies as well.

CHAIR—Following on from that, if the International Accounting Standards Committee standard does not gain general international acceptance, do you see a problem if the Australian Accounting Standards Board automatically adopts that standard?

Mr Barrett—I think I answered that in part. There is a question about leadership here. I would always like to think that in our small way—and bear in mind we are a very small player—we can provide leadership in this arena. But I would have a wary eye on what is being done in other major constituencies. So long as it basically was not out of kilter, yes, it is quite clear. Obviously slight variations would occur but, if it represents the intent and the thrust of other areas, then yes, I would say that is a good idea.

The fact of the matter is that we do not benefit from myriad standards. That is self-evident truth. If we can rationalise the standards and get them down to areas where it really does matter for consistency and clarity, particularly in the interests of those people who have to utilise the various documents that are produced on the basis of standards, that is what is important. It is really the people out there who utilise financial reports whom we should be considering; they are the beneficiaries. That is a discipline on the rest of us who have to either produce them or audit them. At the end of the day, they are useful only to those people out there who make decisions on them, whether it is the managers in the various corporations—the public sector bodies—or the people who actually have an interest: taxpayers in the public sector or shareholders in the case of corporations.

CHAIR—As well as the public sector representation on the national reporting council that you have referred to, can you also see that there is a need perhaps for subsets of the profession, such as auditors or accounting academics, to be part of that body?

Mr Barrett—Like any of these bodies, a broad based range of interests is always a good idea. I certainly would not like it to be just the bailiwick of so-called 'professionals'. You need to introduce an element of commonsense. I am not saying that professionals do not have commonsense, but I think there is room in there for people who have broad based private sector or public sector experience, and actually from the operational point of view, as I said, people who have to use this kind of information. Of course, you do need the experts in there who know the practical problems in putting these standards together in a way that professionals can use them and ensure that they are consistently applied across organisations.

CHAIR—In the issues paper that was put out, in terms of the membership of the FRC and the Australian Accounting Standards Board, although they have certainly got different roles, it seemed to me in terms of the categories of membership that was suggested there was almost duplication, that you had the same sort of people as members of the FRC as the AASB?

Mr Barrett—I agree.

CHAIR—Do you think that the two bodies duplicate each other? Could it operate effectively as one body rather than two?

Mr Barrett—I will put just my view; this would not be an ACAG view. Without talking to the people concerned, who clearly had the ideas, I see these two bodies as reflecting a

similar framework to a lot of other areas of government where you have an overarching body comprised of people with interests in a particular area who are not necessarily experts but who, again, have a commonsense view. They can bring broad based ideas and approaches, particularly in the context of whatever it is that you are talking about, and then you have a band of experts. The experts make sure that all of the i's are dotted and the t's are crossed and put in place. But you have a second review, if you like, of whether what is being put forward is practical, achieves the purposes for which it is being set down and is useful. That seems to me to be not a bad framework. You could get a combination of the two. But they would have to settle any frictional elements within the Accounting Standards Board itself.

My personal viewpoint is that as a guidance and as a second review it is probably not a bad idea. As I said, it is essential that we focus on the people who are going to use the information. Irrespective of whether we are creating nightmares by endless standards and the problems of conflicts, particularly if they arise between Australian standards and international standards and harmonisation objectives, I think that the input of such a group into the official standards setting function could be very, very useful. I am not sure that it should be directive. At the end of the day, the FRC is not responsible; the Accounting Standards Board has to be accountable.

CHAIR—So even though the categories of membership that are suggested are similar to the two groups in terms of appointments, you would perhaps see the FRC as consisting more of generalists, as it were, and the AASB consisting of narrower specialists?

Mr Barrett—It is a broad description. Yes, that would be as we would see it. That would be reflective also of the public sector membership. We could put experts on the standards board and have people with management ability on the FRC.

CHAIR—Are there any other questions?

Mr KELVIN THOMSON—Your submission states that you do not agree that a focus on business would result in Australian accounting standards of a sufficiently high quality. Can you give us an example of what you mean by that?

Mr Barrett—'High quality' might be a bit of a misnomer and perhaps the wrong use of the word. I did give you an example earlier of the financial reporting. Quite clearly, the financial reporting that was oriented to business would not necessarily encompass the public interest that we would be talking about. The practicalities of this remain to be seen.

Mr KELVIN THOMSON—Are you saying that is of a lesser quality?

Mr Barrett—No, I am saying that my view about the use of the word 'quality' might not have been quite what was meant. I would have to take counsel on that from my other auditors-general. My view is that if we are just simply focusing on business aspects the wider ramifications in the public arena would not be taken into account. I was going to go on to this so-called 'quality' aspect.

It is not just a case of the sorts of concepts that we in this room would be used to in terms of the public sector that are simply confined to the public sector. I believe a lot of

public interest concepts should find their way into business. These days, it is clear that a number of businesses see themselves as good corporate citizens, and they are as concerned about broad environmental impact issues and other issues of public concern. I suspect business might be receptive to a standard that encompasses values that we would accept in the public sector that perhaps would not in a strict business sense be accepted in the business community today. In that sense you could use the 'quality' argument—that is, having better quality standards—from the point of view of society as a whole.

Mr KELVIN THOMSON—Secondly, your submission states that a previous proposal that public sector interests be represented on the FRC has been removed and that the AASB qualifications now say 'business, accounting or law', whereas they previously referred to experience in or knowledge of 'accounting, finance, business or government'. And, of course, your emphasis is on government. How did that change arise?

Mr Barrett—I cannot tell you offhand, but we can certainly get back to you. I cannot tell you today, but I will certainly get back to you.

Mr KELVIN THOMSON—It may be that others here know, but I do not.

Mr Barrett—We will get back to you on that.

Mr KELVIN THOMSON—Finally, the conclusion of that part of your submission states that it is therefore considered essential that the AASB retain a public sector consultative group under the new arrangements. What is the appropriate mechanism for that? Is that a matter for legislation or a government commitment? How do you see that working out?

Mr Barrett—You are talking to a person who is a legislative minimalist. I prefer to have legislation as a framework. I am telling you this because you are the people who have to decide. If you were getting advice from someone like me, I would like to see legislation that is of a simple, framework type rather than being prescriptive. I talked about the explanatory material. Obviously what I would like to see is an indication of the government's and the parliament's intent and that people would hold to that as much as they hold to legislation. The clear signal to the Accounting Standards Board should be: 'Yes, you should be setting up appropriate committees, like a public sector consultative group, to assist you in doing the job.' That seems to me to be a pretty persuasive approach, rather than having to put into the legislation, 'Thou shall set up whatever committees.' That is just a view that you might want to think about.

Mr KELVIN THOMSON—That is why I asked.

Senator GIBSON—The chairman asked you about international standards and a long-term vision of where things are going. In respect of our contribution to IOSCO—and I am very much in favour of that—it seems to me that in the end what we are really on about is trying to persuade the US market that ACC standards should be internationalised. After all, US markets contribute some 25 per cent or 30 per cent of the world's equity markets. It dominates the scene. We are trying to get it to be more sensible? Is that a reasonable view?

Mr Barrett—Let us face it, that is the gist of the problem. You would be aware of the problems that we have had in our privatisations when we had to run the US gauntlet and what we had to go through to adhere to their requirements. Obviously, rather like the general accounting office, we would like to say, 'These are the standards. If you want them, you use them.' The US general accounting office's standards are accepted by a number of other countries. Clearly, a lot of thought and effort has gone into those and they are used as a framework. In fact, the international body of which the Australian National Audit Office is a member, INTOSAI—the International Organisation of Supreme Audit Institutions—has a framework of auditing standards. That has the same pervasive effect in the almost 180 countries where that is used as a framework. Based on that, we tried to develop our own auditing standards approach. Clearly, the problem lies in the detail. It is not so much in the framework, the principles; it is in the detail. That is where a tremendous amount of negotiations would have to take place. For pragmatic reasons, I really cannot see that we in Australia can ignore countries like the UK, Japan and the USA. That is why I think the professional bodies have a good point to say that the money markets are very important in that respect.

Senator GIBSON—In the USA what is the relationship between the government accounting standard, the GAO that you just referred to, and the commercial world accounting body?

Mr Barrett—The boot is on the other foot in the United States. The GAO standards influence the private sector. That is my observation from talking to the GAO people. Obviously, there is a lot of relationship between the two, but the GAO standards are very pervasive and persuasive.

CHAIR—Are there any further questions? Mr Barrett and Ms O'Brien, I thank you for appearing before the committee, the evidence you have given and the answers you have given to the questions.

Mr Barrett—Thank you very much, Mr Chairman.

Proceedings suspended from 9.53 a.m. to 10.12 a.m.

BATES, Miss Katherine Jane, Policy Analyst, Australian Chamber of Commerce and Industry, PO Box E14, Kingston, Australian Capital Territory 2604

MARTIN, Mr John, Executive Director, Australian Chamber of Commerce and Industry, PO Box E14, Kingston, Australian Capital Territory 2604

CHAIR—We have before us your written submission. Are there any corrections or alterations that you need to make to that submission?

Mr Martin—No, thanks, Chairman.

CHAIR—Do you wish to make an opening statement to the committee?

Mr Martin—Just very briefly.

CHAIR—Proceed, and then we will move to questions.

Mr Martin—Thank you. ACCI, as I think many of you know, is the peak employer and industry body in Australia. We cover close to 350,000 mainly small and medium enterprises, covering all sectors and all states and territories.

We saw the initiative to formulate the corporate law improvement program as an important one, because it will significantly influence the freeing up of restraints in the areas of capital raising and the manner in which corporate governance worked to the detriment of enterprise and innovation in this country. At the same time, we recognised the importance of balancing the integrity of the system and guarding the interests of shareholders and investors. ACCI, of course, has an interest in all of those aspects.

We saw the process when it started as very much being about allowing companies to make decisions for themselves on the assumption that most enterprises in this country are going to follow reasonable and clear approaches that are set out under law, but not that they are going to try to get around things or be unreasonable in their performance. I think we have seen a sea change in views, both domestically and globally, about the way this should be approached in terms of regulatory functions and the best way to get reasonable and best performance out of both our economic and social functions in business.

I emphasise in this that the approach adopted in drawing up the work that was done in preparation for this bill was quite innovative in itself. It did contrast quite a bit with the previous corporate law simplification exercise, in which we had also been involved, which certainly did not have the same degree of transparency or involvement of the stakeholders in setting the objectives and the overall framework. We saw right from the beginning with this particular exercise the broad objectives and the framework in which the changes in the various areas of fundraising, corporate governance and the other areas of takeovers and accounting standards were drawn up.

Our major interest, as we have set out, Chairman, in the very brief submission we have done, has been mainly in the fundraising and in the corporate governance directors' duties areas. We did have very significant input from two representatives in the process, as I have

indicated in the submission—Rohan Jeffs, who directly represented ACCI, and John Murray of the Master Builders Association, who represented the wider small business community. As a result of their role in the process we were able to get very significant input from a reference group that we had. I could point to a couple of examples, including the sophisticated investor one, which actually came from a suggestion made by the Queensland Chamber of Commerce and Industry.

As we have set out in the remainder of our document, we have strong support for the bill. In one way we wanted to make sure that we appeared to indicate that fact—

CHAIR—There is a division in the Senate. Please excuse us for a few minutes.

Proceedings suspended from 10.17 a.m. to 10.28 a.m.

Mr Martin—As I said, we wanted to appear before your committee to indicate the extent of our support for the process and the outcome. I would be happy to answer any questions.

CHAIR—Firstly, what is the extent to which the chamber had input to the process, and have you had any feedback from members on the draft legislation as distinct from your own assessment of it?

Mr Martin—As I indicated, we had two representatives on the business advisory group that the Treasurer had set up. We actually organised around those two people—Rohan Jeffs from Woolworths and John Murray from Master Builders—a reference group that had about three or four meetings. That covered representatives of business from across Australia—about 10 or so. They were out scouring, putting some of the draft material out to their membership. We found it quite useful and there were a lot of constructive comments. As I was indicating just as the bell rang, the sophisticated investor idea came out of some of our Queensland discussion of how we handle that issue. It was a sensitive issue as to where an investor becomes someone whom you do not have to protect any more, and that was part of that balancing act. That actually came from a suggestion from one of the ACCI members and was then developed.

Subsequently, the draft bill and the information relating to it has been circulated around the ACCI membership and had fairly constructive support. If we ever come here to a committee such as this, we check out whether the membership has any significant problems. I know there are some issues coming from some of the other accounting bodies and so forth on technical issues, but they have not been an issue in the mainstream of smaller businesses to the extent of fundraising or the directors' duties.

CHAIR—Do you think that directors would be more willing to take advantage of opportunities that involve sensible risk taking as a result of the safe harbour provisions for directors?

Mr Martin—We have seen that as the major objective. Increasingly in the recent past there has been a concern that directors were vulnerable and vulnerable for the wrong reasons and that what you want to be able to do is give them some certainty and clarity. We believe that the proposed law will do that.

Mr KELVIN THOMSON—That is what I am saying. I am a bit concerned about what is being suggested. My background is in Victorian state parliament. I went along to the Tricontinental royal commission. It is an experience that tends to scar your soul a bit. The extent of shonky corporate behaviour and so on revealed by that was very disturbing. My concern would be this: if you have got this kind of business judgment rule, doesn't this pose a risk of that kind of conduct re-emerging?

Mr Martin—I agree with you entirely that that type of behaviour and what occurred there, in fact, started to influence a lot of the interpretation and the playing safe that all directors were starting to do. We need to have clarity between what is a reasonable set of actions and what is clearly a rort or criminal type behaviour. Our reading and our input was towards those ends. We believe that, as I said in the evidence, most businesses will try to understand what the rules are and operate fairly and with good business practices. We want a set of rules that allows them to operate the enterprise and be innovative but at the same time be able to capture the criminal or rorting type behaviour. We think there is enough distinction within the various components—the subsections of the law as you propose—to do that.

Mr KELVIN THOMSON—It seems to me that what always happens with regulation is that there is a sort of pendulum at work where misconduct gives rise to regulation, so the pendulum swings off in that direction. Then people start worrying about it standing in the way of, in this case, risk taking so the pendulum swings back. But the risk is that, if it swings back too far, the misconduct and the original mischief will re-emerge. So we have to be careful when we are looking at this that we do not have the pendulum swinging back.

Mr Martin—The integrity of the system and the reasonable protection of the other players—the shareholders and investors—is very important because, if it swings back too far, we will have things bogged down for another reason.

Senator CONROY—I had my soul scaled by Elders and Mr Elliott, with whom I had a few exchanges. I am a bit concerned about the prospect of the good faith sort of issues that almost make it—if I wanted to take a cynical view—you can be utterly incompetent and yet can still get away with not breaching your duties. I am interested in your perspective on whether it really moves it too far to protecting a director in terms of their behaviour? Yesterday in the parliament we had a lively debate about a corporate governance board, and that is a matter I am sure your organisation will put to the committee. The committee I think will have a reference on that sort of matter in the future. I am just interested in whether, as a way of perhaps reassuring the committee down the track, those corporate governance issues can be addressed in that way also as a separate safeguard from, if you like, relaxing the situation now but accepting that down the track there are going to be other issues and other ways perhaps to address this within the corporations?

Mr Martin—Our view would be that this thing may well need finetuning. We came into the exercise very much of the view that at the moment there was this lack of clarity and uncertainty and, therefore, a tendency for directors to be forced to go into the bunker, if you like. That was the worst on one side, and this is clearly an attempt with genuine objectives from all those who were advising and the original sort of aims to get the balance corrected but not to allow the criminal or rorting behaviour to get away. We think it is a risk management issue and there are a lot of gains to be made provided the risk is balanced.

Senator CONROY—Is this particular kind of system pushing people into too conservative a position to protect themselves or does it have the potential to?

Mr Martin—Has had, yes. That has been the feedback we have had in our consultative processes within the ACCI and business section more generally over the last four or five years. As part of this process we have pressed to have it more balanced, more clear as to what reasonable behaviour is.

Senator CONROY—I have read much comment over the last couple of years that Australian companies have not performed as well in comparison with international companies. That could be one of the contributing factors. It may be an unfair judgment that some commentators have made in terms of corporate return, that returns to shareholders have not been as high as in some other countries. Would you see this as a way of perhaps freeing up the situation so they can be a little—adventurous is probably the wrong word—

Mr Martin—I think there is evidence. Cause and effect is difficult to say. We actually had at least anecdotal evidence from representatives of companies, in particular medium and large, that there were problems. How that translated into views as to expansion of business and new areas of development, it is hard to say. I cannot recall a specific study being done. I think Access Economics did some work in this, but I do not think it is specifically pointed at this.

Senator CONROY—You mentioned your anecdotal evidence. Without naming names, could you give the committee an example where the judgment has perhaps been on the conservative side and opportunities have been missed, where investment and jobs could have been created?

Mr Martin—I could possibly get that information back to the committee. I would not like to speak about that off the top of my head. This is something that has developed over, as I said, four or five years. The discussion around the table is that—and some of it is probably more in the feelings of directors—we could have perhaps been more enterprising and grabbed particular projects, and it may just be on individual decisions within managing a business. So I cannot give you anything specific, Senator.

Senator CONROY—It was mentioned yesterday in the parliament when we were debating the Company Law Reform Bill and the corporate governance issues were partly addressed. I might come back to a separate question when we move on.

In terms of the directors business judgment rule, at this stage nobody has been convicted of anything that happened in terms of Elders, yet their company performance collapsed. I think yesterday Ted Kunkel was announcing the final—some people unkindly described it as 'de-Elliottisation' of Fosters. A lot of the decisions that were taken then appear to have not been criminal. Certainly only Ken Jarrett has served any time on an admission of perhaps breach of some directors' duties. I would be worried that the sort of corporate behaviour which Jarrett has subsequently described in a number of articles as—I am not trying to get you to buy into this specific example; it is just a general issue—

Mr Martin—I won't.

Senator CONROY—It is just a general issue. He described it as: if Elliott was under attack it became 'the company was under attack' and there was an incapacity to get a view separate from 'what was good for Elliott was good for the company'. Business judgments were made inside the company that, certainly on balance, with a bit of hindsight, appear to have been very poor in terms of business outcomes. As I said, yesterday Kunkel was announcing the final stepping back and unwinding of all of those judgments.

I would be worried that if we went down this path there would be no capacity for shareholders or regulators to say, 'Clearly there were some very serious errors of judgment that have subsequently come to light.' There would be no accountability now. They would just go, 'At the time we thought it was the best possible business decision.' But clearly there was a string of things beyond just the business decision.

Mr Martin—I can see precisely what you are saying. I think what happened in the 1980s perhaps indicates how difficult it is to have a fairly heavy regulatory regime to catch these things. Quite often, the more you try to fill up every burrow the more difficult the arrangement becomes and the lawyers and people get around it. What we are aiming for and have aimed for in this is a clarity between what is done in good faith, with reasonable knowledge and so forth, and what is clearly other non-acceptable behaviour.

Your view is that you have some scepticism, but we see this more open, transparent type approach and framework as being—it will have to be tested and perhaps, as you indicated, refined in terms of process—an honest attempt to address those issues that you are raising.

Senator CONROY—I guess because we are uniquely Victorian, we suffer a bit more controversy down there. We have got the Crown Casino where it is possible again to question some of the decisions that have been made. Again, I am not inviting you to buy into Crown either, but we have seen the situation where their share price had plummeted, partially through external factors. The Asian crisis is clearly a major factor in that but, again, there seem to have been a string of decisions taken that even at the time others were willing to criticise publicly in terms of the development of the project—where it has gone, the management contract. Brian Powell made a number of other comments about the corporate governance type issues. Again, these are the sorts of areas where certainly I would be concerned that we are relaxing it perhaps just a little too much where Elders IXL say, 'Again, we thought it was good for Crown shareholders and good for everybody that Hudson Conway had the management rights.' They are the sorts of issues that concern me.

Mr Martin—I can understand your concern. I mean, the test will be how in practice this—

Senator CONROY—That is right. The ASX has championed, if you like, the non-black letter situation, yet both the ASX and the ASC are having trouble with Crown. Crown is one they are investigating. I am trying to 'de-Crown' it in terms of this discussion. You would argue that we want to create the climate where people understand that they cannot do these things. It seems there can be operators that, even in this situation right now, are trying to wend their way through. I mean, they have even challenged the right of the ASX and the ASC to look at a couple of the issues they have been willing to look at, and that is in the non-black letter situation. I am just concerned that, even with all the goodwill and good faith

the recommendations have brought forward, there are still quite prominent people who are trying to wend their way through, if you like, a less black-letter scenario.

Mr Martin—I would not like to comment on the specific example. I think it is clearly saying that, whatever you do, you will have problems with that sort of behaviour. What we are trying to signal to the overwhelming majority is: if you behave in a certain way that is more clearly defined than in the past, you will be able to proceed without fear of overstepping the line. I recognise that the criminal or inappropriate intent is always going to be difficult to deal with and we would hope that the courts, the ASX and the ASC will be able to implement something like this more effectively. I understand that the ASX is supportive of this type of approach.

Senator CONROY—Putting aside the tendering process in that example, I did not mean to suggest that there has been any criminal intent in what Crown has done, but certainly it would be possible, if you were a small shareholder, to argue that there has been a fair degree of incompetence. My concern would be that they could argue they met all of these tests, notwithstanding the performance. I am just flagging that that is the sort of issue in relation to which certainly I would be concerned to ensure balance.

CHAIR—Perhaps moving on to another issue, in your submission you have highlighted the benefits to small business of the new fundraising provisions. Are you able to tell us what the average fundraising target would be for most small businesses? How costly has it been for small businesses to raise those funds?

Mr Martin—Once you got into the equity, longer-term capital component, the problem for businesses in the range of around $2 million or beyond was that they were caught up in the whole prospectus for stock exchange rules regime and there did seem to be that sort of significant gap which were undue costs. There was undue complexity and this now provides a way of more flexibly accessing longer-term capital. Once again, the processes, the institutions and the fundraising capacity have to be developed around it.

One of the things that we have found is that there are more intermediaries emerging. In particular, some of our own associations have become involved in the Australian Equity Association, which is electronically based. Under the present arrangements, they are matching investors more readily, but that is a process that has been ongoing. It is very important to the expansion of the companies at the moment. But, once again, there was that degree of uncertainty as to what the rules were and whether they were being bent or broken. We see it as incredibly important for the expansion of investment in the small to medium sector to have that greater flexibility in the fundraising approach.

CHAIR—On the takeovers issue, I noticed an article about a fortnight ago by Bryan Frith, who quoted a couple of lawyers, Peter Cameron and Tim Bednall, in relation to the effect of the takeover provisions of the legislation. Apparently they are arguing for a completely open application of what they call the ‘escalator system’ rather than the limited approach that is in the legislation. Do you have a reaction to that?

Mr Martin—I think there have been comments both ways on that.

Senator CONROY—Yes, they have appeared in the same paper.

Mr Martin—Yes. We spend a lot of our time on the fundraising issue. The directors' duty issue was discussed very widely. As to the takeovers issue—I think the main thing that came out of our consultation with the ACCI membership was that there is a feeling that there is a degree of wastefulness that occurs at the moment in some of the defensive positions that are taken against takeovers where that has ultimately not been in anyone's interest, because it is almost a battle of the players within corporations. Beyond that we see it as a good freeing up, but I would not want to comment on a greater freeing up. We made input into the position as it has been set.

CHAIR—You do not see a big problem with what Frick described as 'lockout bids' preventing rival offers and shareholders not maximising their investment?

Mr Martin—That is not something that we have followed through.

Senator GIBSON—Have you had any reaction from your members about the statutory derivative action proposal?

Mr Martin—No, not specifically. In fact, I just got some further comments from our representatives and they have not raised that.

CHAIR—Another witness has suggested that the ASC, which will become the ASIC, has a lack of experience in consumer protection matters and suggested that there should be a consumer protection commissioner appointed to safeguard investor interests.

Mr Martin—In the ASIC?

CHAIR—Yes. Do you think that is necessary? Do you think it would provide additional investor protection?

Mr Martin—That type of question is best answered in the way you make its fulfilling of its functions work. Our concern has been to ensure that you avoid as much as possible dual regulation. The process, as we see it, meets that requirement. It is not an issue that has been brought up with us. Once again, the issue is the integrity of the arrangements. If it needs something additional in terms of expertise, we would support it. That is part of the implementation phase as to how the ASIC operates. I certainly do not have a view against having that type of personnel involved.

Senator CONROY—It has been argued to the committee in another submission that what you described as dual regulation being a problem is actually a benefit because it means competition between the regulators. I would be interested in your perspective on that. Over many years, it has been demonstrated right across the world that one of the problems is the potential for an industry that is being regulated to capture its own regulator. It becomes a cosy arrangement over time where things get a bit relaxed. The way to avoid that is to have a situation in which you have two regulators. Possibly both could be captured; I guess that is a simple response. It is harder for an industry that is being regulated to reach a cosy

arrangement if there is a competitive situation. I do not mean 'competitive' in the silly sense of the word.

Mr Martin—That is a new variation on the competition theme. Regulators need to be best practice regulators. They need to be close to and understand their industry, but they need to be able to stand back. Why we are against the dual regulation is the uncertainty that it can create and the potential complexity. The way regulation is going is to try to set the broad framework, educate industry so it understands what are the basic rules and get its cooperation. You get better results if at least the overwhelming majority are moving in the right direction. Therefore, we see a case for it being clear who is the regulator and what are the rules. Dual regulation would be contrary to that.

CHAIR—In your submission you highlight the growing importance of electronic commerce. The legislation opens up the field for that and makes it easier to conduct commerce by those means. To what extent are Australian businesses ready to do business electronically?

Mr Martin—The information that has come out indicates that the ones to whom this is important in terms of matching investors against business needs for capital expansion are getting up to speed fairly quickly. Our concern is more with the smaller ones who are probably not inside the grouping that we are covering under this in terms of significant fundraising. To get them into the net and get them up to capacity is going to be a challenge for all economies. I think a lot of work still has to be done. Certainly the ACCI network is working hard to develop programs that will give them potential investor matching services. We have been working closely with the ASX on its initiatives here. It is a big challenge. My guess is that, with some of the developments that have occurred with the deregulation of the telecommunications system and efforts we have been making to get more small business influence and understanding of the systems that are being established, particularly the online one, Australia is not doing too badly. We can always do a lot better. We are probably ahead of most economies.

CHAIR—An issue raised with us by the Auditor-General in relation to the accounting standards aspect of the legislation was the focus—particularly in regard to the Financial Reporting Council—on the private sector and there being no suggested provision for public sector representation on those accounting standard setting bodies, either the FRC or the AASB. There was a feeling on his part that there may be an interpretation of obligations and priorities as being principally to the private sector. Do you have a response to that?

Mr Martin—That is something that I had not picked up. We have not been as directly involved in the accounting standards issues. I would have thought that enfranchisement of the public sector is very important. One of the things that we all say is that we want public sector accounting on much the same footing. I mean, it is moving to an accrual accounting basis in most jurisdictions. So provided it does not mean a takeover by the public sector—because when we have consultations and functions like that, all of a sudden they seem to be able to provide plenty of people to be representative at these sorts of activities—I think that perhaps a careful weighting might be in order.

Mr KELVIN THOMSON—They were not describing it as a takeover, but they were seeking representation. Just to follow that up a little bit, when you talked about support for the bill you said that it removes the one size fits all approach concerning equity administration and corporate governance. But they were really coming to us on the issue of accounting standards and saying that this bill is providing a one size fits all approach. Their submission said that you would not get Australian accounting standards of a sufficiently high quality. When we teased this out a bit, I do not think they were so much saying sufficiently high quality but being concerned that the standards be appropriate to cover their areas of responsibility. They were arguing that perhaps the one size fits all approach might not be right for them.

Mr Martin—I have no problem in principle. I think that is quite right. In fact, it would be wrong if the public sector was not included.

CHAIR—Are there any further questions?

Senator CONROY—In relation to the corporate governance regulations, I was just wondering if you had had a chance to look at them and whether you had any comment, given that they interlock with these references.

Mr Martin—I only just caught up last night with some of the amendments. Senator Murray sent us his 400th press release for the year. Clearly, there have been some adjustments there. Once again, we were supportive of the principles. At the end of the day, we want to see something that allows companies, as much as possible, to make decisions for themselves but within a framework in which they can be called in against their actions without them being directed every step of the way by regulators. I think it was a fairly good result overall.

CHAIR—There are no further questions. Thank you both for your appearance before the committee this morning.

Mr Brown apparently has a medical emergency in his family. That concludes our hearing for this morning. We will make some other arrangements with Mr Brown, perhaps for our Melbourne hearings. We may just have a brief private meeting now.

Committee adjourned at 11.00 a.m.