COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Reference: Matters arising from the Company Law Review Act 1998

MONDAY, 16 AUGUST 1999

PERTH

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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Monday, 16 August 1999

Members: Senator Chapman *(Chair)*, Senators Conroy, Cooney, Gibson and Murray and Ms Julie Bishop, Mr Cameron, Mr Rudd, Mr Sercombe and Dr Southcott

Senators and members in attendance: Ms Julie Bishop, Senator Conroy and Senator Murray

Terms of reference for the inquiry:

To examine whether:

directors of a listed company should be elected by a proportional voting system;
companies should be required by the Corporations Law to report on compliance with environmental regulation;
listed companies should disclose information, which is disclosed to, or required by, foreign exchanges;
companies should be obliged to report any proceedings instituted against the company for any material breach by the company of the Corporations Law, or trade practices law, and, if so, a summary of the alleged breach and the company's positions in relation to it;
an application to register a proprietary company should include a copy of its constitution;*
listed companies must give at least 28 days notice of a general meeting;
listed companies should be required to disclose more information relating to proxy votes;
whether listed companies should be required by law to establish a corporate governance board and an audit committee;
whether the directors and executive officers of a company should be obliged to report to the auditor any suspicion they might have about any fraud or improper conduct involving the company;
whether a director of a listed company should have the power to call a meeting of members;
whether listed companies must specify a place, fax number and electronic address for the purpose of receiving proxy appointments;
whether listed companies' annual reports should include:
(a)discussion of broad policy for determining the nature and amount of emoluments of board members and senior executives of the company; discussion of the relationship between such policy and the company's performance; and
(b)details of the nature and amount of each of the emolument of each director and each of the five named officers of the company receiving the highest emolument.

**This includes consideration of the proposed amendment to Part 2A.2, Section 117 (2)(k) of the*

Law "Applying for registration" namely, that:
(ka)for a company limited by shares or an unlimited company, a statement that the written agreement referred to in subparagraph (k)(i)

i. includes a summary of the rights and conditions attaching to the shares agreed to be taken up;
ii. sets out the total number of persons who have consented to be members and the information referred to in subparagraphs (k)(i) and (k)(ii);
iii. contains a statement that, if a constitution has not been adopted, the Replaceable Rules will apply and that they create a contract between the members the terms of which may alter if the Replaceable Rules change after the company is registered.

WITNESSES

Committee met at 9.33 a.m.

FACTOR, Mr Laurie, Senior Lecturer, Corporate Law, School of Business Law, Curtin University; Representative, WA Joint Legislation Review Committee of: Australian Society of CPAs, Institute of Chartered Accountants and Chartered Institute of Company Secretaries; and Chairman, Western Australian branch, Chartered Institute of Company Secretaries

ACTING CHAIR (Ms Julie Bishop)—In the absence of the chair and the deputy chair, I will be chairing this public hearing today. I declare open the public hearing of the Parliamentary Joint Committee on Corporations and Securities and welcome the witnesses who will be appearing before the committee today. The purpose of the hearing is to take evidence on certain matters arising from the Company Law Review Act 1998. This is the third public hearing on this inquiry and the committee expects to conduct further hearings in Sydney and Canberra. To date, the committee has received 89 written submissions, which it will consider, along with the evidence it receives during its public hearings, in preparing its report.

The committee prefers to conduct its hearings in public. However, if there are any matters that a witness wishes to discuss with the committee in camera, we will consider such a request. I would also like to remind witnesses that the giving of false or misleading evidence may constitute a contempt of parliament. This morning, I welcome the representative of the Western Australian Joint Legislation Review Committee of the Australian Society of CPAs, Institute of Chartered Accountants and the Chartered Institute of Company Secretaries to today's hearing.

ACTING CHAIR—The committee has before it your written submission. Are there any corrections or alterations you wish to make to that submission before we turn to your evidence?

Mr Factor—With the permission of the committee, I planned to go through its terms of reference. I have discussed all of these issues with fellow members of the chartered secretaries, the committee that I represent and other practitioners. I have a submission that is in point by point form. With one or two of the matters that were contained in that correspondence, time has passed over somewhat and we have a slightly different view on one or two aspects.

ACTING CHAIR—Perhaps by way of an opening statement you could go through your presentation.

Mr Factor—I have just followed the order of your terms of reference as it was presented to me. The first item on that was the proportional voting for directors.

ACTING CHAIR—Please proceed.

Mr Factor—This, in some ways, may be one of the more contentious items. It was consistently opposed. I was unable to encounter anyone who supported this particular proposition. It was found there was a very poor level of understanding of exactly what

proportional representation was, even though we use it for the Senate, and people seemed to be well aware of delays in determining results. I guess the overriding theme was that it could produce minority representation that could be destructive of a team spirit within a board of directors.

However, having said that, there is recognition—I think quite widely now—that there is underrepresentation of groups that perhaps should be better represented on a company board. The ones that do come to mind particularly is the representation of women on public company boards and, to a lesser extent but now starting to get recognised, the representation of employees who, through share plans and the like, may have quite an investment in the company.

How to overcome that: it was not considered by all parties I have spoken to that proportional representation is necessarily the way to address that. It was felt that it could produce ticket voting and the like. It could also produce a minority position on a board. I guess we are taking the line through the Senate where most people are acutely aware of what can happen when you get a conflict situation, a balance of interest and a minority representative has a leverage far in excess of their actual representation. That seemed to me to be one of the most compelling reasons not to support proportional representation following the views put to me by many people over some time.

The problem with board selection also comes from the 'job for the boys' concept and the old school tie, and overcoming that is not easy. Suggestions of affirmative action have usually received negative responses. I have to say—a contentious point perhaps—that it is very hard to impose on the private sector a moral imperative to get a wider representation and not to have jobs for the boys when the political leaders in the country tend to not observe that themselves. I am being a mouthpiece there, but that has been a point put to me. We saw one instance of that very recently. To have moral persuasion is not easy from the parliament, it was felt, and affirmative action seems to have resistance. I am not coming up with a solution here, but it was not felt by anyone I have spoken to that proportional representation was necessarily the appropriate way to go.

ACTING CHAIR—Mr Factor, was the committee's conclusion because it is poorly understood that it would not support it or because it could not come up with an alternative or alternatives to overcome the problem?

Mr Factor—Sorry, is the method of proportional representation poorly understood?

ACTING CHAIR—Yes.

Mr Factor—Not necessarily poorly understood by my committee—

ACTING CHAIR—No, as you said in your submission, that the public do not understand that. Is that the reason that you do not support it or is it more the fact that you cannot think of an appropriate alternative?

Mr Factor—We do not support the method. Lack of understanding is certainly one key element. We have now brought the wider public into listed company investments, and their

misunderstanding of the Senate process will be no different for companies. The strongest view was that it would create minority positions on boards. The method we could overcome with education in time. But the feeling that a company could be withheld from certain steps that would be in its best interest or have its actions challenged perhaps publicly in the press by dissident directors would create unrest within the directions of the company, and these were considered unfortunate by-products.

However, it was felt that if there is greater focus on the remuneration or appointment committee, or whatever name may be given to such a committee, of a board where the board is made more accountable—and some are already, of course—for the processes and the policies they have in place in selecting directors. If they better understood the fiduciary obligation and best interest of the company in making their appointments, this may assist. But what is the best interests of the company in appointing a director is very subjective.

Having said all that, I believe you have hit on a major problem area for listed companies. With your permission, I would seek to distribute to the committee a copy of the last BHP and Email voting proxies from the general meeting. The reason I think you have hit on an appropriate area for consideration is that most shareholders are left in complete ignorance as to how they should elect their directors and the voting process.

I selected BHP simply because it is well known, a big company and should perhaps have had a bit more precision over its processes. I would take the committee very briefly through this proxy. On page 1, I have indicated the item that displayed on their notice to elect directors: four vacancies, six candidates. If we turn to page 2, we then have a voting block which consists of for, against and abstain with the six candidates, who were presumably selected by ballot in that order although there is nothing to indicate that.

The member is instructed only four candidates may be elected; they are not instructed as to how many boxes they should complete; and they are not instructed as to how the candidate will get up. Is it the candidate with the greatest votes for? Is the candidate with the greatest number of net votes after against votes are offset? As the listing rules require directors be elected on individual resolutions, do we just work our way through the first four and, if we have four people in positive territory when the votes are netted off, do we not proceed to the fifth or the sixth? I will not go on, but there is a number of different angles. A shareholder is in a complete fog as to which method determined the successful candidates in that case or how they should vote. What is the effect of abstain? Is that treated as a negative? There are many possibilities. If you flip to Email, it is considerably better. Again, there is a vacancy: two out of three. The members here are told to vote in only two of the resolutions and to mark two boxes only. They are clearly told in the last highlighted sentence, ‘Only the two candidates that record the highest number of votes in favour will be elected, provided they each receive a majority vote.’ So it is clear that they are using a netting off approach. There is no uncertainty with abstain and how it will be treated. I can pick up one or two glitches, but it is a much preferred method.

ACTING CHAIR—What do you see as being the significance of the abstain box in the BHP one and the lack thereof in the Email one?

Mr Factor—The uncertainty. They are told to select four candidates with BHP. Should they put abstain on the fifth and sixth selection—we do not know—and should it be treated as a negative response or no response at all, which you can get by not having that box? I just think it clouds the issue further unnecessarily. I cannot see how it adds anything other than confusion.

Senator MURRAY—Do you support preferential voting in the BHP instance—in other words, either numbering 1 to 4, which would be an optional preferential position, or a full preferential position requiring people to number it 1 to 6 and establishing it that way, which is a process well understood by Australian voters.

Mr Factor—Clearly, either instruction you have just mentioned would be a much preferred instruction compared to what we have here. I am not sure that the average member would necessarily desire the trickle down effect that we see.

Senator MURRAY—Let us assume you are right—this committee is solution orientated—and that the way in which the re-election or election of directors is sought should be much improved. Would you suggest that the committee look at a method of fixing it legislatively or that we should simply require ASIC to lay out general rules by which it would monitor that companies are complying with it?

Mr Factor—I was involved in this process right from the beginning and I am a supporter of simplification. I would rather see it with ASIC. It enables it to be more flexible and react rather more speedily. Frankly, I would have thought the ASX should have done better than allow that particular BHP notice to go through in that form, and that is my personal opinion. I think it is fairly clear that it is not satisfactory for them to have done that.

Senator MURRAY—Would you suggest as a solution that legislation determine that ASX would require, in terms of its rules, companies to comply with a certain level of ethics, if you like, in terms of how they present their voting procedures? Would you go further and prefer that the parliament ask the ASX, through whatever device, to institute the preferential system as the normal method so that it is very clear in what order people are establishing their preference for directors?

Mr Factor—I am not sure that we support the preferential system. The support I get is for the system of first-past-the-post. The unfortunate aspect here is that it is not clear how you get to the post first with the maximum number of for votes or the maximum number of netted votes. Your question seems to be more about if there is a preferential system, and we do not support that, and I do not have a view on it.

Senator MURRAY—We are talking about two parts here. One is that the company has a constitution and a process of electing and clearly tells the voters what that process is. It could be a minimum majority vote or a netting out procedure or an elimination procedure and you must only vote for the number of directors that are there—so if there are three there and there are two vacancies you can only vote for two—and whether abstentions are in or out and all of those sorts of things. That is about clear and factual communication, which is the Email approach. If that is what you mean by the ASX rules, then I clearly understand it.

That is the first part of my question. Secondly, would you think it desirable to consider the preferential route, simply because that is well understood, so that companies are aware it is one option they should consider when they are constituting their constitutions? I am not suggesting the parliament should oblige them to have a preferential system; I am just suggesting it does not appear to be a feature of existing company constitutions, as I know them. I do not know if anyone knows any different.

Mr Factor—No, that is correct.

Senator MURRAY—The committee could suggest that, when companies are reviewing their constitutions, they look favourably upon that as an approach, if you thought that appropriate. So there are two parts to my question.

Mr Factor—I will take the second part first. I am very much in favour of companies determining their own constitutional structures. That is a membership role. If they wish to have a proportional voting system then absolutely they should be permitted to take it up. I would not like to see it imposed legislatively but, as an option, very much so.

Senator MURRAY—I am sorry, you used 'proportional' and I was talking about preferential.

Mr Factor—I think a company should be able to select any method it wishes. Personally, I have found that the failings with most constitutions is that they say nothing. They just say the members elect the directors and they do not state the process. Perhaps I have not been precise enough. When I mentioned the ASX, the role I intended to cover was that the ASX gets notices of meetings before they are released. I would have thought when looking over a notice like that—I mean, they are not here to defend themselves and I do not want to be out of court here—

ACTING CHAIR—We can always raise it with them.

Mr Factor—Yes. They received a notice which said nothing more than 'elect and re-elect directors in accordance with the company's constitution', but the reality is the members do not have a clue. I have not looked at the constitution and I do not know whether it has detail on this—probably it has not. All the members have to work with is the voting form on the proxy form, and it is so cloudy that it is impossible to determine how it will operate.

The ASX, I would have thought, reviewing notices for company meetings could look at that and say, 'We are sorry, that is not quite satisfactory. We think that is doing the members a disservice and it does not contain enough information for them to act upon. Please amend it.' They have that role now, and I would like to leave it at that level with the pressure on them to better regulate and be a bit more investigative of the notices handed to them for consideration before they are released. That is the role I envisage.

I am very concerned about legislating in these matters. The method of voting should very much be left up to selection by the company, but properly publicised through the notice to members so they know exactly what they are facing.

Senator MURRAY—Would you suggest that ASIC, as the regulatory authority, should do an occasional sample audit to make sure that the ASX is dealing with this matter with all of the seriousness that it should be?

Mr Factor—If that was considered necessary. I believe the ASX does a first-class job. This is but one instance of many matters that come across their desk. ASIC is somewhat reluctant. I mean, we have seen a moving of responsibilities over the years, quite happily, by ASIC—and the ASC before it—to the ASX. It makes sense for them, with their diminished funding, to move over what they can to a, let us say, pseudo-regulator such as the ASX. If we want to boost up the funding of ASIC again, it can take some of these matters back, but it is just another task to stretch its funds even further.

Senator CONROY—Unfortunately, I am a bit of a pedant on voting systems, so I disagree with you about Email. I am as confused by Email as I am by the first one. 'Each received a majority vote' means nothing to me. It could mean five different things to me. Because there are no abstentions, does that mean it is a majority vote of those who cast their vote? Are they required to vote twice? Can they vote for only one of the motions? In that way perhaps 3,000 votes are cast for one but only 2,000 votes are cast for another and therefore one of the two does not receive a majority. I am quite confused. When I read that they received a majority vote, I thought, 'A majority vote of what?' I am still quite confused by this implied voting system. I absolutely agree with you about the first one.

ACTING CHAIR—Isn't it just first-past-the-post in Email?

Senator CONROY—But it is a majority vote of what—of the total number of people who attend the meeting, of the total number of people who cast a vote, of the total number of people who return the ballot paper? They mainly vote once.

Mr Factor—By mentioning a majority vote, I think it is intended that the 'againsts' be offset against the 'fors'.

ACTING CHAIR—Again this could be dealt with in their memo.

Senator CONROY—I am just putting that I would not be comfortable in saying that, because of what is written there, everybody would automatically understand.

Mr Factor—I think there is a rather even greater problem with that particular voting slip in that it orders that the members are only entitled to vote on two resolutions. It seems extraordinary that a third resolution is put to the meeting and the members are denied the right to vote on it. There are a number of different angles. I just put that point because I think you are absolutely on the right track in examining the area of voting for directors. I am sorry that I cannot come up with an alternative system that would necessarily satisfy all.

I think, Senator Murray, that having a wider range and perhaps a better education of companies about the ranges and alternatives available might be appropriate. But, amongst all the committees and members that I mix with, I was unable to get any support for proportional representation as a method of appointment mainly because of the concern over minority interests being disruptive at the board and undermining any team structure.

Senator MURRAY—At its worst, the election of directors approximates the old rotten borough. It really is a self-selection in a corrupt fashion, but that is only at its very worst; so let us exclude that.

The problem we face is that quite frequently it is minority shareholders who dominate the board. A significant financial minority, for instance in a media company, can end up controlling the entire board. Some of the best, most informed thinking on the proportional representation front has come from Dr Shann Turnbull, whom I am sure you are familiar with. However I, and I am sure the committee, recognise the difficulties with the proportional representation approach. But what it attempts to achieve is that every shareholder—as opposed to shareholding—has an equivalent vote and is able to influence the board appropriately.

The amendment which was originally put to the parliament suggested that listed companies should canvass that as an option as to whether their shareholders would like to consider it; the intention was not to impose it on companies. But, recognising the problem that minority shareholders can and do control entire boards and then self-perpetuate them through this exceptionally vague and inadequate system of voting, how did your committee address that problem? I noticed that you focused on the negatives of minorities. But minorities already control so many boards through the reverse: through having the largest single shareholding.

Mr Factor—Indeed. The answer in short form is that we did not quite address it as you have put it. But the point is well made. You could have a 30 per cent shareholder who simply cannot get onto the board. That is a commanding position to have, but they do not have enough to get on, and they should perhaps have representation. Also vice versa, you can get the reverse.

Senator MURRAY—I was making the reverse point: the 30 percenter does control the 100.

Mr Factor—Indeed. Many influences on boards come from outside of the board, whether it is AIMA or other organisations putting pressure on. I do not have an answer for what you put, how to stop a significant but not majority shareholder controlling a board when the rest of the shareholding is so widely spread.

This is one point we have discussed however: when the shareholding is so widely spread, are minority members going to get a representation or are they just so widely scattered that they are not going to get a candidate up? Telstra might be an example. The employees of Telstra might get a candidate up because, with the way their distribution of shares went, they have a pretty wide shareholding. But are the public beyond that, the million or so of the public who took up shares, really going to get themselves so well organised that they will get a candidate up? I think not.

Senator MURRAY—Let me put a left field proposition, then I will leave it alone because of time purposes. With the national constitution, which is very difficult to change, when there is enough organisation and angst about something, a constitutional convention is held and eventually there is a referendum. Thinkers in this area just want to encourage

companies to review their constitutions, but those who hold power are not really interested in that.

Is it appropriate for this committee to try to encourage large listed companies, such as BHP and Email, to have their own constitutional conventions where they themselves can review their constitutions and the issues of methods of election, corporate governance boards, greater accountability, opening it up to more talent—the point you made earlier—and those sorts of things? That does not seem to happen in the corporate world, and yet this is an issue of democracy, isn't it? It is an issue about those with shareholdings being able to determine how their organisation is run. How do you react to the regulator, the ASX, in some way encouraging companies to review these matters themselves within their own constitutional framework?

Mr Factor—Do you mean review them at a convention attended by members, call a general meeting?

Senator MURRAY—Yes. I have been on many boards. If you examine the constitutional mechanisms, what happens is that the board asks lawyers to fix a particular problem, and that is how it is expressed. But very seldom are the membership and the shareholders themselves, except through their representatives on the boards, active in reviewing these matters. That is why the pressure comes on the regulators, their legislators, to change things, with all the resistance there is because that is trying to make everybody do the same thing.

Mr Factor—What you are suggesting, to my mind, is the most desirable but not necessarily possible outcome. It is not like a country where we get information every day and we can make our political judgments. With a company, so many of the members do not have a clue about how that company is run, how it is structured. They just put their money in, they hope the price of the shares go up and they get out at some stage. The people who do know are the people who currently have control, so to speak, and nothing is going to change. They will control the agenda. They will put the matters before such a meeting. It is not unattractive to me, but I just actually cannot see it coming off.

Senator MURRAY—But that then forces people like ourselves to insist on accountability or better governance, or whatever, if there is a parliamentary majority—and that is the very thing that advocates like you resist.

Mr Factor—I am not resisting. From my experiences, the so-called bigger end of town does things pretty well, I am finding. I have been surprised over the years at how well organised their corporate governance structures are. Perhaps it is because I mainly dwell in professional groups and, therefore, the people I meet there are the people who do have an interest in this any way and run a good ship.

But I do see something quite different at the other end—that is, particularly in Perth, the small junior-explorer type companies. I am not so sure that there is something nasty happening in the woodshed of most of the larger listed companies. I think, if nothing else, a lot of those directors have a lot of personal self-esteem on the line. Most of them, I think,

perform reasonably well. It is just that we do not get enough other talent in there to test against them to see whether the way they are performing could not be higher and better.

ACTING CHAIR—On that positive note, could we move on to a couple of your other matters?

Mr Factor—Yes. Firstly, we thought the environmental regulations quite meritorious but misplaced. The feeling is that the financial report of a company is not necessarily the place to have such disclosure. EPA reports and the like, yes. But the financial reports? We just thought that was, as I say, somewhat misplaced.

There is a word in there also that makes life a little difficult and very subjective, and that is the word 'significant' in 299(1)(f). I could argue in a number of different ways that my company's actions, say, are not significant because 'significant' means the cutting of all the trees in the Amazon Basin. But what we have done is irrelevant on an international scale, and environment is an international matter, not a state matter, and so on. 'Significant' is too subjective, I think.

The good (companies) will comply, the ones that perhaps it was really aimed at may very well be able to duck and dive. We expect to find considerable numbers of standard phrases used here. I just think it is a bit misplaced. I think it is better done through environmental reports by people who are properly equipped to assess performance.

ACTING CHAIR—In other words, it should not be under this legislation; it would be better if it were placed under specific environmental legislation.

Mr Factor—Indeed. We are so corporatised in this country; we probably rate as one of the most corporatised with—what is it?—one million companies over only 18 million people. We must make companies socially, environmentally and in other ways accountable as they are too ingrained in our society. Yet I just do not think this is the appropriate place for such information to be released.

Senator MURRAY—Can we look at the purpose? The purpose of this report is mostly to establish material financial risk or opportunity. Let's take the example of emission standards. Emission standards in general can be dealt with outside of financial risk and reporting. But, if you were a major oil refinery listed on the Stock Exchange, I think you would be obliged to advise your shareholders that European and American standards were likely to find their way to Australia. If they found their way to Australia, you would be obliged to invest $200 million or $250 million each in converting your plant so that you could produce lower diesel fuel, et cetera. That would be a financial issue you should pass across to your members.

In reacting to this, I think there has been a deliberate attempt to regard it as general legislation about general compliance. But it is not. It is about financial risk or financial opportunity to the company. So, whilst I accept that it can be better phrased—and any legislation can be—the intent is to identify something which is really significant for some

companies. Considering that specific example, which I think is a practical one, how would you react to that narrow interpretation of the requirement of the legislation?

Mr Factor—If I understand what you have described correctly, the company is assessing its environmental position and making a projection on what its future responsibilities may be; that is, it will have to provide for X hundred million dollars, or whatever it might be, to meet future obligations?

Senator MURRAY—It is a legitimate evaluation of risk which is apparent; they can see what is going to come. Directors have a responsibility to not only present shareholders but also future shareholders, and the emission standards example is a very practical one.

Mr Factor—The current legislation focuses just on Australian or territorial legislation and not international. So you are thinking of a wider focus?

Senator MURRAY—No. Let me be specific. Emission standards have been established overseas.

Mr Factor—Yes.

Senator MURRAY—Because of what has happened recently—and that is why I used the example—enhanced or accelerated emission standards are to be applied in Australia. There has been very strong pressure on the government to do so and it now is a fact; it has accelerated by 10 years. The consequence of that is a financial impost on the refining industry. If a refining company was listed, given the long time frame which they have to forecast events, I would have assumed that they should have indicated to their shareholders that plant change will be required in future if the following occurred. That goes to evaluation by any shareholder who reads that report as to whether they should stay with the shares, whether they should buy them or whether there is a prospect which affects the financial performance of the company.

It is the environmental area and in some respects these days the health and safety area—and I am thinking, for instance, of class actions on smoking for those companies who are smoking listed—which entail major unquantifiable risk to companies. Surely it is in the interests of the shareholders for the company to make a considered evaluation of that in a narrow financial risk sense.

Mr Factor—A lot of companies faced exactly that with the Y2K and they were brought to the line with quite specific requirements, although some of them struggled mightily to come up with a figure. We have seen those figures change a lot as well. What are you suggesting is so broad and general; I cannot see where the matters you have just raised would come about under the existing legislation. It seems to be a much wider scope than the existing legislation provides for.

Senator MURRAY—But the purpose of the legislation is to ensure that shareholders are properly informed; that is what it is about. The key elements in terms of proper information are things such as financial risk.

Mr Factor—We have a directors' report that looks ahead at matters that will affect the future of the company and change its current profit performance in a material manner.

ACTING CHAIR—The disclosure requirements.

Mr Factor—Yes. I am not sure that we should specifically pick on the environment. There are many other angles as well. Most people I speak to are quite supportive of the theme behind companies being made accountable to their environmental obligations; it was just felt that this is an inappropriate method of placing that before the public. Also, it is going into the financial pages. It can get buried in the financial pages. If we really want to look at companies' environmental planning, perhaps the financial pages are not the best place to get a wider audience anyway.

Senator MURRAY—But the clause does not ask that they expose their environmental obligations; it asks that material and significant factors are alerted to the shareholder.

Mr Factor—Yes.

ACTING CHAIR—I think I understand Senator Murray's position and perhaps yours too, Mr Factor. Can we move on?

Mr Factor—Yes. There is nothing too contentious with the foreign exchange disclosures; we had no major objection with this. Given that the same information can be reorganised and reshaped for a foreign exchange and possibly provide a slightly different window into the company's operations—not new information, just reorganised and reshaped—it would be unfortunate, indeed, if a foreign exchange took a different view of an Australian company with that view not being available to the domestic market. So, we had no major objection on that one.

We had a little bit of difficulty with the reporting of proceedings against the company. First of all, it seemed that the company, by stating that charges or whatever had been laid against it, was sort of spreading the word, with no guilt having been proved at this stage. Obviously it will make a statement of innocence—what else can it do? It cannot divulge sensibly very much at all about its position because, if the matter is sub judice, it possibly will undermine its own defence. So what is it going to say? 'This has been laid against us; we vigorously deny it'—we will see these standard words—'and the matter will be determined in due course in the courts,' or something like that.

ACTING CHAIR—It is asking for even more than that; it is asking for a summary of the allegations and the company's position. They would have to summarise their position in relation to each allegation, which would be disclosing one's hand.

Mr Factor—Exactly. Also, if it is a financial angle that is being sought, what is it going to say? 'The potential damages here will be.' You cannot expect the company to be guessing at whatever might fall upon it.

ACTING CHAIR—If there were a vexatious claim for $3 billion—nobody can stop a claimant or a plaintiff putting that in its statement of claim if it wishes to, even if

subsequently it is to be struck out—at that point, what is the company meant to do potentially in terms of the financial risk?

Mr Factor—I see this perhaps having value after the event; that is, perhaps a company should be brought to account in the sense that it has to state in its annual report any matters that have been finalised, any proceedings that have been found against it. The matter is over. Presumably it is not going to appeal, or anything.

ACTING CHAIR—What about confidential settlements?

Mr Factor—Yes, that is another angle.

Senator MURRAY—This was a unanimous recommendation of the committee in 1996 which the government decided not to proceed with. We all understand the qualifications being put by both you and the chair. Nevertheless, the view of the committee at that time was that material risk faced some companies as a result of litigation against them, and shareholders should be aware of that and it should not be concealed. That is essentially the matter. It was being concealed, and potentially hundreds of millions of claims could be made in certain extraordinary circumstances. What do you feel about that?

Mr Factor—That is a valid point. But the problem is that the company could not possibly indicate what it thinks the reach of those damages, if successful, might be. All it could state is that this action has been taken against the company. It is not necessarily going to inform the members particularly well one way or another as to what the value of that action may result in; what, if successful, the size of the damage may be. We could not quite put our finger on what the value of this would be. But after the event, why shouldn't a company that has breached the law stand up and admit to its members that this has happened in the last year, and the effect of this was X, Y, Z? Maybe that will lead to changes on the board. But not during proceedings; that is where we had trouble.

I will proceed with the next issue. We have changed position on the matter of proprietary company constitutions. I am on the ASIC regional committee. I did put to Alan Cameron, only a few weeks ago at our meeting, how on earth would ASIC manage a million constitutions landing on its desk. He said that he considered it essential that all companies should have to lodge a constitution. That was news to me. I have spoken with others about this, and they do support the inclusion of proprietary company constitutions. Most, hopefully, will take up the replaceable rules.

I did note in the matters for hearing today that reference was made to section 117(2) with a (ka) amendment. I just thought that section 117(2)(ka)(iii) appeared to be quite unnecessary. This is a statement for those registering a company that they acknowledge the contractual relationship, and that they understand that the constitution will change from time to time and they will be bound by the new terms. You will find 117(2)(ka)(iii) in the agenda for today; it is in italics at the foot of the page. I just thought that was unnecessary duplication.

We already have section 140 which says that members enter into a contract; it has been around for a long time. Admittedly the new drafting of section 140(1) does not make it quite

as clear as its predecessor that—this is a moving feast of a contract—any changes in the future will continue to bind the member. Maybe that could be marginally reworded. But the replaceable rules and a constitution both operate under that contractual arrangement. I thought (iii) there was somewhat unnecessary. It just restates what is already in the legislation.

The move to 28 days in fact received little support. I suppose it had an unhappy birth, mainly because companies got such late notice of it. They are like battleships: they take a long time to turn around. There was a lot that breached the law. It was considered very regrettable that the commission was put in a position where it could not legally give proper relief. So it had to close its eyes and operate under section 1322 to allow companies to get by with shorter than 28 days notice where necessary.

Having said that about the short notice of its birth, I thought companies would actually settle in this year and just accept it. All we have got back are negative responses. There are so many worried companies out there. The representation on the board is getting more competitive. If they get nominations for directors under the listing rules, there is simply no time to get an adequate notice out. The nomination periods of directors are 30 or 35 days, depending upon the circumstances. You cannot have a notice on 28 when somebody lobs in their nomination just a few days before and you have to get out a notice to half a million people. You simply cannot get it printed and so on.

Senator CONROY—Is that an argument for extending the nomination period perhaps?

Mr Factor—Possibly.

Senator CONROY—I presume it works in reverse. You could say, 'Go back to 21,' or you could say, 'Push it out to 40 days for directors.' Either of those are valid to solve your problem.

Mr Factor—That would solve it. We also have the reporting section 315, the 21-day reporting deadline and financial reports to members. Why is that now still at 21 when the others moved to 28? I have not found anyone who actually said, 'This is good. This enables the overseas shareholders that were originally behind the move.' Perhaps we are too insular here in Perth, but I have not encountered anybody who has actually said, 'This has resulted in improved circumstances.'

ACTING CHAIR—Another thought against it could be that information would be increasingly out of date. The greater the period of time for calling a meeting, the more likely it is that information will become out of date.

Mr Factor—Yes, that is conceivable.

ACTING CHAIR—A lot can happen in seven days.

Mr Factor—I note that you are going to hear from AMEC later today. I think you will find that they will be arguing matters such as the time delay. When their members are wishing to raise capital, they want to get into the marketplace as soon as possible. They call

a general meeting because perhaps the issue will exceed 15 per cent. They are obliged to do that. By the time you have 28 days, plus other add-on bits and pieces, we are talking a month and a half. The market could be quite different; the placement is now not suitable, given whatever changes have occurred. Could I make the recommendation to the committee that we perhaps consider moving 28 back to 21 for all meetings with the add-on that a company's members—and that is what the notice is all about; it is for their benefit—may by special resolution amend the 21 days to no less than 14 days. That then becomes a standing notice period for that company, which can be changed in the future by simply passing another special resolution and reverting back to 21. Give the company the choice of going to 14 if it wishes to, but if it does not take such an action then the standard is 21. That is a recommendation.

Senator MURRAY—If you would go to that recommendation, why don't you hold it at 28 and let the companies by special exemption make—

ACTING CHAIR—Go 14 or 21.

Mr Factor—My view is that 21 is not a bad period and, if you do put it in at 28, every company will change, and they could all jump down to 14. Twenty-eight is so on the nose amongst so many companies that there will be huge pressure to get that to change. But, if you put it at 21, I think you would find that a lot of companies would live with that.

Senator MURRAY—We had a fascinating review of that issue in Melbourne where the person concerned effectively indicated that, 21 days in, they had put 25 or 26 anyway, I seem to recall.

ACTING CHAIR—The 28 could end up at about 36.

Mr Factor—It does, yes.

Senator MURRAY—33, I think.

Senator CONROY—Mr Factor, you make comments on the lack of consultation for these amendments in your opening paragraph, and you have also made a couple of verbal references to this. I understand why that impression may be there—because the government have sought to give that impression—but, as Senator Murray has indicated, the draft of the legislation was reported on by this committee in 1996, and this issue was debated at length in that committee report. Then, in 1998, there was the specific legislation, and again this committee dealt with that issue.

Senator MURRAY—Three months prior.

Senator CONROY—The fact that it was passed when most people did not expect it to be passed is not the same as having no consultation.

Mr Factor—Yes, that is a point well made. I accept that point. But it was a huge surprise to so many people out there, and transitionary mechanisms were not put in place to enable it to—

Senator CONROY—We thought ASIC attempted to put those in place.

Senator MURRAY—I recall the parliamentary secretary putting a transitional bill back to the parliament, which was passed as a matter of urgency in early August 1998, to cover that particular problem. So the parliament did address it and did fix it.

ACTING CHAIR—Nevertheless, we have Mr Factor's views on it. Can we move on?

Mr Factor—On the proxy information of 251AA, we had a lot of problems putting our finger on exactly what was intended to be achieved. Disclosure is a good thing. However, there is no likelihood in most cases that the proxies lodged are going to match with the votes cast. The law itself says that a proxy does not have to vote. If they do vote, they should follow their instructions, but they are entitled to withhold their vote even though they have been instructed to vote. That applies to any proxy on a show of hands, and on a poll the chair must vote if instructed but again the individual, the non-chair proxy, can choose not to vote. In fact, they may not even attend; they may get held up in the traffic or whatever. There is not necessarily going to be a reconciliation between the votes lodged by proxy and the actual votes cast that are reported in the minutes if a poll is taken. Why, therefore, do we have these two? Is it going to cause dissension? Is a member going to pick upon this and perhaps disrupt matters unnecessarily? We have had a lot of problems trying to put our finger on why.

Senator CONROY—This is in relation to proxy votes. Unless the person who has had the proxy appointed does not turn up, with most of what you have just described I am struggling to understand where the impact is.

Mr Factor—The law now requires that the proxies lodged be recorded. Then, if a matter goes to a poll, the votes cast by proxy in that poll must be minuted and forwarded to the ASX. There is not necessarily going to be a correlation between those cast and those granted because the proxy holder does not have to vote on a poll unless it is the chair.

Senator CONROY—There is an 'abstain' column normally in these things.

Mr Factor—No. The instruction may be for, against or abstain, but the proxy can choose not to vote at all, no matter how they are instructed. A non-chair proxy in the law as it is drafted now can choose not to vote. They have a choice: either not to vote or to vote as instructed.

Senator MURRAY—But aren't most proxies in the hands of the chair?

Mr Factor—Most are. But I am saying that the figures will not balance. We had trouble working out exactly what was intended.

Senator CONROY—Shareholders would like to know how the institutions are voting and what the chair is doing. It is fairly simple. I am struggling to understand why you are confused about the intent. The intent is so that shareholders can be informed about in particular the chair, what proxies are held and how they are being cast.

Mr Factor—The chair knows exactly what proxies there are.

Senator CONROY—Yes, I know the chair does, but the shareholders sitting in the meeting might like to know too.

Mr Factor—Should they know at the outset? I have seen meetings disintegrate with very angry shareholders because at the outset the chair has said, in a sense, 'Well, you can do whatever you like, but every decision has already been made.'

Senator CONROY—You would call that an insensitive chair, wouldn't you? One who was looking for an argument, I would have thought.

Mr Factor—No, I have seen some rather eminent chairs do that. I have seen others, who are a bit more skilled perhaps, announce that, not before a show of hands but just before a demand for a poll, to stop any time wasting.

Senator CONROY—I can understand the little shareholder sitting there who suddenly finds out that 62 per cent of shareholders have already voted against them and who therefore does not bother. So I can understand the argument that it may influence the outcome of the final vote in terms of the actual percentage and that it is therefore better to wait until after the vote before it is disclosed. But are you arguing that, even after the vote, that information should not be disclosed?

Mr Factor—No, after the vote the chair would announce to the meeting that the matter had been carried.

Senator CONROY—If the institutions hand over their proxies to the chair, my point is that the institutions are accountable to their fund members and just having the chair say that a vote has passed with a 62 per cent majority does not enlighten shareholders or add to the information available to them. However, if the chair says, 'It has passed with a 62 per cent majority, and I had 50 per cent of proxies in my hand and this is how they were all voting,' there is at least some information there. I do not understand what the problem with disclosure is.

Mr Factor—There is no obligation on the company to ensure that the proxy votes as instructed. That is a matter between the shareholder and the proxy they appoint. In fact, there is a lot of legal argument to suggest that the shareholder has no rights against the proxy unless they have paid them consideration. There is nothing the shareholder can do to ensure that the proxy votes as instructed. We now have in place, for the first time, a law that says that, if you are going to vote, you have to vote as instructed. I think this is a good thing because it takes away the uncertainty that existed between those two outside parties. However, the company still has no responsibility to ensure that the votes are cast as instructed.

Senator CONROY—Do you think it is a reasonable situation that you can hand over a proxy in 'good faith', if I can use that perhaps naive term?

Mr Factor—If you hand it to the company, the company should cast it as directed, but if you hand it to an outsider then no, the company is not a party to that.

Senator CONROY—I think that is a fair delineation.

Senator MURRAY—People like you are very important to us in arriving at a view on matters, but I am interested in how you inform yourself in coming to a position. You mentioned that you could not be quite sure about how this proxy issue arose, and yet submissions were put to the March 1998 committee on this issue—statements from all of the people who were arguing for this position are recorded in *Hansard* and reflected in the report of the time. Would your committee, as a matter of course, look at these things and summarise them so that, in discussing this, you are aware of such matters or do you just approach this as though the committee is already aware of such matters and so try to work out what it all means?

Mr Factor—First of all, most of the responsibility for looking up all of these things ends up with the person present and, like all of us, I have many things on the go. Perhaps my language was bit loose if it appeared that I was suggesting that I did not know how it all came about. What I was trying to state was that I cannot put my finger on exactly what it is trying to achieve. It is disclosure, but it is disclosure that will just hang there. It is not disclosure that will lead to any course of action. No-one sitting there is going to be able to reconcile the two figures and say, 'Aha, something strange happened here.'

Senator CONROY—It may not lead to action for that vote on that day. But let us say I am a one-share share owner and I see that my super fund has voted opposite from me. Maybe I would then like to talk to them about that in future and convince them that perhaps they should not just blindly hand over the proxy to the chair. They may choose to ignore me and say, 'Oh, he is just a nutter,' but in terms of the intent, if institutions are voting or, as in most cases, do not vote, it might be possible to influence that. Surely, more than just the board is allowed to try to influence those issues. In terms of shareholder participation and democracy, I cannot go and lobby people about how to vote on an issue if I do not know who they are and how they voted.

Mr Factor—You would not know how your fund voted because the figures are just in a global sense. I would have thought that your fund might in fact inform you. I think it is a matter between the member of the fund and the fund, as distinct from bringing the company into it.

Senator MURRAY—There are a couple of points that perhaps we should explore. The first reflects the view of those who proposed this: that this was a mechanism to encourage greater participation by people who were not attending meetings or putting in proxies and yet, by virtue of their shareholdings, should be assisting in the management of the company and, as Senator Conroy quite rightly points out, the funds—the managed investment funds and the superannuation funds. That was one main purpose for the mechanism.

The second main purpose reflected the concern that, at times, the vote by a show of hands—the poll—was actually quite different to the vote by the proxies and that that should be clearly identified. Where the proxy shareholders were establishing by vast majority which

way they wanted to go, the poll people were influenced by who attended—or who was manoeuvred to attend, as sometimes happens—and the way in which the chair performed on the day. That is why the pre-vote system was established. I am recounting to you the arguments that were put. In all these things, all that is happening is a greater disclosure and more transparency. Regardless of some of the problems that you have identified, surely you would accept that, in matters of democratic expression, greater transparency and understanding of what has happened is in the interests of all shareholders.

Mr Factor—I do not have any objection to that at all. In fact, at a personal level, I have been quite disturbed by the influence of organisations such as AIMA—just to pull out of the air one that I know; they are not alone here—that may end up with 16 per cent of a company and impose their values on the company in returns for their members when a great proportion of that company's shareholding could be spread across a wider community that sees things a little differently. I do not object to what you say but, unless we are going to get the proxy votes displayed by who instructed what, is the shareholder going to be any the wiser?

ACTING CHAIR—Can we move on. It is a fascinating topic, but there are four remaining issues in your submission. I note that, in the last three, you support the proposal. Is there any comment that you wanted to make about the Corporate Governance and Audit Committee?

Mr Factor—Yes. Perth is a small junior-explorer town and I did some research years ago into the corporate governance procedures before they came into the listing rules among such companies, and the larger ones, and they were totally against it. To have a mandatory governance board was considered a gross overreaction. Most medium to large sized companies have such a board anyway, but the smaller ones duck and dive at the moment and half of them do not even have an audit committee. They say—they have the standard phrase that goes into their annual report—that it is not suitable for a company of their size, and they will do the same with the corporate governance board.

ACTING CHAIR—Would you suggest that it should apply to a particular sized company, with a company that measured defined threshold, a particular market capitalisation?

Mr Factor—That is very much a moving target. Depending upon the flavour of the day, if you are a telco or something, suddenly you have got one and, who knows, next year we might find some other high-tech thing to get into and suddenly you are not. It is probably not by capitalisation. But, again, it has been my experience that the companies that matter—the big ones, the ones where there is a lot of money involved—tend to do it pretty well now. If we could find companies that we could put our finger on and say, 'Look, these are significant corporations and they are failing here, there and everywhere,' what we went through with Coles-Myer a few years ago shook a lot of boards and I think hanging the washing out on the line like that—

Senator CONROY—I am not as confident as you. The AIMA blue book guidelines have been around a long time and they cover not just having the committee but things like the structure, who should be chairing it and having an independent director chair

remuneration boards. They do regular reports and they are not as optimistic or as happy about the situation as you seem to be. Maybe it is a bit different here in Perth and they do not weight it in the same way.

Mr Factor—Possibly it is the professional circle which I work in. Because the people I encounter in that circle are people who are actually interested in this sort of thing, they translate that into their work practices. We did not have any support for that as a mandatory requirement.

If I can just quickly go to the report to auditors, there was some disquiet about that because it seemed to place a person in the position almost of being a fifth columnist within a company. Certainly at a minimum it was regarded that the word 'material' should be introduced, that you only have to report on a breach of legislation that was considered material and that perhaps there should be a first stage to report to the board, and if the board does not act, then go to the auditor. It also did not refer to the behaviour of officers, just of the company, and I was not sure whether the company was meant to include all of its officers and how far down the list of officers. We had a little bit of a difficulty with that one. The calling of a general meeting by one director has got a bit of publicity.

Senator MURRAY—You have made the remark, 'Please advise if the committee would like a copy of this paper,' in your submission where you say that listed companies should by law have a corporate governance board/audit committee. I would like to ask that we do get it.

Mr Factor—Yes, certainly. I do not have it here, I am sorry.

Senator MURRAY—If you could send it to us, it would be very helpful.

Mr Factor—Yes, indeed. I know that the ASX was against the calling of a general meeting by a single director. I personally think that it is a whistleblowing clause, that it is not so necessarily out of place. I do not think it has been abused. I can name one or two directors—

ACTING CHAIR—It has the potential for it.

Mr Factor—It has the potential, but it has been in table A for 50 years. We do not have a history of abuse. There is another angle on it. If a director does abuse it, then they are using their powers in a manner that is not in the best interests of the company. They open themselves up to litigation by the company which, remember, will be literally taking its course from the majority of the other directors. They open themselves up to litigation. I think that is a good way of controlling such behaviour and I personally do not have a problem with it.

There is nothing much on the list on specifying a place, facts, electronic address. Verification may be a problem with some electronic addresses. That is the only submission that we had on that one. Second to last was remuneration. We are going to be looking at standard package clauses there, of course, with the first of the two items. But the one that seems to be winding everybody up, of course, is the five officer emoluments. This does need

correction, particularly for Western Australia. We have a great number of small junior explorers, some of which actually do not even run to five employees. I know that might seem strange, but everyone is on contract drilling holes out in wherever, and back here in town we have got the standard three directors. Quite often they are executives of the company as well—geologists, whatever. Maybe there is one that is independent. And they might have an office manager and a receptionist. That receptionist is going to actually figure in the top five, because the way it is drafted it says 'officers'. That attracts the definition in 82A, which includes employees. It needs at minimum to be given the term 'executive officer' and put into that category within section 9, an executive officer being someone involved in the management of the company. Surely it is those remunerations that were intended to be reported upon.

ACTING CHAIR—Would it be there better to aggregate?

Mr Factor—Banding again? I think that a lot of incomes are already known from the bandings. The bandings have not necessarily hidden too much away. We have received all sorts of arguments—loss of privacy. Increases in salary packaging have been quite strongly pushed, that now we know what everyone else is getting these people will want something similar. But we have got it on an international basis elsewhere. I just think it has been drafted far too widely. But I know that some are very much vehemently against—

Senator CONROY—It was drafted and then ASIC issued a sort of explanatory note. I am not sure that the explanatory note was exactly the same. So I think there is legitimate reason to try to find a redraft on that.

Mr Factor—Yes, I believe so.

Senator MURRAY—In industrial relations law, workplace relations law, there is a cut-off of $68,000, above which you do not have to comply with a number of pieces of the legislation. With this five employees thing, rather than to list a whole load of exclusions, would it be easier simply to say that below a certain monetary amount—let's just pick a figure: $100,000—you do not have to disclose? That would cut out that receptionist and such people. Is that a simple way to do it?

Mr Factor—Yes, it would. That would certainly address the problem I had earlier, unless we have the best paid receptionist in town. They set the figure and you have to keep changing it.

ACTING CHAIR—Index.

Mr Factor—You will need to index, yes.

ACTING CHAIR—Is there anything further? I am just trying to move you along quickly.

Mr Factor—Yes, I know. The last item, which was publicised on the week-end and which I got a phone call about on Thursday, is the requisitioning of meetings by 100 members. That is not in the submission, but I was advised to include it. I would have liked

to have had sitting next to me the company secretary of Wesfarmers. He is my deputy on the Chartered Secretaries. However, he is tied up organising their meeting that they have been requisitioned to hold.

The problem is going to be somewhat quelled; I believe there are listing rule amendments coming up that will stop off-market transfers of non-marketable parcels. But it does not exist right now and we have got this situation where, after all these years, 100 suddenly seems to be too low for some companies. However, I also have a view that there is a major democratic principle involved here that we cannot easily push to one side. With the ASX allowing companies of 500 members minimum or more, 100 members could represent 20 per cent of the membership. So I do not personally think we can just say, 'Cross out 100.'

I was going to recommend that you might like to consider the possibility of joining together 100 members with a percentage of the membership, something like the greater of 100 members or five per cent of the total number of members, say, at midnight on the last day of the preceding month or something like that. So the 100 can be put into context: 100 coming from Telstra is ludicrous but 100 for a small junior explorer or similar is meaningful. So I am not saying we necessarily should do away with the raw number of 100, but join it with a—

ACTING CHAIR—A percentage.

Mr Factor—Yes, a percentage of the total membership. We have also retained five per cent of the votes. That is the suggestion here.

Senator MURRAY—I think you make some good points there, but five per cent could sometimes be ridiculous too. There are companies with, say, more than a million shareholders. So five per cent is 50,000. That is a lot of people, individually, to get. You could have three measures—100, 1,000 or five per cent, that sort of thing. For the very large companies I can see five per cent being very difficult to physically organise.

Mr Factor—The problem is, though, that if we do have a company of the size you indicated then the cost of that meeting is going to be enormous. There is no change out of $50,000 or $60,000 for a company like Wesfarmers to call a meeting. That is not including all the management, time and legal opinions that have been sought and so on. They will be out of pocket, goodness knows; it is not my place to know. But it would be $150,000 plus. They would have preferred, of course, to run that meeting in conjunction with their annual general meeting which takes place only a month or two later, but they have not got the go-ahead on that.

I think we need to focus on what is happening here. There is no reason for these companies to be holding these meetings at all, you understand. Legally, they are not obliged to do so because every one of the matters being put to them by the requisitionists is in fact a crossover into the management powers of the board. The boards have, under their constitutions, power to manage the company. What is happening is unconstitutional. What the companies are doing, however, is saying, 'We're going to get severe odium, et cetera and bad PR in the press. If we don't go ahead, we will be seen to be trying to withhold

something, so we'll go ahead and hold it.' The reality is that, even if resolutions were passed in any of these situations, the board is not obliged to follow them. We have got case after case supporting this position. There is just no need for the companies to do it. It is a PR exercise that is driving them.

That crosses over into the other part of what was advertised at the weekend, that is, 249Q: a meeting must be held for a proper purpose. I just raise the curious possibility that, if the directors of a company think, 'Well, we'd better go ahead because we don't want to be seen to be the bad guys here,' and they go ahead and hold the meeting. They do not have to hold the meeting—it is unconstitutional, in a strict sense. If it costs them more to do that than it would have done to simply hold their proper legal ground and refuse—have they broken the law? Have they set themselves up in a position where they could—

ACTING CHAIR—If the meeting were, at the end of the day, deemed to be held for an improper purpose, do you mean, and the directors have proceeded to hold it in any event?

Mr Factor—Yes. Are they setting themselves up that they could possibly be liable for this extra cost? The normal course of events should be, in a situation of management interference, that the company refuses the request. The members then presumably would commence to take action within 21 days, because the board is required to act, and then the company gets an injunction and prevents it because it is an unconstitutional act by the members.

Senator MURRAY—What would happen if the requisition had to be coincident with an AGM that the company was going to call anyway, provided that requisition was within, say, three months of the meeting? I am bearing in mind all the notice periods and so on. It seems to me that, if you have got an AGM just around the corner, the two should coincide.

Mr Factor—Absolutely, but that did not work down the road at Wesfarmers, so they are going to be holding their special meeting very shortly.

Senator MURRAY—But if the law permits it?

Mr Factor—But the law does. This is one last point I want to make: we are not doing a great disservice to members here because the law, in section 249N, still permits members to put their item on the agenda, and it still allows that to take place with 100 members. I am not even suggesting we put in my five per cent of total membership or anything. They can get an item onto the agenda, under 249N, with simply 100 members. But what they cannot do under 249N is force the company to call a meeting at great cost and disruption. It would just be held in the same manner in which you suggest.

Senator MURRAY—But I am suggesting that you could not within three months of the AGM date. In other words, it would have to be coincident with the AGM date.

Mr Factor—That, to me, makes a lot of sense, yes. But then we have got this issue—and we have got a huge amount of case history to overturn—as to whether the board should be accepting such matters, given that it is an unconstitutional act by the members crossing over into the areas of management.

ACTING CHAIR—At this point, Mr Factor, I am afraid we have run out of time. As you pointed out, a further inquiry was advertised over the weekend and further submissions on it are being invited up until 27 August. So, in the interests of time, if there is anything further that the groups which you represent wish to put in that regard we would welcome a written submission by 27 August. I thank you for your time this morning. We have given you quite an extended period, but there were many matters that we wished to cover. Thank you very much for your input and contribution this morning. If there is anything further, please send it to the committee in writing. Finally, I table the document to which you referred during your evidence, that is, the pro forma notice of meeting of BHP and Email. Thank you, Mr Factor.

Mr Factor—Thank you.

[11.00 a.m.]

EVANS, Mr Paul, Partner, Freehill Hollingdale and Page

MASLEN-STANNAGE, Ms Rebecca, Senior Associate, Freehill Hollingdale and Page

ACTING CHAIR—Welcome. As was pointed out earlier, this is the third public hearing on this inquiry and the committee will be conducting further hearings in Sydney and Canberra. We have received 89 written submissions which we will consider along with the evidence that we receive during the public hearings when preparing the report. The committee does prefer to conduct its hearings in public, but if there are any matters that you wish to discuss with the committee in camera, we will consider those requests. I must also remind witnesses that the giving of false or misleading evidence may constitute a contempt of the parliament. Is there anything you wish to add to the capacity in which you are appearing?

Mr Evans—I appear in my personal capacity and to some extent as a representative of the views of one section of our firm that is concerned with these matters, together with the canvassed views of a group of clients whom we circulated with the committee's terms of reference for the purpose of preparing our submission.

ACTING CHAIR—Would this be Freehills nationally or Freehills Perth?

Mr Evans—No. This is only the Freehills Perth office, although we did advise our interstate offices of the submission.

ACTING CHAIR—We have your written submission. Are there any corrections or alterations you wish to make before making an opening statement and then taking questions?

Mr Evans—No, there are no corrections.

ACTING CHAIR—Is there an opening statement that you would wish to make to the committee, or do you wish to proceed to move through your submission?

Mr Evans—There is something I would like to say very briefly by way of background to this matter. The views which I express are expressed by virtue of 15 years as a practitioner predominantly in the corporate law area, and predominantly in that area as a corporate litigator looking at the conduct of directors and the conduct of companies. It is also expressed in more recent times by virtue of the fact that I am a director and sometimes chairman of two public companies at the present time.

The submissions which we put in reflect what appeared to be a key issue underlying the terms of reference, and that is a question of philosophy—political philosophy or economic philosophy—as to the purpose of a listed company; that is, whether it is an economic animal or a social animal. The submissions are drafted from the perspective that it is an economic animal and exists to serve economic purposes in the community and not other purposes.

If that is the case, and that is the thrust of the submissions, then the principal underlying philosophy at the moment is one of corporate agility. As I am painfully aware in one of my capacities as a director, Australia is a very small player and Australian companies are incredibly small players in the world market, and in all world markets. Fleetness of foot, consistency of purpose and coherence of objectives are critical components of business success.

In one company of which I am a director at the moment we are looking at a transaction which is in the early stages of formulation. Going to shareholders to gain the necessary funding approvals for that transaction is going to take somewhere in excess of 80 days under the current timetable, once we have factored in ASIC approvals, ASX approvals, drafting, timetabling and presentation to members. That same transaction could be approved by a junior regional manager of a large American corporation in 48 hours. I hope that gives you some stark illustration of the difficulties one faces in layers of corporate governance and the difficulties which are faced by Australian businesses where most Australian listed companies are still small listed companies.

In relation to the particular items in our submission, perhaps I will deal with items 2, 3 and 4. With item 5, we simply stand on the submission, unless the committee has any queries, and items 6 and 7 Ms Maslen-Stannage will deal with primarily, save for any interjections that I might make based on my personal experience, and there have been a few touching upon items 6 and 7.

ACTING CHAIR—You will start with proportional voting?

Mr Evans—I am sorry, it is items 5 and 7. Yes, we will start with proportional voting.

ACTING CHAIR—Perhaps you can expand on the position you put forward—that the proportional voting system is not appropriate for listed companies.

Mr Evans—In general terms, the question of proportional voting comes down to a balance between what I call representation and coherence in direction. A representative board might be thought to be a board which represents broadly a wide constituency, as does the parliament. In economic and practical management terms, my belief is that that is not the case. The whole purpose of joint stock companies is to bring together capital from a wide base of shareholders to pursue an object of making a profit. That is why they exist. That requires, in our environment, a great deal of agility. To secure that agility, one needs a quite cohesive and, in many cases, strong board and executive direction.

Proportional representation means a representation of minority interests. While board debates are often vigorous they should, in my view, be vigorously directed towards the primary object of the company, which is making money for its shareholders, rather than power plays between groups of shareholders. Those power plays should be won and lost on the floor of the meeting and not repeated on every occasion on which the board of directors meets to discuss the business of the company. The problem with proportional representation is that inherently it embeds the continuity of such plays.

Basically, the purpose of our listed company structure is to ensure there is a market in which dissatisfied shareholders—those holding minority positions—who see no future benefit in those positions can exit their economic interest in the company at whatever price the market is prepared to pay for it. The public company system should not exist so as to perpetuate minority positions in what I call a position of political power inside a corporation. It should, in fact, encourage minority players to quit the corporation if they do not believe their interests are being served. That is the purpose of the market—to provide them with the vehicle for doing that.

ACTING CHAIR—We have some concern about the loss of corporate knowledge or institutional knowledge.

Mr Evans—It is certainly the case in relation to a wholesale change of the board. Such losses of corporate knowledge do occur, particularly in smaller companies where perhaps they occur too often—maybe because a large shareholder acquires a position in which they can split the board, and that happens. That can be a very expensive exercise for a company. I take as a simple example a mining company which has two or three projects. If its board is also effectively its executives, as is often the case, the departure of that board when a new majority shareholder comes along effectively means the loss of all institutional knowledge in relation to those tenements and their history, and quite an expensive relearning curve for the new board management structure in recapturing that data from the company's records, such as they may be. That is a very simple example. In a large company the position is perhaps worse because the financial complexity of its arrangements, the history of its dealings with key suppliers, key customers and so on, are likely to be more complicated and, therefore, the value of institutional knowledge that much greater.

ACTING CHAIR—Do you have any concern about the oft-expressed concern that there is not enough diversity in board representation within Australia?

Mr Evans—It is quite probably the case that there is not enough diversity. There are probably two or three reasons for that, none of which have anything to do with proportional voting. One is that it is quite difficult to get quality directors in Australian companies. The remuneration is generally inadequate, particularly at the lower end of the board. There are very few companies that can even afford to pay non-executive directors the amount which the Australian Institute of Company Directors recommends as being the minimum for effectively remunerating a director for service. Even a professional director is practically limited to carrying four or five boards in different areas, because it is difficult to be a director of two significant companies in the same area when you are dealing with an office which will take up practically 15 to 20 per cent of your time on a full-time basis. The larger the company the greater the necessary involvement. That is one aspect—diversity.

Senator CONROY—John Ralph must be a superman.

Mr Evans—John Ralph does very well in his capacity.

Senator CONROY—I think there would be about six or seven of them.

Mr Evans—Yes, and how he does it I am not sure. I am a director of two small companies, and that takes a good two to three days a month of my time in addition to my practice. Those are companies with very limited scales of operations which are quite focused. To deal with the diversity of those operations would challenge most people. Mr Ralph obviously rises to the challenge exceptionally well. That is one of the aspects. I think it is very difficult to persuade people because of the availability of remuneration. Secondly, there is a relatively small pool in this country of executive talent—those who have a range of management skills, professional qualifications and time to fill those offices. We have well over 1,000 companies on the boards at the moment with a minimum requirement of somewhere over 5,000 directors. Even allowing for overlapping groups in the juniors, that is still quite a significant number of people in a country with two-thirds the population of California.

ACTING CHAIR—There is an argument, of course, that that pool of directors will not expand unless we ensure that the turnover is such that people get an opportunity to serve on boards. It becomes circular.

Mr Evans—There is a circularity in that sense. It is indeed the responsibility of the boards themselves to ensure that they are bringing on fresh blood, some of whom will be in executive ranks and moving on to the board. To the extent that that is encouraged, I do not necessarily think that is a good idea. The other area is executive search, where boards have to go out and actively look for directors who are appropriate to their operations. Major shareholders have to go out and actively look for directors who are appropriate to a company's operations when they nominate them.

Senator MURRAY—Everyone knows the problem exists, but it is the solution that is hard to find. I want to really explore the solution with you. We have three main scenarios, but there are many others. The first is that, where there is a majority shareholder of over 50 per cent, they determine the entire board and the other 49 per cent can go hang if that 51 per cent decides. Telstra might be an example. The government effectively determines the board. The government may well decide to spread that load. And I do not cast any aspersions on the directors—that is just an example.

The second example is where minorities dominate. Take a media company. Media proprietors are constrained by law in terms of their percentage and yet everyone knows that minority media proprietors dominate the entire board. A 30 per cent owner in fact tells the 70 per cent to go hang. The third example is where you get genuinely dispersed shareholdings. Everybody has a minor amount. There are not easy examples that come to hand, although I guess the 33 per cent of Telstra would fall into that category.

In each of those examples, substantial numbers of shareholders are potentially disadvantaged by the method firstly of director election and then of director perpetuation of the culture, style and nature of directorships. Proportional representation is one way of trying to deal with that issue. Preferential voting is a second way of trying to deal with that issue. The third way, which we discussed earlier with Mr Factor, is the potential for far better information and design of the voting process in terms of the existing constitutions. They are simply badly done, and Mr Factor gave some good examples of that. If you accept that there

is a problem—and you might not—how do we, as people who are attempting to introduce better standards of corporate management or governance, approach this problem?

Mr Evans—It seems that me that you are articulating the problem as being one where there is a perceived paucity of good corporate governance because of the control factor—that is, the fact that the board tends to be appointed predominantly by majority shareholders or by a group of influential shareholders. For practical purposes, I have combined items 1 and 2. My experience suggests that 30 per cent to 35 per cent of a company is normally sufficient to secure control of its board if you are minded to do so. Once one has that position—

Senator MURRAY—Which you could not have under proportional representation.

Mr Evans—That would be true if one had candidates who were prepared to stand to represent the proportional interests. Taking the example of a mining company with a board of three, proportional representation suggests that your cut-off is around 27 per cent in order to get one into each slot in the three. A board of three may be all that a mining company can afford. I am a director of a mining company which has a very few hundred thousand dollars in the bank. It has three directors; it has one employee.

Senator MURRAY—Are we talking listed companies here?

Mr Evans—We are talking about a listed company. Perhaps we consider ourselves better off than many junior miners in Western Australia at the moment. One has those two situations—one, the control group and, two, the open register. I would indicate here that one of the companies I am a director of has a very open register. The top 10 shareholders control less than 30 per cent of the shares, which is an unusual situation in Australia these days.

You are looking at two different appointment models. One is the controlling shareholder appointment model. The question there is: does the shareholder use their voting power, their economic interest in the company, to appoint all the directors or a majority of the directors, leaving either the directors to appoint the rest or using some executive search model to appoint some independents? That is good corporate governance and probably the model commonly pursued today. There would be few companies of which I am aware where a majority shareholder would pursue absolute control, unless there were some pressing business issue for it that drove that imperative. It simply does not give the right appearance for dealing with shareholders. If one goes to that model of exercising control, one may say, 'That's a matter of the shareholder's economic right, at the end of the day. It is a manifestation of majority rule in its simplest form.'

For the wide open register, the usual question is a very simple one: are the directors who are in office doing a good job as the shareholders perceive it? That is a question of the quality of the reports that they are receiving and the quality of the performance of the company. If there is a wide open register, it falls in anybody's hands to move to displace the directors or, perhaps more commonly, to go out and find somebody who is prepared to bid for the company if they think the company has a business whose opportunities can be maximised under other hands. If you do not like it, you sell out on the marketplace.

ACTING CHAIR—Perhaps we could now proceed to the environmental regulation.

Mr Evans—We could deal with 2 and 3 together, in view of the time.

ACTING CHAIR—Certainly.

Mr Evans—Both of these are matters dealing effectively with self-disclosure—disclosure of possible culpability. The question there is again a philosophical one: is this about economics and the financial interests of shareholders, or is it about social policy in some manner in which listed companies are being particularly targeted for a particular obligation? If it is about economics and the disclosure of shareholder value in relation to compliance, the primary tool for shareholders in ensuring that they know what is going on in a company is the Australian Stock Exchange listing, or 3.1, which makes mandatory the disclosure of material price impacting information about the company on an urgent basis. In other words, as soon as you have material price sensitive information, you have a mandatory obligation to disclose forthwith. If you do not do so, you become non-compliant with your continuous disclosure obligations and run into a host of problems both with the exchange and with the commission.

If one has a serious environmental problem—a discharge, an explosion or something of that nature—then one has material price sensitive information almost undoubtedly. One has a disclosure obligation as to the nature, extent and possible impact of the problem. What one does not have to do is assess and disclose culpability or one's position in relation to that. The same is true whether it is environmental or whether one is prosecuted by the Competition Commission for a trade practices breach.

The question is this: why should you as a listed company be obliged to disclose to all and sundry your position in relation to the contravention when nobody else is subject to that burden? That is a philosophical question and one that I cannot answer. I can only say that, from an economic point of view, one should not. From a legal perspective as a defence attorney, one should not. As a plaintiff's attorney, I would love you to because it gives me an advantage. It gives me something to go and beat you over the head with regarding your shareholding base. It gives me something to go and beat you over the head with in court if you have an available admission.

If you state your position early and incorrectly, as often happens, because one cannot necessarily assess your position accurately in haste, then one has a contemporaneous admission which can be used against you when your defence subsequently changes. That is simply unfair to the company. It is unfair to its shareholders, because at the end of the day the person who loses out when the company loses is the shareholders who have invested their money. They are the first blast line of loss.

ACTING CHAIR—One of the matters that concerned me in relation to the environmental regulation requirement was precisely the philosophy behind it. If it is to be more than just continuous disclosure, then where does one draw the line? Why would it not be then a statement about your industrial relations standing or level of compliance or occupational health, safety and welfare? Where does one draw the line? What does the continuous disclosure obligation mean if it does not mean to cover those sorts of situations?

Mr Evans—Your lists in rule 3.1 on obligation will affect all of those things. If one has a major industrial relations incident, then it will be picked up under ASX 3.1. If one comes to line item reporting, and basically this is the start of line item compliance reporting, one can think of instances where companies might have three line item reports because there are really three sets of legislation which affect them. I can think of one venture we looked at a while ago which had 53 separate regulatory bodies at a state and Commonwealth level who were responsible for the regulation of the operation of that organisation which required 53 compliance reports.

Apart from the simple cost of that, when one is looking at being open and transparent in the marketplace, how far does one have to go and what level of obligation are you putting on the directors and the executives to go into a due diligence exercise for any reporting purposes? It is hard enough to get directors to take office at the moment. If you are going to get directors to sign off on non-fundraising—in other words, it is not something you have to do in order for the company to survive—due diligence on a semi-annual basis on 53 different regulatory compliance regimes, you will have a lot of very unhappy and very expensive directors because of the time it takes to undertake that sort of exercise.

ACTING CHAIR—In relation to the second aspect, the requirement to summarise allegations and the company's position under Corporations Law or trade practices, have you considered what would be the status at law of the company's response? Currently, if there is a statement of claim in, say, a trade practices proceedings, it can contain all sorts of allegations in relation to what might constitute misleading and deceptive conduct. There could be all sorts of defamatory imputations arising. I assume that under this the company would be obliged to set them out, or at least the substantial aspect of it, and then its response which might also reflect upon the plaintiff applicant. Have you considered the status in terms of defamation of what would be covered by privilege?

Mr Evans—There would have to be an argument that if a disclosure of that nature is required by law it would be covered by qualified privilege. That, however, is by no means clear. One would certainly want to ensure that that privilege attached. To take an example, your standard statement of claim published by the commission against a trade practices contravener these days will generally join in the officers involved in the contravention who are directly personally liable. The company publishes the report that the company and X, its chief marketing officer, have been prosecuted for a contravention of section 45 or 45A relating to price fixing. That is one impact. It has a direct and immediate impact upon the individuals concerned where blame may ultimately not be established.

Secondly, the nature of the types of allegations that are made, particularly in the trade practices context, are such that it is almost impossible to state a position at an early stage in the proceedings which is meaningful, other than to simply deny. I will give you one good example of that. I was involved in a contravention of section 45 and 45A claim on behalf of a number of Perth companies a few years ago relating to price fixing and market agreement. The commission pleaded against those companies 26 separate markets in which a contravention was alleged to have occurred on a tiered basis from the finest to the broadest. The market they ultimately established was a question which determined culpability. If they established the finest of markets, there was a clear contravention. If they established the broadest of markets, there was no contravention. The economic factors that go into market

analysis to say which market in fact exists are so complex that they are rarely resolved at below full court level. First instance judges regularly err in their market definitions.

So the company is left in the position of saying, 'Well, I've got this list of allegations against me which I have to publish.' The defence is a denial, because that is basically the only defence one can make at that stage. The company then says, 'We will find out whether we have contravened based upon the determination of what the market is some time in the next two years.' You have met that disclosure. Whose interest has been served by it? The fact that the proceedings have been commenced will already have been disclosed in the listing of rule 3.1.

ACTING CHAIR—Would the company also be required to give some sort of assessment of its downside, its culpability or if the breaches are found to have occurred?

Mr Evans—A contingency note will invariably be required by the auditor. At an early stage in proceedings the inevitable contingency note is that we will make provision for legal costs but otherwise we will make no provision because firstly we deny liability and believe we will be successful and secondly we have no idea what either the penalties or reparations will be in the event of success.

ACTING CHAIR—So what does that tell the shareholder?

Mr Evans—Absolutely nothing, other than the fact that they are going to cop a very expensive legal bill in the near future, which they know by virtue of the fact that the commission has commenced proceedings against them. That is the one inevitable corollary of commission proceedings.

Senator CONROY—I just have one question. I am not sure if it is exactly in this basket, but I am interested if you are able to comment. If you are not for any commercial reason, please say. In relation to Ok Tedi BHP, at what point should they have disclosed? That issue was an ongoing one for a long time before it became a very serious issue. Does that sort of problem fall within this reporting? You would argue that it should have been disclosed continuously on the way due to the listing rule. Was it in your experience?

Mr Evans—I have to say that I was somewhat engaged in other things when Ok Tedi blew up and therefore did not pay a great deal of attention other than to Slater and Gordon's manoeuvrings for a compensation claim. In my view it is plainly an ASX 3.1 disclosure question, the threshold for disclosure being the apprehension of material financial risk to the company. When that threshold was crossed I have no idea. My recollection of the papers the other day is that only now have BHP actually formed the view that they have an irremediable problem despite their settlement. Undoubtedly, there have been many millions of dollars of consultants' fees expended in reaching that conclusion. When that conclusion could have been reached, one has no idea. They had the obligation. They have either met it or they have not. Certain consequences would flow from those positions.

Senator CONROY—You described earlier the philosophical position of environment social justice as opposed to economic. I think the point certainly that Senator Murray would make is that they are interlinked. It is just not as simple as drawing a line between them. I

am not an expert other than from what I have seen in the media—I have not followed it closely—but anybody who went and stood next to the mine could see the degradation around it and could recognise that there was a potential problem.

ACTING CHAIR—Liability is another question, though.

Mr Evans—Liability is another question, as is impact. It is a quite complex political and commercial question in that regard given that my understanding is that the Ok Tedi mine underwrites a fair amount of the Papua New Guinean economy. It has certain preferential environmental rights because of that.

Somebody has done a cost-benefit analysis, correctly or incorrectly, at a political and commercial level, to say this is or is not an acceptable cost. If the cost-benefit analysis says—and BHP was proceeding on the basis that it did—that it was acceptable from a broad social and economic policy perspective in PNG to do what it did, then it has no listing rule disclosure obligation because everything is on track, as far as it is concerned. It was wrong or may have been wrong, as it turned out, as the Victorian proceedings may have demonstrated.

However, I think that raises such a complex problem that it perhaps illustrates quite starkly the problem of this sort of obligation. What environmental obligations do you have an obligation to disclose—your PNG obligations, your Australian obligations, your PNG activities tested against your Australian obligations, the financial impact of those obligations? If so, whose interests are then being served: the shareholders, your Australian stakeholders, your PNG non-stakeholders—that is, the people on the ground in PNG as opposed to the PNG government?

Senator CONROY—Do you think that is causing a rethink of that 3.1 disclosure rule, in terms of having to cope with that? If I was a BHP shareholder, which I am not, and all of a sudden—

ACTING CHAIR—He hastens to add.

Senator CONROY—I am not a shareholder in anybody. I would be reasonably frustrated if it had not been indicated to me earlier—just from an external perspective—and this liability suddenly just blew up in my face. In terms of that disclosure issue, do you think all those points that you have just made are causing a rethink on 3.1?

Mr Evans—Certainly, everybody looks at 3.1 very closely. But 3.1 is only a current manifestation of our long evolutionary line which moved us to the continuous disclosure model. I think in 1995 we had the principal amendments that moved us to continuous disclosure: the enhanced disclosure listed entity model. Are those arrangements working better than they were in the 1970s and 1980s? I think undoubtedly. Are they working perfectly? No. Will they ever work perfectly? No.

At the end of the day, if somebody wants to bury something, they will bury it. It does not matter how much you legislate to require them to disclose it, it will not come out. Do you put in place such a web of sanctions that the critical information which must be

disclosed comes out? Yes. And in most cases it will, but not in every case. You will never achieve a model that does achieve that in every case. The information you want out requires you to assess what stakeholders you want to serve and what philosophy is driving the service of those stakeholders.

Senator MURRAY—The parliament attempts, through the committee process, to address situations—as in this instance—where disclosure which has not been occurring in the past should be encouraged to occur in the future. So, in 1996, the committee unanimously agreed that major legal transgressions of the Trade Practices Act and so on should be appropriately disclosed. And so it was with environmental matters. What they were looking for consistently was material and significant financial risk disclosure which could affect shareholder value to some major degree. As we all know, environmental matters can result in hundreds of millions, not just a minor amount. Listening to you, it seems to me that you accept the principle of proper disclosure of not only present risk but reasonably foreseeable substantial future risk.

Mr Evans—Indeed, Senator. And I think the mechanism is already there.

Senator MURRAY—Yes.

Mr Evans—That is the whole point: that listing rule 3.1 does provide that legal—

Senator MURRAY—I think that your argument is that it is inappropriate to expand it because you have got it. The difficulty parliament faces is that, unless the disclosure rule is sufficiently expansible or sufficiently well developed, there may still be areas left out. You then get an argument about the kind of definition you should pursue.

Let me put a precise question to you and see how you respond. Emission standards are currently a major issue. European and American standards, particularly European, are ahead of Australian. Australia has now agreed that they will catch up. The consequences of that are very significant costs to refineries and quite considerable costs to transport companies and anybody who uses engines which have emission results. We are talking hundreds of millions of dollars. In your view, would it be appropriate for a company which is publicly listed to disclose the fact to its shareholders that, in its opinion, it is likely to be obliged to catch up to European emission standards, and that that would entail significant financial investment and shareholders should be aware of it? Or, because that has not materialised yet and legislation has not been enacted, should they just ignore what is a reasonable assessment of future risk?

Mr Evans—That is a very well-tailored question, because I happen to be a director of a company which produces compressed natural gas conversion kits for diesel engines and so it is of particular interest.

ACTING CHAIR—I think it is just coincidental, isn't it?

Senator MURRAY—You know me; I might know that.

Mr Evans—To the extent that a proper analysis of the impact of those emission standards which discloses that the introduction of the standards is reasonably proximate and reasonably foreseeable, and that there is a reasonably finite cost associated with them, then the company should make a disclosure at some stage in relation to its future capital expenditure requirements. When that stage is going to be a matter for fine judgment. I would be very surprised if it was other than part of an annual reporting package, and really only then in the context of a future capital expenditure projection or a future revenue impact projection.

One has to say that the variabilities of business cycles are such that, if it were beyond next year or perhaps the year after that, I would be surprised if one could meaningfully forecast an impact on the company such as to merit a disclosure of that specifically, as opposed to any other business risk.

Senator MURRAY—That is a strange remark coming from someone who is so experienced in mining, because typically mining investments have long lead times in terms of forecasting. You really do have to take a view of a market in five or 10 years time.

Mr Evans—One does, and one does so with one's heart in one's mouth because, if you look at a standard discounted cash flow model of the net present value of a mining project, it has so many assumptions in it that one has to say that, although it is not meaningless, it is at least risky. One sees that, in fact, in the current debates that have been going on in the courts predominantly in relation to takeover predictions.

Senator MURRAY—But the fact is you still do it, and you still do disclose it to shareholders.

Mr Evans—One does that, and one only does that because one has to make a sensible business decision about going into an investment or not. Any business decision is based upon saying, 'Do I think that I am going to make a profit at the end of the day based upon these eight assumptions?' If you take one standard gold mining project, the assumption is that when I drill out the reserves as I start my mining project, I will in fact have the number of tonnes there; I will in fact have the number of grams per tonne in that reserve; I will in fact get the metallurgical recovery as a percentage of grams per tonne; I will in fact be able to sell that at a nominal gold price; and I will in fact be able to sell that US dollar denominated gold at a dollar price.

Senator MURRAY—All that should be disclosed to present and future shareholders. That is the point.

Mr Evans—Frankly, one does not actually disclose that much detail ordinarily, unless one needs to do a specific capital raising upon it. In that case, one may and one heavily caveats that by saying, 'These are the eight key assumptions. They are subject to all these qualifications as to what may happened.' If you are looking at a situation in which that emissions package is one part of the business of a refinery, as one example, or one part of the business of a transport fleet, one combines that capital cost expenditure of the refinery with the variability in the oil price and the variability in market demand. To take an American example which is not so applicable here, whether it is a warm winter or a cold

winter will impact upon your profits for the next two years far more than almost any capital expenditure that one can conceive.

It is a much more complex projection for a company which is what I call an active trading vehicle than a mining company which is looking at a single project on a single set of assumptions based on some solid research. Therefore, it is a question of imminence in relation to disclosure. I disclose in a mining company because I have a project which requires funding or a project which I am initiating. In an ongoing business, I disclose impact over the next year or the next two years if I can predict the whole mass of factors that impact upon my bottom line profit and my bottom line balance sheet over those two years. It is a much more complex exercise for that sort of trading enterprise than for the mining company.

ACTING CHAIR—Are there any other matters that you want to deal with?

Mr Evans—No, I think that deals with my part of it.

ACTING CHAIR—Ms Maslen-Stannage, would you like to talk about the 28 days notice?

Ms Maslen-Stannage—Our main concern here is simply that a measure which is apparently intended to improve notice can, in fact, result in a lesser standard of information going out to shareholders. The reason is that the information is more stale that it would have been with the lesser period of notice. It is not just 28 days. In addition to that, you have to allow a period for drafting the documentation, printing and there might be ASX vetting requirements and ASIC lodgment requirements. So, in some cases, the information that actually gets to shareholders is already perhaps up to two months old. That additional two weeks being added onto the period for ordinary resolutions, we say has actually lessened the quality of information as a result.

There is a secondary concern and a relatively minor one which is that two weeks has actually now been cut off the period for calling your annual general meeting. One only has to be on St Georges Terrace in the last week of the AGM season and see the brokers running from meeting to meeting to see how difficult companies find it to make the deadline anyway. Now they have two weeks less than they used to have.

ACTING CHAIR—What is your suggestion for the notice period for a general meeting, if not 28 days?

Ms Maslen-Stannage—There is an element of the 'if it ain't broke, don't fix it' thought behind the previous regime, which was 14 and 21. However, perhaps 21 is a compromise. You still have a problem with the staleness of information, but at least it is one week less. As a matter of practicality, people have to have sufficient information, so you cannot give it to them two days before the meeting is on. Certainly, we would say a lesser period than 28 days.

ACTING CHAIR—We will move to the next issue, which is the information about proxy votes.

Ms Maslen-Stannage—With that one, we really did not wish to add to what we have said here. It is a replaceable rule, so, in the scheme of things, we do not see this being as material as our other submissions. We are happy to answer any questions on it.

ACTING CHAIR—Are there any questions? No, there are not. What about the remuneration issue?

Ms Maslen-Stannage—It boils down to two concerns. One is the privacy and security concerns of the particular executives who will have their remuneration disclosed. On the other hand, you have the interests of the company, where their prime executives' remuneration packages are now to be revealed in detail, giving information to competitors as to exactly what sort of package might entice that particular executive away. We say that there are those two concerns.

On the other hand, it does not seem that by mentioning the name of the specific individual attached to each package—as opposed to the band system where it is on an anonymous basis—that there are improvements on the corporate governance side. The question is whether the board is remunerating its executives appropriately. That is something that you judge the board on as a whole, and we say it can be judged by looking at the executive remuneration as a whole, without having to boil it down to individuals.

Senator MURRAY—I have a question on that. That proposition of yours does not address the problem that has been identified by shareholder groups who have campaigned for this. The problem essentially is that self-perpetuating boards of directors can act contrary to the long-term interests of the company by focusing on present value rather than future value. In other words, they benefit present shareholders rather than future shareholders by indulging in management decisions and board decisions which advance the values of the shares short term, but may in fact be negative for the company in the longer term. The second major argument is that individual directors' packages and remuneration voted on and determined by they themselves—even if approved by the general meeting—are not related to performance. So, the share value goes down and profits go down, but they still have an increase in their return.

So all those accountability issues have driven the desire for disclosure. On the other hand, you have quite rightly indicated the difficulties of privacy and in some circumstances the possible danger of kidnapping or things which have happened in other countries. How do you deal with the legitimate concerns if you do not go for disclosure?

Ms Maslen-Stannage—Perhaps I could start by addressing your first point about the directors' duty to future shareholders as opposed to current shareholders. I see that a little differently as the board acting for the existing shareholders from time to time. I am a little surprised at the idea that the obligation would be to future shareholders rather than being an ongoing obligation to whoever are the present shareholders at any point in time. However, the other aspects—and that one, to an extent—are, I would say, adequately addressed by the band system. It is board performance which the shareholders need to be able to judge, and board performance can be judged by seeing what is being paid without specifically knowing to which individuals it is being paid.

Senator MURRAY—But doesn't the individual relate eventually to the ability of the shareholder to decide whether a director should be re-elected, for instance? How would you determine it otherwise if you cannot identify personal performance?

Ms Maslen-Stannage—Are we talking about executive directors?

Senator MURRAY—In the example I am giving you, yes. I recognise the problems you rightly identify, but the shareholder groups demanding disclosure internationally—this is not just an Australian trend—believe that the two issues that I put up earlier, and possibly others that my colleagues could add, require the need for disclosure.

Ms Maslen-Stannage—Again, it is a slightly novel proposition that shareholders vote on the re-election of a director based on the remuneration of that individual because the remuneration of the individual reflects on the board as a whole, and while I can see that shareholders may vote against whoever is up for election because they feel that the executives and directors are being over-remunerated—

Senator MURRAY—Without passing any judgment, let us give a current example, and I deliberately, on the record, indicate I do not pass any judgment. Mr Trumble from AMP was very highly remunerated—strong options, good cash returns, et cetera—and there was a strong feeling amongst shareholders that that, relative to the actual performance of AMP, was not justified. Eventually—this is my judgment from reading the informed press on the matter—he lost his job because of that circumstance. Without the disclosure of his options, his remuneration and so on, there might not have been that impression of the inappropriateness, the distance, between return and performance.

Ms Maslen-Stannage—This begs the question of the performance indicators that the shareholders are using.

Mr Evans—Senator, quite frankly, Mr Trumble's remuneration may have been quite irrelevant to the board's ultimate decision to terminate him. The question was: was he producing the results that the company required through its board? If he was not, whether he was being paid $1 million or $10 million ultimately would not have mattered; you would not have kept him on at $300,000 if he was not producing the result because, in a board which is setting a strategic direction based on performance, you will reward performance and punish non-performance irrespective of the remuneration. Remuneration then comes into issue only in asking: what do I have to pay in the marketplace to get somebody with the skills mix that I expect to produce the performance that I set in my strategic directions?

I am going through an exercise at the moment to hire a new chief financial officer and I expect to pay several tens of thousands of dollars to recruit this person and I expect to pay them many more tens of thousands of dollars. I do not particularly want, in three months time, after the guy is just getting up to speed on his job, my competitor down the road to come along and say, 'I know you are being paid $165,000, plus these options and these benefits. I will offer you $185,000.'

Senator MURRAY—There is the issue of public accountability. In the public's mind—although, I know strictly speaking it should not be compared—listed companies are a public

property and millions of Australians have an interest in them. The principle of public disclosure of remuneration and packages is very widely established throughout the public sector. The remuneration of every person employed by government is available for people to know. If you want to know what a director-general or a parliamentarian, and so on, earns you can find that out. Why should it be that for hundreds of thousands of Australians there is that principle of disclosure established—quite properly—when they are receiving taxpayer funds, but it not be the same for the leading executives of publicly listed companies?

ACTING CHAIR—Mr Evans, you do not have to comment on the suggestion that anyone would headhunt parliamentarians, if they knew their salary.

Mr Evans—I will resist the temptation!

Ms Maslen-Stannage—A key difference is that there the disclosure relates to a particular office which will often have a number of people occupying the same office. Therefore, there is not the same attention on an individual attached to that from a privacy perspective. We know from the media reporting we get that it is a very popular topic in the media to know precisely how much a person in business is earning. When we get the media talking about how much politicians are earning, it is not the singling out of individuals as it is when we see the earnings of others.

Senator CONROY—We are denigrated as a class, don't worry.

Ms Maslen-Stannage—But there is a sense of anonymity, despite the fact that people know what individuals are earning, because there is not the same specific attention on an individual.

Senator MURRAY—Are you sure? In Western Australia everyone knows what the Police Commissioner gets, for instance. I think it was banner headlines on the front page of the newspaper.

Ms Maslen-Stannage—Yes, but it is not seen to reflect badly on that person as an individual. Using your example of Trumble, there was some very negative publicity directed towards him as an individual due to the amount that he was earning.

Senator CONROY—I come at it from a slightly different angle from Senator Murray. I am not so fussed about the aggregate level of remuneration and what you have had to pay to get this individual as opposed to that individual. I come at it from the point of view that a general meeting is required to pass a resolution about a change in remuneration. My view would be: how can I vote for a change if I do not know the aggregate? The salami slicing operations is what goes on now, where one year it may be the options package that goes up and another year it may be the director's fee that goes up, et cetera. As a shareholder, I may have just bought into a company, or I might have been there for 10 years, and I am asked to vote on an options package without having the capacity to calculate whether I think it is a fair increase, because I do not know what I am dealing with.

Mr Evans—Are you talking about directors or executives, because there are some differences between the two?

Senator CONROY—For simplicity, let us talk in terms of an executive director.

ACTING CHAIR—An executive director or executive officer?

Senator CONROY—I am not up on Corporations Law to truly understand that distinction.

Mr Evans—The distinction is important because of the way the packaging is done in a practical sense. Directors receive a proportion which may not add up to 100 per cent of a lump sum allowance for directors fees. Traditionally, they are allowed to portion that out amongst themselves to reflect the different responsibilities and the different burdens they bear.

Executive directors may be remunerated on two bases: simply through their executive package or, perhaps more commonly—it is hard to say—through a combination of the two. That is to say, they receive a certain component as directors fees and a certain component as their executive remuneration. Executive officers receive only their executive remuneration. So at the executive director level there may or may not be an overlay between the director's chunk of funds—increases in which are approved by a general meeting explicitly—and between the remuneration pool that is the salary cost to the organisation. That distinction is somewhat important. If one is looking purely at an executive officer—that is, at a chief financial officer who, we will say, is not a board member—he receives a salary plus benefits package for doing his job as an employee, as an executive officer.

Senator CONROY—Let us start with that individual and then, if we have time—which I doubt—we can work back through. Let us say that we decide this year that we want, instead of giving an increase in salary, to give an options package. If you were to go to the shareholders meeting and say that you want to increase that individual's salary by $20,000, perhaps mentally I can work out whether $20,000, in terms of what he was getting or of the performance of the company, is a good thing. If the options package is clearly ill-defined—and many companies are currently trying to argue that it is not possible to define the value of an options package; I would be interested in a submission on that—how, as a shareholder, am I, sitting there with my one vote, meant to determine, when an options package comes on the table, whether that options package is a fair increase or not?

Mr Evans—Senator, as a shareholder, you will not get a say in the matter, I would have to say. If he is purely an executive, that is not an issue for the shareholders. It is part of the managing director's and board's question in packaging that officer's remuneration, within the context of a plan which would probably have been approved by shareholders before. Most option plans and share plans are approved by the shareholders, and they generally go something like this: the directors may allot up to five per cent of the issued capital of the company by way of securities or convertible securities to employees, as part of an employee incentive plan.

The individual number of securities to be allotted to a particular employee—and even, to some extent, the terms of allotment—will be set by the board and the managing director. Only directors require explicit approval for the allotment of any form of securities by a special resolution, and those require individual line item disclosure of the number of

securities to be allotted to the director and the terms of allotment and, together with that, it will list globally the remuneration of the board.

So what one will see, in the annual report or whatever other current financial disclosure there is, is a global disclosure of the directors' emoluments and the banded disclosure of their individual allotments unnamed, and then the option or share package going to individual directors—with a stated rationale. That statement is required to be lodged with ASIC for approval by ASIC 14 days prior to dispatch to shareholders, and it requires ASX screening as well, for quality and quantity of information.

Senator CONROY—You have probably just argued my case for me. I can only make one further comment in terms of the philosophical position you talk about in relation to economic entity and social entity. Many studies around the world, recent OECD ones, show that good corporate governance leads to improve market performance. I am not sure where you would define corporate governance in terms of social or economic entity. I got the impression, can I say, that you seem to think that some of the corporate governance issues that were perhaps under discussion, as well as others that we have glossed over more today, would perhaps not necessarily fall under 'economic' entity. Can I put to you in closing that certainly I myself would see some of those corporate governance issues in terms of the economic value issue.

Mr Evans—Absolutely, Senator. I would not for a moment doubt that good corporate governance leads to good performance, if it is done well. But, the reason it has probably been done well is that the company is a good company, with good management doing it well. If it is a good company with good management, it will have happy and wealthy shareholders. It does not get that way by virtue of black letter prescription, I would have to say. It is my very strong impression that black letter prescription does not drive that result.

Smart managers and smart directors who are themselves well remunerated generate that result by making wealthy shareholders. That is a closed loop. Shareholders who are happy will willingly pay directors more, in order to buy good quality directors who will then generate a good result. Directors who are open and transparent and who provide a good result to the shareholders produce wealth.

ACTING CHAIR—A virtuous cycle.

Mr Evans—Absolutely.

ACTING CHAIR—On that basis, I thank Ms Maslen-Stannage and Mr Evans for your time this morning. Your contribution has been greatly appreciated. Committees such as this could not do their work effectively without the assistance of firms such as Freehills. I thank you for your time here this morning.

[12.01 p.m.]

HANCOCK, Associate Professor Phil, Member, Legislation Committee, Accounting Association of Australia and New Zealand

ACTING CHAIR—I welcome you to the hearing this morning. The committee is conducting its hearings in public and we are taking evidence on matters arising from the Company Law Review Act 1998. If there are any matters that you wish to discuss with the committee in camera, we will consider such a request. I need to remind you for the record that the giving of false or misleading evidence may constitute a contempt of the parliament. We have your submission. Are there any corrections or alterations you wish to make to that before we ask you to make an opening statement?

Prof. Hancock—No.

ACTING CHAIR—Would you like to make a general statement about it or do you wish to raise the matters of significance? We do have a bit of a time constraint, having run over time with earlier witnesses.

Prof. Hancock—No. The association responded to a letter directed to Senator Chapman. The points we raised were responding to some of the concerns that were identified in respect of the Company Law Review Act. I am quite happy to take any questions on the comments we have made in that submission.

Senator MURRAY—Your submission is very helpful—short, precise and to the point. Professor, I am not familiar with your association. How many members do you have, roughly speaking?

Prof. Hancock—We have about 600 members, most of whom are members of the universities in New Zealand and Australia teaching accounting, finance and business related subjects. We also have members from practices as well.

Senator MURRAY—With all those members, how do you consult to get to a view? Do you have a subcommittee that comes to a view or do you disseminate the issues and wait for feedback?

Prof. Hancock—That is a good question. Given the need to respond in a timely fashion, we do not disseminate widely. We do have an executive committee which consists of nine individuals essentially from Australia and New Zealand. We also have a special interest group. We call ourselves the Accounting Standards Interest Group, of which I am an office bearer. We have some 50 or 60 members. Essentially, we look to the interest group to give us some reaction. Then Professor Brown—who is in the US at the moment and apologises for not being here—and I essentially coordinated and prepared the submission.

Senator MURRAY—Professor, quite often business and academic leaders and politicians like to maintain that their laws, regulations and practices should be competitive. I often think the word should be ‘comparative’ so that people who operate in different legal jurisdictions and different countries are familiar with systems and so on. A number of the issues which

have been raised in this committee are consistent with some international trends—for instance, the earlier discussion on remuneration. As you know, public disclosure of remuneration is quite common in a number of OECD countries and other countries as well. There is the question of disclosing matters for publicly listed companies which they already have to disclose in other primary exchanges. There is the question of the 28-day rule, which as you know is established elsewhere and so on. Before we get into the detail of this, how important do you think it is for us to override parochial local objections, such as to the 28-day rule, in the interests of having conformity and comparability with our international trading partners and the common international countries with which we interact?

Prof. Hancock—That is a good question. Certainly in relation to the financial reporting standards or accounting standards we have also made a submission on that in terms of our international harmonisation moves. I have been quite closely involved in that, having worked in London in that area as well as working in Melbourne in the setting of accounting standards in Australia. So the issue is similar in a sense where we are moving supposedly with accounting standards to harmonise ourselves with what are called international accounting standards. The issue there is that we are, in a sense, aligning ourselves to a set of standards at a time when other jurisdictions are not necessarily moving in that direction.

Part of my response would be: how do we decide what is the appropriate benchmark, whatever we are looking at, which we should move ourselves towards? In the accounting standards area, the jurisdiction in the US is generally known as having the most rigorous set of reporting standards. Certainly, if the US exchanges do not endorse the use of international accounting standards then that as a benchmark will be significantly watered down from many Australian corporates' point of view because obviously listing in the US is one of the main objectives because of its enormous source of capital. So the benchmark of international accounting standards, albeit a fairly good one to aim at, becomes an inappropriate benchmark if the US capital market does not accept it. I endorse the objective of looking at and having comparability, but the issue is where you have different jurisdictions which are doing slightly different things. What we align ourselves with is always the issue.

Senator MURRAY—And what we are trying to achieve.

Prof. Hancock—Yes.

Senator MURRAY—I would hate to class myself as an expert on US law, but I have read quite generally and reasonably widely on the subject. I get the impression that America is an exceptionally strongly regulated market with very strong rules of disclosure, much more in fact than we had in either the old law or the new law. Yet it is recognised internationally as being the epitome of effective capitalism, if you like—very dynamic, very innovative, very effective, very efficient. Why do you think our business and professional sectors by and large take a view of the undesirability of following the American model?

Prof. Hancock—That is a good question. I am not entirely sure what the answer is. If I look to European countries, for instance, they are certainly very strongly opposed to any moves towards a US type system—again, very strongly because of the nationalistic feeling that the Europeans can achieve desirable results without having to look to the US for direction all the time. It is a view which does embrace nationalistic feelings and so on. At

least that is the way I see it. Again, in the setting of the accounting standards, the Europeans are not keen to look at the US accounting standards as the model and are very strongly pushing the development of a new set of accounting standards which are being produced by the International Accounting Standards Committee.

Senator MURRAY—But the core argument of those opposing the sorts of things being considered by this committee is that the result of accepting environmental disclosure, disclosure of material legal matters, the 28-day rule or the remuneration disclosure all gums up and unnecessarily regulates and rigidifies our system. Yet those sorts of things go on in America and do the very opposite. They in fact contribute towards a very dynamic market. In your opinion, are we merely seeing the exercise of self-interest and a non-transparent mentality and culture in this country which should be resisted, or do you think that the people opposing these sorts of things are merely properly outlining arguments which should be heeded?

Prof. Hancock—Inevitably, self-interest will come into play in whatever jurisdiction you are looking at. It is an inevitable consequence of most people's point of view in many ways. Self-interest will, in part, contribute to the way they interpret and the views they express. It is not my view that there is this deliberate preference for a less transparent system. I would certainly hate to think that was the case. In the area of financial reporting, we certainly have a very well-developed approach to establishing accounting standards. We are quite well respected around the world in terms of our status as a standard setter, together with the US, the UK and Canada.

As a country, we have supported the development of accounting standards which bring about certain disclosures and transparency, the related parties being an obvious example of that. That standard has been revised several times as new transactions or situations arise which were seemingly not covered by the existing standard. With this need for disclosing information—particularly about related parties which, in terms of public entities, are the sorts of transactions which cause shareholders a lot of concern—we have certainly been at the forefront in developing requirements for disclosure, which makes it more transparent with what entities are doing with related parties. I do not think there is that deliberate point of view.

Senator MURRAY—This is my last question.

ACTING CHAIR—Can I ask you to bring it down to the specifics.

Senator MURRAY—I have deliberately kept it away from the specific issues because your submission very aptly deals with that. I sense that, in those opposing many of these things, there is an underpinning of—and I hate to use the word 'ideological' as it is the wrong word—resistance to this which arises from the prevailing culture. Essentially, there are issues of corporate governance, improved accountability, election and re-election of directors, the limited pool of talent which is there—despite some astonishingly good directors in many companies—and the lack of gender and racial change in those boards. There are lots of issues about preserving what is and resistance to changing it. That is what I am searching for underneath. I think the provocateurs in this—the Australian Shareholders Association, the international governance people and some good academic thinkers—are

more up against culture than the actual issue. That is why I have pursued this line with you. Your organisation seems to me to have an international analytical perspective which is a little different.

To bring that general comment down to a specific question, do you think it is the job of parliament and the regulators to lead in the issues of imposing or initiating better corporate governance and better election procedures in the face of a resistant directorial class, or do you think they should merely leave it alone and let companies and their constitutions and shareholders over time address these issues themselves? That is the essential argument that has been put to us: we should stay out of it, and they should get into it.

ACTING CHAIR—Regulation versus self-regulation.

Prof. Hancock—I talk to my students about this for a couple of weeks in one of our courses, so it is, again, a very leading question. My view would indicate—as I am sure would the views of some of my colleagues—that parliament has a difficult job. I do not believe it is parliament's role to lead and to regulate to the point where it creates so much regulation and red tape that it hampers the operations of organisations, creativity and so on. But at the same time, there are times when the market does not self-regulate to the point where it does need some direction, some legislative requirements, to assist in its running in an efficient and appropriate way. My answer is going to be one which inevitably would suggest that parliament has a role to play. I believe the markets are normally fairly able to regulate and operate in a manner that does not require parliament to get involved in a detailed fashion, but there is a role to play. I am not going to give you an answer which is going to help you in a great way.

ACTING CHAIR—Could I take you to a specific matter along the lines of what we are talking about—that is, your first issue about listed companies disclosing information required by foreign exchanges. What do you say to the proposition that this sort of provision is contrary to the overall concept of simplification—that objective of the company law review—and that it could be counterproductive in that financial information disclosed to foreign exchanges might well be complying with different accounting standards and, therefore, its disclosure in Australia could be confusing to investors or even misleading?

Prof. Hancock—I would not hold that point of view simply because I believe markets are fairly efficient and fairly well informed. The reaction and the pricing in markets are as a result of those who are well informed and who are able to discern and distinguish between information that is arrived at using different reporting rules, for example. It already happens in Australia in respect of many companies that disclose supplementary information—the banks, for instance, which list in the US. The information that they are required to disclose in the US jurisdiction, for instance, is there as supplementary disclosure. Clearly, there is a difference between the results arrived at using the US reporting rules and those arrived at using Australian reporting rules. If you were looking at what we might call an average shareholder who tries to digest that information, they would probably be confused, but I suspect the average shareholder does not try to digest that information. It is the analysts who are informed who would be able to use that information if they thought it was appropriate in forming a decision about the value of that particular enterprise.

ACTING CHAIR—Do you have any concern about there being unnecessary paperwork for little tangible benefit?

Prof. Hancock—That is certainly a concern. That is one of the reasons why, in respect of accounting reporting rules, there are a lot of benefits from having a 'global'—for want of a better name—set of accounting standards and thus eliminating this need to have to adopt different reporting rules for different jurisdictions. The supplemental disclosures that are currently there would disappear.

ACTING CHAIR—Has the time then arrived for this requirement? Or are we ahead of ourselves, in the sense that there is not yet a global market in terms of the accounting standards and the financial disclosure requirements around the world?

Prof. Hancock—It is a good question. With respect to accounting standards, we were jumping out in front and the other major capital markets around the world were not following in the same way. The UK, Canada and the United States were not moving towards adopting international standards. The desirability of moving to a set of common rules is still there but, if the other major players are not moving to that same set of rules, then what do we have to gain? In fact, we may well lose by seemingly trying to lead the pack. That is the criticism in terms of that area of the rules. We argued very strongly in opposing the use of international accounting standards too soon. I guess that would apply in the same way to any set of regulations.

ACTING CHAIR—I just wanted you to elaborate on the breaches of Corporations Law or trade practices law. You possibly heard the evidence being given by the previous witnesses from Freehill in relation to that matter. Did you have anything to add to that? Your submission suggests that this requirement already comes within the existing disclosure regime, in so far as it is a contingent event. Is there anything further you wish to say in relation to that?

Prof. Hancock—No, not really, other than, again, the accounting standards are moving to adopt a new international standard on provisions and contingent items which, again, will broaden the coverage of contingent events. That is currently international standard No. 37, probably to be adopted soon in this jurisdiction.

Senator MURRAY—In regard to item 4, that suggestion for amendment was a very intelligent suggestion, if I may say so. Much of the argument put to us about various clauses is that they should be wiped out. I think most of the argument should really relate to amendment, not otherwise. That suggestion of yours is right, because ultimately the requirement that parliament has laid down relates to financial risk. The return and an assessment of risk is what the shareholder is in there for in the end. Thank you for that. I had that view.

Your remuneration comment is in the same arena of trying to make the intention work better. You might have heard, though, the previous witnesses put quite a lot of stress on the undesirability of it. The committee would be interested in your feelings about the effectiveness and the efficacy of disclosure of remuneration and packages for the top five.

Prof. Hancock—I listened to both arguments. Clearly there are points on both sides of the ledger. The ability to assess the appropriate rewards for senior executives clearly should be related to performance. Whether you can do that when it is in a banding system is again a debatable point. I share the concerns about individuals and their specific packages being disclosed and the potential risks that could bring with it. But clearly it certainly enables better assessment of the appropriateness of the level of remuneration that is being paid to top executives.

In the latest issue of our *Australian CPA* magazine, Jan McCahey, the chief accountant of ACIC, made the comment about the lack of disclosure by companies of options and the value of options. Clearly there are values ascribed to options. Even if it is not in the money at the present time, there is still a value to a share option. The lack of disclosure about the fair values of these financial instruments is a concern that she raised. It is one that certainly can be overcome. There are ways of valuing options—even if there is not a secondary market available—which are readily known and can certainly be used. So the lack of disclosure about at least the value of these items is certainly disappointing.

Senator MURRAY—It is certainly no harder to value options than it is to value intangible assets.

Prof. Hancock—It might even be easier.

Senator MURRAY—I would think it is a lot easier.

ACTING CHAIR—Is there any concluding statement you would like to make, Professor?

Prof. Hancock—The latest magazine does also have some information about audit committees and the result of a survey in 1996 about the lack of disclosure in respect of audit committees. I just point that out for your information.

ACTING CHAIR—It might be something that we should have a look at. Would it be possible for you to provide us with a copy of that article?

Prof. Hancock—Yes, most definitely.

ACTING CHAIR—We can arrange that after the hearing. Thank you very much for your time in appearing before us this morning and also for the time of your association in preparing a submission. We certainly appreciate that input. I am sorry for running a little over time this morning. Thank you.

Prof. Hancock—Thank you.

[12.32 p.m.]

JOOSTE, Mr Peter, QC (Private capacity)

ACTING CHAIR—Welcome, Mr Jooste. This committee prefers to conduct its hearings in public. However, if there are any matters that you wish to discuss with us in camera, we would obviously consider such a request. It is necessary for me to remind you that the giving of false or misleading evidence before a committee may constitute a contempt of the parliament. Do you have any comments to make on the capacity in which you appear?

Mr Jooste—Thank you very much indeed for this opportunity. I am a senior counsel practising at Wickham Chambers as a barrister. It is really in that capacity that I appear, not in any formal capacity representing an association, although I do sit on the Law Society corporations committee. I understand that there will be a separate representation in that regard, so I will not cover those points.

ACTING CHAIR—Thank you. We do have a submission from you, for which we thank you. Is there any addition, alteration or amendment you would wish to make to that submission?

Mr Jooste—Certain of the submissions there may require a little adjustment, I think, on reflection, it was a very cryptic submission. I also took the opportunity of bringing to the joint parliamentary committee's attention a totally different matter regarding the Wakim decision, and I wondered whether a copy of that had been circulated.

ACTING CHAIR—Yes, it has. Could we deal with that in a moment? If we perhaps deal with the submission on the matters arising from the Company Law Review Act first, and then we can turn to your paper.

Mr Jooste—Certainly. There was one other matter dealing with section 414 which is outside the submission but within the general purview of the Corporations Law review, and I notice that some of the other submissions have strayed into slightly extraneous areas when they have warranted it. That might be a matter which we could raise again as a small subsidiary matter on the outside of the main body of submissions.

ACTING CHAIR—Turning to the point in your submission about the proportional voting system, are you suggesting that you are not against it, per se; you just feel that the proposal requires a greater degree of investigation and public consultation?

Mr Jooste—Yes, every one of these submissions obviously has a balance. I think at this point in time the balance is for a system that is very clear, well understood and known internationally. I think that it is clearly understood that our current system of one share, one vote accords with international practices and, in a sense, is what drives the market on a day-to-day basis. So that, whilst I have a great deal of sympathy for minority shareholders in being able to gain representation and a voice in the governance of the company, it might well be at the expense of a system that is recognised internationally that one could achieve that—a fairly complicated system of voting for a quota or at least a number of seats that

would have to become available in each year and, as well, possibly shorten the period of tenure of each of the directors, with probable consequences on short-term focus.

ACTING CHAIR—I do not have any further questions in relation to breaches of the Corporations Law. Senator Murray, is there anything you want to raise on that matter?

Senator MURRAY—I will come back to the voting one. Are you happy to do it item by item?

ACTING CHAIR—I am happy to do it item by item; I think it will be less confusing.

Senator MURRAY—Mr Jooste, the proportional voting proposal—as put to the parliament, rejected by the parliament and then referred to this committee—was not to impose proportional voting on listed companies but to ask listed companies to put the proposition to their shareholders at their next meeting or at a time appropriate to see whether shareholders would like a better method of minorities in particular being represented. I think there are three occasions on which we should look at dissatisfaction with the existing system whereby boards are elected.

One is where a shareholder or a few shareholders control over 50 per cent of the company but control effectively 100 per cent of the board. That is a classic minorities position. The second is where the majority is disadvantaged, and that is where a single shareholder may control, say, 30 per cent. I have used the typical example of media companies, which are constrained in terms of shareholding but effectively control the board, so 70 per cent can, in theory, lose out. The third is where the shareholding is widely dispersed but a board has somehow arisen which has captured the positions and thereafter just perpetuated, and minorities feel incapable of changing the nature of the board without legal challenge and a huge fracture going on.

If we accept that there is unhappiness and that the proportional voting system is not achieving the result we want, we then have to look at solutions. One of the solutions put up is that preferential voting is adopted, so people actually have to rank directors in order of preference, and you then get a full or an optional preferential system. A third view was put today by Mr Factor from the Curtin University, who believed that far better expression of the provisions of the constitution, far better procedures in presenting election and re-election, would in fact make it a more transparent and better exercise. I know that you have got a great deal of experience in these areas. Given that there is a concern, have you thought through some possible solutions, or do you think it is very difficult to arrive at any?

Mr Jooste—I have a feeling that companies like the recent Allgas company—I think I have got the name right—where there was a Queensland restriction of 12.5 per cent as a maximum percentage being held by a particular shareholder, or companies that have those constraints, may well benefit from some type of proportional voting system. But I think that the real answer is, as you say, to put it to the shareholders and let the shareholders decide, albeit in a majority fashion. But that is not so anomalous, because every other decision that they are going to make is, in fact, under that system, a majority vote. So if a company, or at least a 75 per cent vote for a change in the constitution, wishes to bring that in, then its

shareholders will either suffer the consequences of how the market views their particular structures or not.

Senator MURRAY—Mr Jooste, I would expect you, over probably decades of practising commercial law, to have actually written many constitutions—memorandums, as they used to be, and articles. Tell me, from the point of view of legal practitioners, does the way in which voting should be exercised exercise your minds, or would a lawyer asked to devise a constitution for a new company to become a listed company follow a standard format? I ask you that question because writers like Mr Shann-Turnbull—it might be Dr Shann-Turnbull—provoke these ideas and say that they are established in America and so on; but it is possible that those tasked with constructing constitutions simply are not recognising it as a problem and, therefore, are just going along in the way it always was done.

Mr Jooste—Yes. There was a time, and there are times during the ebb and flow of corporate law, where people are merely following precedence. But I think that we are in a period, at this point in time, where far closer attention is being given to the structuring of constitutions and how corporate governance fits into that and how your elected representatives actually take your company forward or not. As the competition increases and as the liability of getting things wrong increases, so the advisers are being brought into line to ensure that their drafting of those constitutions fits in with what is acceptable—ultimately to the market, in the case of listed companies. So I do not think that there would be a resistance to the idea, as such; but there might be a resistance to those self-evident things that come with the package, as it were. There might be a fear of short-term focus in order to adjust to that type of system—and, once again, it could be a balance of whether proportional representation is really what the body of shareholders require or whether they prefer a system where the directors represent the largest groups.

Senator MURRAY—With regard to election systems—and I am deliberately broadening it beyond proportional to preferential—and also to better communication, is it your experience that established companies sometimes, seldom or only as an exception, come to their specialist advisers such as yourself and say, 'We think our constitution needs a review. Tell us where it is poor in terms of governance or process or those sorts of things'? Or, once the company is established, do they simply leave it aside and forget about that area of review except when a problem arises because of changes in laws?

Mr Jooste—No. In the listed companies field, it is a question of almost constant review and also compliance with the listing rules—which is a great driver to the actual format of a constitution.

ACTING CHAIR—As listing rules change, the companies would be going back to their constitution to see the impact or whether or not it is able to cope in its format with that change.

Mr Jooste—Yes. So it really brings about a situation where the listing rules are the appropriate place.

Senator MURRAY—Behind my question is that it may be appropriate, rather than the legislature to change the law, to encourage ASIC and in fact the ASX to encourage

practitioners such as yourselves to review constitutions when you are asked to do so, with some additional perspectives in mind which may not be normal if the normal reaction is just changes in law or changes in disclosure rules. The pressure on us is primarily from groups driving for better governance, greater accountability and better, in whatever frame you want to put it, director selection. Those issues are difficult to deal with legislatively.

Mr Jooste—I think you have hit the point there. I believe that the correct mechanism for that type of reform, or at least new, innovative thinking, is in fact in the ASX listing rules. That comes about because, for instance, you get articles that can accommodate all the listing rules by saying that the constitution of this company is governed, in so far as a discrepancy between it and the listing rules is concerned, in preference of the listing rules. So you have almost got an omnibus rolling system to bring you into line with what the market rules are. It would be within that forum, with its own constituencies and stakeholders and pressures brought to bear, that the listing rules could provide the mechanism for what the black letter law would be cumbersome and inflexible to achieve.

ACTING CHAIR—The next issue I was going to look at was the corporate governance and audit committee. Do you have any question on the constitution of the 28 days, Senator Murray?

Senator MURRAY—The problem we face is that there are good arguments on both sides. The 28-day rule was essentially driven by those who want us to have a comparative regime with foreign jurisdictions and give sufficient time to meet those demands. People tend to fall one way or the other. In the end we are going to have to decide.

Mr Jooste—Yes. My clear preference would be to leave the system on a 21-day clear basis because of the effective lengthening of the procedure anyway which causes costs inefficiency and probably out-of-date information to slip via the 28-day rule. Clearly I have got no argument whatsoever with the situation that shareholders should have sufficient time within which to evaluate information, but I do not think that there is sufficient evidence, or a clear, clarion shout, from that set of stakeholders for a longer time period. I might be wrong in that, but anecdotally there does not seem to be a huge build-up towards that. There seem to be more cries of, 'It is too long and too inefficient.'

ACTING CHAIR—In terms of the greater efficiencies that we expect in almost every other area of our lives, it would be fair to assume that greater efficiencies in the dissemination of information would also go against the extension to 28 days from 21 days.

Mr Jooste—Yes, I think so. I think that you have quite a large body of judicial comment based, for instance, on the NRMA case which says that directors have to be selective in the information that they produce and that they do not have to produce an encyclopedia every time they do something. In fact, it would be misleading in some instances to do so. You are rather sitting on the horns of a dilemma as a director, but certainly the balance seems to be towards ensuring that your information is not so suffuse as to be misleading, so there is a trend towards shortening it, making it more cryptic and presenting it in a better fashion. That should assist in the time period on meetings anyway.

ACTING CHAIR—In relation to the corporate governance and audit committee issue, you have opposed the proposal. Would you elaborate on that?

Mr Jooste—Yes, certainly.

ACTING CHAIR—Your submission just had two points in relation to that. You say it is best served, given the demands of shareholders, by representation on a single board, augmented as needed.

Mr Jooste—Let me say at the outset that I think an audit committee serves a very good function. The audit committee can be of tremendous benefit in providing a platform within which to review holistically what is being presented insofar as information and all sorts of check lists are concerned. It is with a separate governance board—rather than a separate governance committee—that my thoughts would have been, in that that adoption of a model would be quite revolutionary in a way within, let us say, the old Commonwealth countries which shared the 1928 companies act. I think that it would introduce systems which would be less efficient in the final analysis, more costly and not in the spirit of simplification because there would be areas there for tension in jurisdiction between those two boards.

Senator MURRAY—Once again we are dealing with an expressed problem and we are searching for solutions. Essentially, the expressed problem is the conflict of interest situation. A board at present determines its own remuneration in the package sense and, even where the board asks the shareholders for their support, it goes through, generally speaking, with the board's unanimous approval and support.

Another major area of conflict of interest is the board appointing its own auditors and valuers. Yet the auditors and valuers, who are then dependent on that board for the continuing contract and for the amount of money that they will be paid, are obliged to determine the value of assets and options and tend to the balance sheets—those discretionary elements which could influence the way in which shareholders and the market view the company.

The concept of the corporate governance board was to deal with all issues in which there would be a conflict of interest situation—another one, I would add, is the related party transactions issue, which came up in the Coles Myer board problem—but audit committees or committees which are subsets of the main board do not resolve that issue because they are, in the end, part of the same governing mechanism. With the corporate governance board idea—or a company senate, as it is known in America and in some companies in Australia—the intention is that those directors have a very limited brief to cover those areas and the main board gets on with the rest. Given your rejection of that model, we are still left with a problem: how do, should or can companies deal with those issues?

To give you an example, one method in which the Insolvency Practitioners Association have suggested that the audit matter be dealt with is simply that ASIC would have a panel of auditors available and they would give the company the auditor they chose from the panel—so take it out of the board's hands and put it into a third party's hands. Given that there is a problem, how should the parliament and the regulators find a solution? What should they do?

Mr Jooste—You have mentioned that there is a problem, and I think that we do not want to focus the solution to that problem on yet another layer of expense. Whilst there is a clear model from America possibly, their dynamics would have to be carefully looked at in order to ensure that it was not a useless exercise in merely replicating that system. I really need to explain myself a little more on that, because I believe that the solution is really not in trying to produce a bifurcation of a director's existing duty—namely, to say, 'You need to relax somewhat because, in corporate governance aspects, we will relieve you of your duty and have a "truly independent" separate board determine that matter'—but to leave alone the existing fiduciary position of a director, which, if properly understood, ensures that his shifting of hats is not merely token—namely, his liabilities are extreme at the top end of the scale.

Certainly, the system of enforcement and the court decisions in that regard would bolster that to the extreme. In other words, no director today could be forgiven or would be allowed to be forgiven for either turning a blind eye or not making himself well aware where he has a conflict. Certainly within the last, say, seven years, that realisation as it were has really been focused upon and has becomes starkly and efficiently exposed to all boards. So it is a slightly different climate to what pervaded, say, a decade ago.

Senator MURRAY—Excuse my ignorance on this, but does the ASX, for instance, have a format whereby it provides listed companies with a standard method of how they should deal with conflicts of interest, with related transactions, with determining their own remunerations and making recommendations to shareholders, and how they should appoint auditors, valuers and other professionals whose appointment can result in a perspective of the company? Do they get involved in that, or not? My understanding is that they do not, that at present it depends on the board and that, therefore, the worst boards do it badly.

Mr Jooste—Certainly in the area of corporate governance statements the ASX has rules that spring to mind immediately. But, within the ASIC policy statements and practice notes there would be a body of principles which would govern the appointment of experts or how independence is gained. And there would be a body of case law that would highlight conflict of interest situations and how to deal with them. Certainly, examples have been given within that sphere of how this should be dealt with.

Conflict of interest is always a difficult area but, as we know, the Company Law Reform Program has in fact bolstered minority shareholders' rights by the imminent disappearance of the rule in Foss and Harbottle, giving shareholders direct access via the representative or derivative action to ensure that situations like that are better enforced and well policed. So the shareholders themselves have the mechanism to ensure that situation.

I would have thought that that would have been the preferable route at this stage, rather than adding a layer of a corporate governance board. Certainly on the American model that might be more split between a really, truly high-powered and large executive team and a non-executive senate type review. Larger companies, I think, attempt to achieve that already and, obviously, through the corporate governance reports—mainly on the UK model, the Cadbury committee and the like—have given that sort of indication.

Senator MURRAY—You are referring to a non-executive committee?

Mr Jooste—Yes. Although the audit committee is called the 'audit' committee, I think it should not be seen as checking again the financial figures but as a broader concept of a checklist approach that could encompass some of those aspects of being able to—

Senator MURRAY—Effectively an auditing governance committee.

Mr Jooste—Yes, auditing the governance as well. 'Audit' is perhaps a slightly misleading word in that it connotes looking at financials again.

Senator MURRAY—It is a technical approach, as opposed to an ethical approach.

Mr Jooste—Yes.

ACTING CHAIR—In relation to the issue of remuneration, do you draw a distinction between directors and executive officers at any point in your thinking?

Mr Jooste—Yes, certainly. I think at the outset I mentioned that I might have an adjustment to my submission in regard to this point. I believe that there are two approaches here: the fig leaf approach, as it is called, and also what is called the jigsaw problem. I think I need to elaborate on that to show exactly where my submission is coming from. I think that the world trend clearly—through the Greenbury committee and the way the American SEC requirements have gone—is to total transparency and doing away with the fig leaf and, in fact, it has produced a situation where, instead of finding information dotted all over the spectrum in a number of places, they have gathered that together out of the jigsaw and put it in a succinct statement so that it can be recognised and evaluated by shareholders.

Rather than dismissing the situation and really adopting the fig leaf approach and saying that privacy overrides what we are trying to achieve here, I think that a balanced approach is probably one that should be looked at—that is, to really focus on rectifying the jigsaw side of things; in other words, to ensure via legislation, or at least through the ASX listing rules or possibly a flexible model like that, that there is correlation of all the information leading to remuneration put forward in one remuneration statement. In other words, that it can be seen. It is not in the notes to the accounts, via the related party provisions or via an accounting standard or the like, thus producing the information in a number of places, but that it be channelled into one place. That would make evaluation much easier.

You are then left with the situation of whether you still adopt a fig leaf approach in the face of what is clearly—overseas, at least—a situation of far greater transparency and disclosure. I think then, at that point, it is almost a spin of a coin situation as to what the market really requires. If the market is demanding that everybody know exactly what executives are earning and what the total remuneration or individual remuneration concerned is, then a listing rule situation could develop. But it would be developing within a framework that you had been able to set which would have clarified the disclosure vehicles—namely, by bringing it all into one remuneration statement—but at this stage perhaps Australia might not be ready to discard the fig leaf so quickly.

Senator MURRAY—That seems a very sensible response to me.

ACTING CHAIR—Would you like to summarise the position taken with your second submission? I have not had the opportunity to read it in detail, but perhaps you could outline the purpose of the paper and the conclusion that you have reached.

Mr Jooste—Yes. However, before doing so, I would note again section 414 of the Corporations Law as it is now. It is very easy to say and it slips off the tongue, but it is really all to do with compulsory acquisition. As everyone has recognised now, the clear proposals have brought in a totally new mechanism whereby 100 per cent control can be achieved once total overwhelming economic ownership has been established. I note this only because it seems that the CASAC—and by that I mean the Companies and Securities Advisory Committee—recommended the repeal of section 414 because it sat as a lower standard of achieving compulsory acquisition when a totally new sweeping regime was being put in place. I think that is all I need say there. I just note that section 414 will look out of place if the new proposals are brought in.

But of far more importance for Australia as a whole and in order to produce its economic efficiencies, its simplification of the law and to bolster its financial position on a global scale—which, as I understand it, is the thrust of the role for Australia of the Hon. Joe Hockey MP—and bringing that about is this, as it were, dead weight of the Wakim decision. This has caused a great deal of consternation amongst practitioners, academics and the like; namely, that cross-vesting legislation has put the national scheme back into the position in which it was in 1991—that is, without the ability of the Federal Court to exercise state jurisdiction. That is it in a nutshell.

I have deliberately put forward a proposal called ‘corporate conjunctions’ to attempt to widen the debate from the customary constitutional positions that spring to mind immediately. I have done so in a very self-acknowledged simplistic way because I believe that, at this point in time, if it holds enough intellectual integrity, it will survive; if it does not, it will have been worth the exercise in attempting to find a solution well based on High Court authorities that is inexpensive and that utilises two principal important platforms existing within Australia already. They are the Corporations Law as it stands, which is acknowledged as a very complicated piece of legislation that has taken a great deal of time and effort to put in place; and the current system of courts as they existed prior to Wakim—in other words, not to change the dynamics in any way but to utilise those existing platforms. Probably the most important platform of all is made up of the dynamics of state and federal jealousies in the jurisdiction of incorporation; in other words, to retain the state position in so far as their corporations are concerned but to spread the dynamics where the ACT is concerned.

All the paper is saying is that Wakim decided two things: one, a major situation in so far as the illegality of state vesting in federal courts is concerned on a jurisdictional basis; but also that, in so far as the ACT was concerned, the Federal Court did indeed have power because of the territory or section 122 power. It seems that to waste that decision would be a pity because, utilising a model of multi-incorporation or dual incorporation, you could achieve basically the referral of state power to the Commonwealth.

ACTING CHAIR—In other words, by changing the concept of incorporation; if you incorporate in a state, it is taken as incorporation across the nation.

Mr Jooste—It is precisely that, either within the territory or on a multi-state basis. It is as simple as that.

Senator CONROY—Would that require legislation in state parliaments to amend their incorporation?

Mr Jooste—I believe it certainly would require the states to be involved just as they were in a cooperative manner with the Commonwealth.

Senator MURRAY—But it is almost a one-liner, isn't it? The state legislation would simply say that any registration by a corporation in terms of the federal Corporations Law is permitted by the state and automatically transferred. You do not need to replicate the Corporations Law; you would just find an access regime. Isn't that so?

Mr Jooste—It is virtually the same as the applied legislation as it exists at present. But it merely replicates it back into a jurisdiction which has the full power of the federal Constitution behind it.

ACTING CHAIR—I wonder how the states would react? I am just thinking that the place of incorporation and home exchanges and the like are matters of great interest and concern to the states.

Mr Jooste—Yes, I think they are. From that point of view though, they would still retain, let's say, their primary incorporation situation, even though a duality was involved or was to become involved in it. So you would have that; obviously it would not be a detraction from the states or their power in any way.

ACTING CHAIR—It is certainly an interesting matter for us to take on board. It is not, as you say, strictly within the terms of reference, but thank you for providing to us a copy of your paper and the idea of corporate conjunctions.

Mr Jooste—It is for you, Madam Chair, and the committee to do with as you see fit.

Senator CONROY—The committee at its last meeting decided to get a briefing from among the secretariat. Perhaps we may be having some separate distinct hearings or discussions or a roundtable discussion of some sort to see what ideas—of which this certainly would seem to be one—would be worth looking at. So we may come back to you and harass you over it a bit more.

Mr Jooste—I hope you do.

ACTING CHAIR—Mr Jooste, thank you for your time this afternoon and for your submissions to the committee. They are much appreciated and they will assist us in preparing our report. Thank you very much for your attendance.

Mr Jooste—Thank you very much indeed.

[1.17 p.m.]

YOUNG, Mr Grahame, Member, Law Society of Western Australia

ACTING CHAIR—Welcome. Mr Young, today we are inquiring into and taking evidence on certain matters arising from the Company Law Review Act 1998. We conduct our hearings in public but, if there are any matters that you wish to discuss with the committee in camera—I am not sure that there will be, but if at any point there are—we would consider such a request. I am also obliged to remind you that the giving of false or misleading evidence may constitute a contempt of the parliament. I understand that you are representing the Law Society of Western Australia today.

Mr Young—Madam Chair, I am to a degree representing the Law Society in respect of the submission made by the Law Society. At the time the letter was written, I was convenor of the Commercial Law Committee and principally responsible for the draft. The Law Society has permitted me to make some private comment on some of the other matters. I will make that comment not only as a solicitor of about 30 years standing, but also as a practising company director and, I might add, chairman of a number of audit committees on those companies.

ACTING CHAIR—The Law Society, whilst commenting that they had insufficient time to make a submission, has confined their submission to the 28-day, 21-day issue. Would you like to deal with that first. Perhaps we can then turn to any matters that you wish to raise.

Mr Young—Yes. In respect of the Law Society's comments on the commentary process and the input process, as you would realise, the law societies and kindred bodies rely very much on voluntary help. It is done usually by quite busy people who relish the opportunity to comment. But, as it appeared then, as it may not appear now with GST amendments and constitutional matters, the political process appears to have overtaken the consultation process. The Law Society's concern was and is simply that care needs to be taken to ensure that the quality input from the volunteers continues.

ACTING CHAIR—Because it is almost 12 months since the date of the submission. There is not always adequate coordination in terms of the parliamentary process and the taking of submissions; I appreciate that.

Mr Young—On the 21-day, 28-day matter, my only comment is that, over the period, the competitive disadvantage of listed companies that need to go to a general meeting, particularly where it is an extraordinary general meeting, has become more apparent. The length of time involved in settling and having approved the materials for the general meeting through the ASX—having them printed, distributed, then waiting the 28 days and so on—means that a listed company finds that in a volatile environment people are unwilling to say, 'Well, we'll happily wait six or seven weeks on the assumption that things will remain the same.' They do not.

Admittedly, changing from 28 days to 21 days takes out only one week. The practicality is that you say, 'It is about a month before we can get this meeting on,' rather than saying, 'It's a month and a half or more.' It is a question of finding a balance. Whilst I would say

that 14 days is too short at present, that may not be—using electronic communications—so in the future. Twenty-eight days is simply too long.

Senator MURRAY—As far as 'solution orientated' is concerned, I do not think it was ever the intention of parliament that it should have been longer than 28 days. But what people such as you are saying—and as somebody indicated in Melbourne at the last hearing—is that when it was 21 days, it was effectively 25 or 26. Will it fix the problem if the legislation were to say 'not more than 28 days and not less than 21'? In other words, by enforcing a waiting period of three weeks effectively you have to add the extra days anyway.

Mr Young—I am not certain on that because there are times when matters are necessarily time driven. An annual general meeting is such a case where to get your accounts out within the appropriate periods, to get them within the annual report, to distribute the annual report and then to find a day when the venues are available, sometimes the annual report with notice of meeting will go out more than 28 days beforehand.

Senator MURRAY—But the assumption in the law at present is that the 28 days operates as a statutory minimum.

Mr Young—Yes.

Senator MURRAY—So effectively the time is longer. You could indicate that it was a maximum but you would still have to establish a statutory minimum. If you did, you might in fact get over that problem.

Mr Young—It is the extraneous things—the need on many occasions to submit to the ASX and, for some related party matters, to ASIC. The postal thing can be got over—by that I mean the constitution—to a degree by some deeming, and that does not seem to have been challenged. As always, it is just a matter of trying to obtain the best balance, and I think that is probably best done by reverting to the 21 days for all forms of resolution.

ACTING CHAIR—Not more than 21 days or at least 21 days?

Mr Young—At least 21 days.

Senator CONROY—I have some general comments that I would like to make about your submission but I will stick to this for the moment. Earlier today—and I am not sure if you had arrived then—we were arguing about the difference between seven and eight weeks, given the ASX, ASIC, the printing, the publication, the distribution et cetera. Maybe it is six to seven rather than seven to eight.

I am trying to understand this: when you say there is a practical problem with a volatile market, what is the difference between six and seven weeks for old news, new news? There comes a point where, if the meeting is here—and my apologies to Hansard for the waving of the hands—and you are talking about when you effectively have to post it out here, you are talking about one week—seven days—in terms of the volatility of the information.

I am just surprised to see so much passion—and there has been a whole range of people who have put in submissions—on this question of a seven-day difference. If it were seven days before the actual meeting, I could understand the argument a little better. But, given that you are really talking about six to seven weeks as the only real difference or about seven to eight weeks—as some earlier witnesses have said—the argument about the sensitivity and volatility tends to lose a little bit, in my perspective, in terms of how incredibly relevant people seem to feel the passion of it is.

Mr Young—I understand that. Perhaps I can take a concrete example where there is a vending in of an asset for an issue of shares and that may require approvals for a number of reasons, and the perceived value of the asset—the perceived value of the shares—is relatively easy to hold for four to five weeks. It becomes very difficult to hold at seven to eight weeks. The more you can push it towards the four to five weeks, the more relaxed people are and the less complex the other elements of the deal become. People tend to want to put in conditions precedent or subsequent, to start developing elaborate mechanisms for adjustments and so on, whereas they say, 'We are prepared to accept a market risk for a number of weeks,' as an underwriter does on an initial public offering. The further out it gets, the more nervous they get.

Senator CONROY—If people knew it was now 28 days, would they prepare one week earlier for those sorts of events? It was 14; it has moved out by seven. Presumably, that was okay and everyone was able to factor it in. Is it a factoring in situation, where people can learn to live with it, or is there an inherent problem with the extra seven days?

Mr Young—The problem is that people looked at the previous 14 days and 21 days and worked around the 21 days with the extras. They felt it was, generally speaking, as much as it could be dragged out without the extra provisions and conditions. When it gets that bit longer, caution tends to take over and it complicates the deals, which brings me back to that point. It just becomes commercially more difficult to do the deal for the listed company as against the unlisted company.

ACTING CHAIR—Particularly if you do not have many or any foreign shareholders.

Mr Young—I recognise that 14 days was generally too short for a company with any foreign shareholders of any note. I am on the board of a company that has a very large foreign shareholding. We are very conscious of that.

Senator CONROY—I have been surprised at the resistance through the quite lengthy discussions on some of these issues. I will come back to that in a minute. There has been resistance to the introduction of things like faxes and emails. It may surprise you, but many people appeared before our committee and actually opposed this as a mandatory situation. They said it should be left up to individual companies to make the decision themselves. I agree that 14 days without any form of electronic communication is a tough task, and maybe 28 days would not be as necessary if everybody were into electronic communications. I am surprised that there has been such resistance to the inclusion of something like a fax number or perhaps an email address, which might not be addressed specifically in the amendments we moved.

Mr Young—I certainly agree that there are people who do not like fax proxies, for example. They think they provide greater opportunities for a last-minute raid and so on. I think that was just starting. Certainly taking advantage of fax proxies and so on is entirely appropriate. Some of the difficulties regarding email responses might be got around. It is really about the digital issue and authentication. Unfortunately, it is only too easy to forward a dummy email.

Senator CONROY—I accept the confidentiality problem and the security problem. The technology may need to go with that. It is a legitimate concern.

ACTING CHAIR—You indicated that you had some other areas that you wanted to raise beyond just the one that the Law Society raised.

Mr Young—There were a group of governance areas: proportionate voting; the corporate governance board; audit committees, reports to auditors; and some of the reporting issues. I would like to make some brief comment on them, but I want to leave myself open for any questioning the committee may have.

ACTING CHAIR—Would you like to summarise your position in relation to each of them. As you go through, if the senators or I have a question, we will stop you.

Senator MURRAY—Mr Young, I think you were here during the question and answer session with Mr Jooste QC. If you have any observations arising from that interchange, it would be helpful it you could give them.

Mr Young—I understand to a degree what lies behind the proportional voting matter. I believe there is a view about the tyranny of the active part of the majority. I am concerned about, if you like, going back to first principles. What is the prime duty of the directors? The prime duty of directors is to act bona fide in the interests of the company as a whole. To the extent you are seen to be aligning the directors as representatives of a portion of shareholders or, worse still, having directors beholden to a group of shareholders, you really are taking away from that message.

Although I do not think the current system is perfect by any means—I will come back to that—the sort of compromise we have at present, with the three-year rolling terms and one-third being elected each year, gives an annual accountability. It enables the board to take a long-term view as against a short-term view, which might be forced if you had annual elections. You lose accountability if you have triennial elections.

Proportional voting seems to work best when you have the whole board elected at one time. Otherwise, you get anomalies. On a seven-man board, it is very simple to see a situation where the elections might be of two, two and four. In the year when you should have three elected, there is a casual vacancy and that person needs to be re-elected. The percentages needed to elect a director change very dramatically.

On the other hand, I do not think it is appropriate that the order of election should determine the outcome. That is where there are six positions within the maximum number, for example, and eight candidacies. The six incumbents who come up first all get elected.

The chairman then declares that the next two cannot be put. I do not think that is an appropriate use of the powers.

Senator MURRAY—There was a recent example of that in a company.

Mr Young—There have been examples over the last two to three years. I think Coles was one of them. There are a number of systems that could be used to overcome that where that situation arises. Without having gone into greater depth, I would not like to advocate one. Give people the number of votes they have for the number of open candidacies, but they do not have to exercise all of them. So you can have one vote for one candidate or one vote for each of the three open candidacies. The crossing-off system could perhaps work, where you actually vote against the candidates you do not want rather than for the candidates.

ACTING CHAIR—Is it necessary to prescribe it, or would you leave it up to companies to determine how they wish their voting to proceed?

Mr Young—It would only be necessary to prescribe that the situation I described earlier should not arise. You would then leave it to the company to devise some means. If that is not working, either the ASX or its listing rules or the Corporations Law should do it. First of all, the companies within the prescribed area should be given discretion as to how to organise it.

Senator MURRAY—Mr Factor from Curtin University and Senator Conroy had an interesting exchange earlier about the factual and helpful way in which voting should go on. My understanding of their conclusion was that the ASX and ASIC need to get more involved in ensuring that the companies' election process and the paperwork enhances, explains and assists the process of voting intelligently as much as possible. He gave us two examples of BHP and Email. BHP is very flawed and Email is still flawed but better. It indicated the problem. Existing practices are very deficient in this process. Without having heard that exchange, would you support the ASX and ASIC in trying to ensure the maximum transparency, helpfulness and efficacy, if you like, of the voting system to improve existing practices?

ACTING CHAIR—We have specifically suggested that notices of meeting could be more fulsome in their explanation of how you are voting and how it is being counted.

Mr Young—Yes. I would also go a step further to say that they should at least bring in the broad statement that, under whatever process is adopted, each candidate has an equal chance of election. It is not currently the case.

Senator MURRAY—You could amend that, however. It would require the company to change its constitution, I guess. You could introduce a system of preferential voting, which all Australians are familiar with. It could be either optional, with one to four out of six, or fully, which is numbered 1 to 6.

Mr Young—There is always a difficulty in trying to find a one-size-fits-all solution for companies that range from junior Western Australian explorers to the BHPs, Telstras and so

on. A general statement requiring fairness and equality of opportunity and then leaving the company to work out a system within that is probably the best solution, until it is proven that that does not work. One then needs to get more prescriptive.

ACTING CHAIR—Are there other matters that you wish to refer to?

Mr Young—I have a quick comment about the corporate governance board. I am not sure how the hearings have gone. It seems to me that the corporate governance board is trying to revert to a model that has been recently abandoned, which is the trustee manager model. We have now gone to the single responsible entity. To put it another way, when you buy your computer hardware from one place and the software from another and something goes wrong, each blames the other. A single responsible entity, the board of directors, with very clear duties and procedures, as in the related parties issues, is the best way of going.

I heard something of the exchange between Senator Murray and Mr Jooste on the audit independence matter. That is best tackled through ensuring the independence of auditors by other means. Whether that is by decree, as the US appears to be moving towards, which is that the audit function must be separated from any consulting function, or the doling out of assignments on a rotating basis, as the court does with liquidators, my initial reaction is that the latter is not a good idea. There needs to be a degree of confidence and trust between both parties in the audit process, which may not occur so readily in that latter situation. The United States approach of trying to separate the conflict of interests that arises through the auditor doing a lot of consulting may be worth going into further.

ACTING CHAIR—That is in relation to the independent auditor. What about audit committees?

Mr Young—I am strongly in favour of audit committees. It would not concern me if they were made compulsory. I would simply say that that should not prevent the audit committee being a committee of the whole board. I am on one audit committee where that is the case. The board is a small one with only four people. Each is on the audit committee but there is a different chairman. So the chairman of the audit committee, which is me, is different from the chairman of the company. That committee functions as a full audit committee, notwithstanding the smallness of the size of the board.

Senator MURRAY—Do you consider the role of an audit committee to be, ethically, audit and governance, not just audit? Should that title really be used rather than the technical sounding title of ‘audit’?

Mr Young—Audit committees started looking to strengthen the relationship between the board and, in particular, the independent non-executive directors and the auditors and getting them more involved in the process of audit. That goes back eight to 10 years ago. In the eight to 10 years, audit committees have moved away from a simple technical monitoring committee. They are far more involved in wider matters of corporate governance.

My concern is that auditors audit the financial information and the processes. In the course of that they obviously become aware of a whole range of things, as does the audit committee. I am not sure it is appropriate for auditors to audit corporate governance.

Senator MURRAY—I asked that question because, if the impetus towards considering a corporate governance board comes about because of a genuine concern by a number of institutions and individuals about related party transactions, there could be conflicts of interest about the board determining its own remuneration. There are also dangers with boards appointing their own professional advisers—auditors and valuers—who therefore influence the nature of the performance or the perspective given to the performance of the company, with consequent effects on their options, et cetera. Those things have to be dealt with.

If somebody like you said that you would not object to the presence of an audit committee being mandated for listed companies, making it mandatory would be requiring it to make its functions mandatory and probably to deal with some of the issues I have just outlined to you. In that case, the description of the committee has to relate to what it is about. That is why audits and governance are put together. How do you react to that view?

Mr Young—I have come to the view that it is inevitable that the audit committee takes a wider role. I suppose it therefore follows that if the audit committee is mandated then, to a degree, the role is mandated and that could be a wider role than merely technical. You would have to be careful in deciding how wide that role is, otherwise I think you have some potential for taking from the board what is the board's responsibility generally within the myriad of control mechanisms that exist.

The audit committee is always a committee of the board. It only recommends to the board; it investigates on behalf of the board; it gets its hands dirty, if you like, for the board—so the board knows that somebody has done it. It is not in any way superior to the board; it is a creature of the board. The design criteria would have to be very carefully worked out.

ACTING CHAIR—Any further matters, Mr Young?

Mr Young—Just arising out of that, I noticed there was a matter of reporting matters to auditors. It is perhaps because of the experience that I have had that I wonder what the auditors then do. The auditors' powers are somewhat constrained. They are there to report on the financial statements. They also have an obligation to report to ASIC if they know of any breaches of the law, but they do not have any investigatory powers except in relation to the financial statements and reports.

I suspect the matters of improper conduct—aside from fraud which obviously will impact on the financial statements—in many cases are not going to impact on the financial statements. This morning I was trying to think of an example. The only one I could readily think of was that perhaps a director who was a substantial shareholder—acknowledging that the company needed additional funds and that the raising of additional funds might make the company more vulnerable to takeover, which might suit his personal financial needs—would skew things towards a takeover bid being made rather than an injection of finance. That would have nothing to do whatever with the financial statements, but he may well be breaching his duties to the company. That might sound a little far-fetched.

Senator MURRAY—The Accounting Association of Australia and New Zealand made the recommendation that the clause be amended when they said:

Improper conduct may well encompass activities in which the auditor has no professional interest or obligation. Thus we suggest that the words 'involving the company' be amended to read 'involving the financial affairs of the company'.

Do you think that would fix the problem?

Mr Young—It fixes one part of the problem in that then the auditors have power to do something about it. It does not fix the other part of the problem, which is—as I see it—that there is an apprehension that a director or officer may have suspicions but does nothing about it. What is one to do about that person? I am not sure if an obligation to report is appropriate, but one well might request that there be privilege for any report made, be that to ASX or ASIC.

ACTING CHAIR—There would be anyway, wouldn't there?

Mr Young—There would be some qualified privilege. But for the whistleblower I think it would be good to see that encoded in the law so they could take comfort from it.

ACTING CHAIR—Does every company have an auditor?

Mr Young—Every public company, yes.

ACTING CHAIR—Have a look at the KPMG submission—I suggest they do not.

Senator CONROY—I wanted to talk about your submission in general. If you could pass back to the Law Society of Western Australia that I was particularly grateful for the following view:

The Society recognises that the Parliament has power to amend impending legislation.

If you could please communicate that to Ms O'Brien; I understand she is not the president any more. I understand why a misapprehension has arisen about the matters that were the subject of amendment—I was probably the mover and I think Senator Murray might have been the seconder of the amendments referred to—but I was wondering whether or not the society was aware that this committee, in conjunction with all the other consultations that were going on, held a public inquiry into the original draft and in 1996 came up with unanimous support for these amendments—

Senator MURRAY—A number of them anyway.

Senator CONROY—It might not have been all of them, but a substantial proportion of these amendments were actually supported following a public inquiry with public submissions and public debate. Then when the legislation was finalised and submitted to the parliament there was a further public hearing. Again, while the party lines came into play and the government members opposed any of the recommendations, the Democrats and the Labor Party indicated that they were still supporting those amendments and were going to

pursue them. I am wondering whether or not 'a surprise at something passing the parliament' as opposed to 'a lack of consultation' was a more appropriate response than saying, 'We recognise the parliament has the power but we ought not to have exercised it in this case.'

Senator MURRAY—I should point out just before you respond that the corporations and securities committee held its hearings and issued its report in March 1998, and the bill was considered in June 1998. So there was a gap of three months between a clear indication of where the parliament was going as opposed to where the government was going—and the two are distinct, as we all know—and the eventual resolution of the bill.

Mr Young—The issue, as it was seen, was that invitations were given to comment on a bill, there was a process and then—apparently at a late stage—there was no government proposal, but the parliament came to a position which took some by surprise.

Senator CONROY—Surprise isn't the same as no consultation.

Mr Young—But after the positions had been established—the input had been given, if you like, on a basis that may have been somewhat naive in that the commentary had been on the bill, the work had been done on the bill, there was a report that other matters might be considered—there was no invitation for consultation on those other matters. I think that is the point. I am not saying there was not some time for those who followed what had happened to comment, but that no consultation was invited following the finalisation of the public hearings.

ACTING CHAIR—I understand the position that the Law Society would find itself in. I don't think it is fruitful to put Mr Young through the—

Senator CONROY—I appreciate your view on it, Ms Bishop, but I have a couple more questions.

ACTING CHAIR—I am well aware of how the Law Society operates.

Senator CONROY—I am not, so I am interested in Mr Young's description of it.

Senator MURRAY—Can I explore a typical example for you, Mr Young, because frankly the Law Society faces the same difficulties the parliament does—that is, having a divided view. Let us take the 28-day issue. When the committee heard the submissions and the arguments, the submitters in March 1998 were divided. There were those who supported the government's proposition of 21 days; there were those who supported the 28 days. The parliament had to make a decision out of those. The minorities clearly indicated they were going to go the 28 days and, in the end, the parliament resolved it. All I think you should recognise is that, in the parliamentary process, you have to judge competing viewpoints. We were not faced with a unanimous view in the marketplace by the Law Society and by other submitters on the 28- versus 21-day position. That is all I would offer you as explanation for the sorts of events that occur.

Senator CONROY—I have one more question on one of your other paragraphs. In the final paragraph on the first page you are expounding this principle:

Accordingly, the Society contends that when a Bill has been the subject of extensive public consultation that it ought not be amended before becoming law without a similar opportunity to comment on any proposed amendments.

I have not received a letter from your society concerning the GST legislation yet. I was wondering when it would be arriving, because about 128 amendments were moved with no notice in the Senate and passed within a week.

ACTING CHAIR—I don't think this is a fruitful area of inquiry, Senator Conroy.

Senator CONROY—I just missed your submission to the GST inquiry on that.

Mr Young—It is not a committee of the society that I am on, but I am not aware that the society was consulted on the original legislation.

ACTING CHAIR—Mr Young, I don't think the questioning is taking us any distance at all in considering the terms of reference before this committee. Is there any other matter that you wish to comment on generally?

Mr Young—No, thank you.

ACTING CHAIR—I thank you for your time here this afternoon. It has been most useful and if you could pass on my thanks to the Law Society for the submission that has been made. Obviously, the committee will be reporting in due course.

[2.07 p.m.]

CRABB, Mr Rick, Partner, Blakiston and Crabb Solicitors; and Associate Member, Association of Mining and Exploration Companies

ACTING CHAIR—Welcome to the third public hearing of this inquiry into matters arising from the Company Law Review Act 1998. The committee does conduct its hearings in public; however, if there are any matters that you wish to discuss with the committee in camera then we would consider any such request. I remind you that the giving of false or misleading evidence may constitute a contempt of the parliament. In what capacity are you appearing?

Mr Crabb—I am appearing in two capacities: firstly, as a partner of Blakiston and Crabb Solicitors, who have made a submission to the committee, and, secondly, I am here representing the Association of Mining and Exploration Companies, of which I am an associate member and a member of the committee dealing with company law matters.

ACTING CHAIR—I understand that the committee is happy for you to make submissions on its behalf.

Mr Crabb—Yes.

ACTING CHAIR—We do have your Blakiston and Crabb submission. Are there any corrections or alterations you wish to make to that submission before we turn to it?

Mr Crabb—There are no corrections. I want to expand on the section dealing with environmental compliance. In some contexts it may be viewed as a correction, but it is perhaps sufficient for me to expand rather than necessarily correct the particular wording.

ACTING CHAIR—We also have the AMEC submission. Would it be more convenient for you to deal with the Blakiston and Crabb submission and then the AMEC one, or are they similar in conclusion and we can deal with them together?

Senator CONROY—Do you disagree with yourself on any one of the points?

Mr Crabb—Funny you should say that. I will deal with the Blakiston and Crabb submission first, and then I will address those matters which are different in the AMEC submission.

ACTING CHAIR—On that basis, do you wish to make an opening statement in relation to the Blakiston and Crabb submission?

Mr Crabb—The only very brief opening statement is this: it is important that, in the ongoing review of the Corporations Law, there ought to be recognition that one of the main thrusts of the amendments is to simplify the law. The point I have made in our submission is that some of these proposed amendments are perhaps not a simplification. The result is some imbalance in the Corporations Law between certain provisions, such as those dealing with issuing prospectuses and takeovers, and some of these particular provisions here.

ACTING CHAIR—Do you think a number of those concerns arise from the fact that there is such a variance in company size and make-up and that we are trying to get an across-the-board approach? You have specifically said that a number of the matters are not in the interests of smaller listed companies. Being solicitors in Western Australia dealing with a particular class of corporations, do you think it is a question of trying to apply rules across-the-board rather than considering the classes?

Mr Crabb—Yes, I would agree that that is the problem. On the one hand, there is a desire obviously by the government and also by the stock exchange in Australia to promote international investment. There is a requirement or desire to comply with international standards but, to a large extent, the proposed new amendments, the CLERP amendments, are really setting new standards. It is extremely positive in that regard, but part of the problem I see at the moment for the Australian stock market is that it is very heavily leaning towards the larger end of the market. This is not so much the effect of the Corporations Law. It is really just the way the market has proceeded. I have been thinking quite extensively about how we can rectify that problem.

Putting my AMEC hat on, AMEC was reasonably proactive in approaching the Stock Exchange for some of the changes that are now taking effect on 1 September with a view to assisting smaller companies. That is why the thrust of my submission is to highlight compliance problems for small companies.

ACTING CHAIR—Perhaps we can now take the 28 days notice matter. There has been quite a deal of evidence given about this. Perhaps you could summarise the position that you take on that.

Mr Crabb—With respect, I think it is a retroactive step. It would seem to benefit only large offshore investors. The implication is that it has been put in for that reason. Some overseas investors do not think they have sufficient notice of meetings. I do not think it has any additional benefit for Australian investors, whether they are small or institutional. Again, we see the thrust of changes elsewhere in the act, such as the reference to facsimile proxies and email of proxies. This provision is contrary to that because it is extending the time period. We have a situation in the Stock Exchange where it is now trade plus two days for settlement. Investors are accepting greater speed at that end of the market and then we have a relatively archaic provision here.

The problem—and this would apply for small or large companies—is that we should not view the 28 days in isolation. It needs to be recognised that, if there is a substantial transaction requiring an independent expert's report and substantial meeting materials, that may take anywhere from three to six weeks or more to prepare. If it is a related party transaction, the material needs to go through the Australian Securities and Investments Commission with a 14-day period. Usually before that, it would need to be run by the Stock Exchange.

ACTING CHAIR—It could be six to eight weeks.

Mr Crabb—Yes, then you give the 28 days notice. It really extends by a total of four to five months. On the one hand, people might say, 'Extending the 14-day or 21-day period,

whichever applies, to 28 is not significant.' But, viewed in the whole context, I think it is. I said in our submission that, if we had a provision allowing for facsimile or email of the meeting materials to overseas people—in trying to keep the cost down and not make it an obligation to fax to local people; email is inexpensive—I think that would be a far better result. It is generally a backward step. I really do not see what was wrong with the old provisions in my experience.

Senator CONROY—That is the 14-day provision?

Mr Crabb—It is 14 days, or 21 days if it is a special resolution. So for important transactions it is effectively 21 days because that was the special resolution provision. That is a long time. I am sure the overseas shareholders would receive the material within seven days. If they see that they have another 21 days, they will just sit on it. It is not going to take them 21 days to actually digest it. They will probably spend anything from five minutes to a couple of hours on it and they will have ample time to address it.

Senator MURRAY—In March 1998, four positions were put to the committee. Firstly, there were those who believed that notice periods should be entirely at the discretion of the company in terms of its constitution. Secondly, there were those who supported the 14-day period. I did not hear anyone for seven; I think 14 was the next one. Thirdly, there was the 21-day period, which was the government's preferred position, and the last one was the 28-day period, which—as you have rightly pointed out—was driven very hard by the international investors and those with international links. We have subsequently been advised by witnesses to the committee that in fact those statutory times are always a minima because there are 'plus days' involved for various reasons.

One prospect which the committee could consider could be to make the 28 days a maximum, so we would have 'not more than 28 days' and perhaps—if the government's view were to prevail—'not less than 21'. In other words, the seven in between would be discretionary according to the nature of the company and the nature of the shareholders. If that flexibility were to be added to the existing regime, would that be an improvement of any significance or is that just fiddling at the edges?

Mr Crabb—I think it would be an improvement to reduce the maximum period back to 21 days. As for reducing the minimum period to 21 days, I do not see any great danger in saying the maximum is 28, although it does seem unnecessarily restrictive; there may very well be a good reason to go one or two days beyond that depending on the availability of directors for the particular meeting or whatever. But having a provision like that at least does allow some communication from a major shareholder, for example, to say, 'Informally, I require 28 days.' In that way the company knows that if they want the continued support of that shareholder that is the sort of notice period they ought to sit with.

Senator MURRAY—Proponents of the 21-day approach are arguing that effectively it becomes 25 or 26 because of the determinants of the date and that 28 becomes in fact 33 or 35. Parliament was not intending that it be effectively 33 or 35; it was intending that it be a maximum of 28, and that is why I put that 'not more than/not less than' scenario to you to consider. Do you think people would settle down if the parliament agreed to that or would

they still be chipping away at us and saying, 'This is still too long. We want to make an immediate decision, et cetera'?

Mr Crabb—I personally do not have any problem with the 14-day and 21-day provision that we had. At the moment, given the way communication proceeds, I do not see any justification for reducing those further. I would grant that there may be circumstances where there would be a very simple resolution which could be fairly quickly put to shareholders. Maybe eventually we will have the situation where that can be done by an email vote plebiscite or whatever and it is instantly decided and they can proceed.

A very good example of that is a decision to quickly raise some more money. At the moment you must go to shareholders if you are going to place shares of more than 15 per cent of the current share capital base. If a company would like to quickly take advantage of a market opportunity and place more funds, at the moment it would need to take 28 days to get that but in the meantime the placement opportunity has perhaps been lost.

That is where there is considerable concern. In a way, it is in the context of those resolutions that previously only required 14 days and now require 28 days that is the most problem and not so much those provisions that previously required 21 days, because we have doubled the period. That is why I say we should return to the old provision.

The answer to the question about overseas shareholders is to insert a provision allowing them to have their material emailed to them so they will have at least a full, clear 21 days. I think their concern is that it may take seven days for them to receive their material. The trouble for these overseas shareholders is partly of their own making because they have nominee holders. The material is sent to a nominee holder in Sydney who then passes it on to a nominee holder in London who then passes it on to the actual investor. It is their own structure that is creating the problem not so much the company's.

Senator MURRAY—I wish to explore this a little further on behalf of international investors. I note from your CV that you indicate strong professional practice in resource and mining work in Western Australia. A number of South African companies are interested, therefore there would be a number of South African shareholders. The South African postal system has collapsed in many parts of the country. Unless you were to provide by notice a courier service there is a real danger that a significant shareholder in South Africa, for instance, would be unable to get appropriate notice. The assumption in the modern world is that postal services, email, fax and all that work very well. In many countries where the first Third World kind of mix exists that is not so. We should be cognisant of that in those sectors and industries where it matters a great deal.

ACTING CHAIR—If the postal system has collapsed, 21 or 28 days might not fix the problem.

Senator MURRAY—It is very often very slow. It is not a question of it not getting there, it is just not a three- or four-day service as it might be if you send a notice from here to London.

Mr Crabb—I have a couple of comments on that. I have some direct experience with South African investment in Australia. I am chairman of a company which is going to come under the control of a South African company. Most of the investment out of South Africa is not actually coming from shareholders in the sense that we may think of it as coming from South African companies which are expanding their operations over here.

Senator MURRAY—But they still receive correspondence by mail.

Mr Crabb—That is true, but it is unlikely that they would be mere shareholders; they would be controlling parties. Your general point is correct. This may apply generally in any other country, but I query whether we need to adopt our law here to deal with Third World investors where it is really their problem. When we are looking at the international market we are looking at the sophisticated international market—whether it is the US or elsewhere. I think the current provisions are adequate.

ACTING CHAIR—We will move on to some of the other issues you have raised. We will look now at the corporate governance and audit committee issue.

Mr Crabb—In the case of smaller listed companies, it is really not practical. I sit on a few company boards where we only have four directors. We meet once or twice monthly, if not more often than that informally. It is basically run by the board. You know what is going on at all times. The thought of having a separate corporate governance board or audit committee is superfluous because two directors—the independent directors—would sit separately and, as an independent director, you have the obligation to consider those factors anyway.

Senator MURRAY—Assuming that the government and the parliament accepted that something should be done in this area and, for instance, mandated—as was the suggestion earlier—that an audit/governance committee should be required in listed companies, if the parliament and the government were to look at that seriously, would the way to deal with your problem be to allow companies to apply to ASIC to be excepted from that rule? In the circumstances you have described, it is pointless. Would that be an easier way to deal with it rather than not introducing a good principle in major listed companies which have large boards and millions of shareholders, et cetera?

Mr Crabb—Yes. I do not have any problem at all with the concept that large corporations ought to have audit committees and remuneration committees, et cetera. I would be surprised if large corporations did not all have those. It is a principle that is quite appropriate. Allowing ASIC the capacity to make a class order which they can alter from time to time depending on market circumstances may be sufficient. I do not know whether market capitalisation of $100 million is too high. Possibly, $50 million is too low, but there is always the point of whoever appears on the cusp.

Senator MURRAY—The proposition I put to you is that you would not even determine a threshold. ASIC would determine it at its discretion, because sometimes $25 million might be too low, and $200 million might be too high, et cetera.

Mr Crabb—Yes. Again, if there were power in ASIC to make such case by case modifications or exemptions, that would be appropriate. It may have the view that a company—although it is relatively small—because of past problems with continuous disclosure or whatever should not be exempt. If we could overcome what I see as a problem for small companies in that fashion, that would be fine.

Senator CONROY—On that point, you made a reference earlier to your worry that some of the proposed changes are not helping the simplification proposal. The committee would probably be looking at CLERP 6. I am not sure whether that is familiar to you at all at this stage. One of the strong arguments that have been used for the CLERP 6 proposals is a simplification, but it is becoming harder and harder to see how, in the end, all of the judgmental powers are not being left fundamentally to ASIC under the CLERP 6 proposal. Whenever I have met with the business community, I have got the strong feeling that certainty is the thing they need more than anything else. It being left up to ASIC to make a decision on a whole variety of areas—whether they be CLERP 6, CLERP 1 to 4, or this one—does not give you the certainty that you need. You may say that that uncertainty is better than black letter. It is a little philosophical.

Mr Crabb—Yes, I agree with that. ASIC would probably prefer not to be left with too much discretion and trying to second-guess parliament.

Senator CONROY—Takeovers is an area where they chop and change all the time. There are continual arguments about what the rule is.

Mr Crabb—Yes.

Senator CONROY—There are arguments about, 'You have varied it here, but you have not varied it there.' I am seeing that cropping up a little bit more under the heading of 'simplification', which is passing some powers back to ASIC that, as you say, they may not want.

Mr Crabb—In this particular area you are talking about—corporate governance boards and audit committees—if these separate committees have to be established, I do not think it is going to improve the governance of those small companies, because there will be little difference between those committees and the full board. The idea of having these separate committees is that certain non-executive directors have a greater focus and a greater scrutiny of activities than they might have otherwise had as merely non-executive directors. But in these small companies, you have to look at everything anyway. In a way, you have part of that function in a separate committee. It is not an area I am greatly concerned about. As a lawyer I can see the difference, but it creates extra pages in an annual report where people regurgitate the standard material and we have not really made an improvement in corporate governance.

Senator MURRAY—There are three ways in which this has been evaluated by progressive thinkers who specialise in this area. The first view is that you just simplify, modernise and make more efficient the law pretty well as it has been. It is just updated, really, and modernised. The second view is that you move onto a kind of trade practices approach. The trade practices approach has established principles and to underpin it with a

mandatory code of conduct which is established for a particular industry or whatever. As you know, that happens in franchising, telecommunications and a number of other areas.

The third view is that you say that companies which fulfil a certain number of characteristics—for instance, they would have corporate governance boards and very good practices of some sort in that area—would not have to abide by much of the black letter law. In other words, because they have got the right structure, they can ignore a lot of the law and much more self-regulation takes place.

Do you have any feeling on whether the government should start to look in that direction? I remind you that I think the committee was told that the Canadian corporations law is 90 pages long, or something, based on trying to get a minimum amount of black letter law, but making sure that companies do well against certain principles.

Mr Crabb—I actually like that third approach, because what it should result in is, a number of situations where these companies, which are not strictly speaking obliged to comply with a whole list of black letter law provisions, will nevertheless comply with all of them and report all of them. But what it gives them is the capacity to not deal with some that they do not consider to be important, material or appropriate. The result is to produce a better quality publication, whether it be a prospectus or an annual report, which is more meaningful for shareholders, or is thought to be more appropriate.

The problem at the moment is that, notwithstanding the changes that the Corporations Law instituted many years ago, the prospectuses still follow a particular format and have a lot of unnecessary information. It has taken a long time for corporations and their advisers to slowly break out of that and be a bit bolder in producing a better type of document. Often it has been in the context of government issues where we have seen that and things have followed forward from there.

I do think that is a good approach and it is a self-regulation approach. It is consistent with the way the tax legislation has proceeded. The idea is that you have a sophisticated market. The market is very critical if people do not get things right. That is where they look. They do not look to the law. They say, 'How is the investing public going to react to us?' If you have a law that cannot be enforced because ASIC is understaffed or underfunded, it is pointless, but in the marketplace they will suffer immediately if they do not maintain the standards. That is where this general legislative change seems to have been directed.

ACTING CHAIR—One other issue that has raised quite a deal of comment is in relation to remuneration. You have said in your submission that it will be a boon for executive remuneration consultants and will also lead to increases in the levels of remuneration. Finally, you suggested it is highly prescriptive and could lead to unintended consequences. Would you perhaps elaborate on those three propositions?

Mr Crabb—Yes. They were perhaps a couple of throwaway comments and I do not really have any evidence to present, although I can probably chase up some material in the financial press. I do not know who else has appeared before the committee. There is a financial consulting firm called Cullen Egan Dell, which is an international firm. They are

quoted in the *Financial Review* in the context of executive remuneration. I think organisations like that would confirm that what has happened in the US as a result of particular disclosure of particular executives' salaries is to substantially increase the level of remuneration payable to them. **Senator CONROY**—They should be thankful, then. Why are they complaining? Why are they attacking them?

Mr Crabb—Yes, that is right. This is a difficult area. This really crops up on a couple of other points. We have to accept that we are going to have to comply with the US model. If we want to have international recognition, then unfortunately Australia, like many other countries, has to look there. We will have to accept some of these consequences that flow from that.

I am certainly not an expert in this area, but my understanding is that the result has been that top end management has received substantial increases. Middle management, where there is not this disclosure, is not a perfect market for executives, therefore, their salaries have languished back. It has created this imbalance. On the other hand, there ought to be disclosure. These people are running the company. Personally, I would be quite comfortable with the previous position where there was disclosure within the band, and you rely on executive directors and non-executive directors to fulfil their duties to make sure the company is paying the appropriate remuneration.

Senator CONROY—You are not aware of an upsurge in kidnappings in the last 12 months?

Mr Crabb—No, if there is, it has been kept quiet.

ACTING CHAIR—In relation to that issue as well as perhaps the information required by foreign exchanges, is it just a question of timing of these amendments in the sense that we are heading towards international harmonisation, international standards and the like? Both the remuneration issue and the information required by foreign exchanges could well be matters that in due course we would have to address. So, is it just a question of timing at present?

Mr Crabb—I think that is right. We will eventually have—whether it is a decade or two away—a completely integrated reporting system. As mentioned in my letter, the concern I have is that, strictly read, this section seems to require you to report in the same form as you have in the US or Canada, for example. The accounting standards are different and you end up with a confusing set of two reports. I really do not see what was wrong with the current situation where, if you disclosed something that is material in the US, Canada or wherever, you must also obviously disclose it here, but you disclose that in a format that is suitable for the current market.

My reading of listing rule 3.1, which is supported by section 1001A and 1001D of the Corporations Law is that that is achieved. This will just result in extra paper going onto the ASX file, which may well confuse investors. It is again contrary. The principle is right of disclosing both markets, but we are just going against the simplification thrust.

ACTING CHAIR—I think we have dealt with your submission. Would you like to move on to the AMEC submission and, if there are any matters that you have not dealt with in your submission or about which there is a different position being put forward by AMEC, could you draw our attention to them?

Mr Crabb—The other point I would like to touch on from my submission is the environmental compliance, which is section 299(1)(f). This again is one of those difficult areas. My basic proposition is that it should not be the function of the Corporations Law to restate, duplicate or override specific environmental legislation. There is already a lot of environmental legislation operating at a state and Commonwealth level. We do have ASX listing rule 3.1 and section 1001A et cetera of the Corporations Law, which requires disclosure of material matters; so that, if there is a breach of a material environmental requirement, than I have no doubt in saying that it must be disclosed. No doubt the auditors would raise it. If it is kept confidential by directors, they are breaching their directors duties, et cetera. So I really do think that that area is quite adequately covered. Obviously, it is appropriate that environmental standards are maintained, but I think this is not the area to cover it in.

Senator MURRAY—The sentence you have there, which says that the new provision will require companies to undertake full environmental audits and include details about compliance, I think is wrong. The reason I say that is that I attended a seminar at which the senior ASIC person responsible for providing advice in this area spoke, and the accounting standards people spoke. It is not true that companies will have to do an environmental audit. As I recall the ASIC note on this, they are merely required to notify anything which is 'particular, material and significant' concerning financial risk. That does not invalidate your general point, but I think you are wrong to believe that the ASIC note which interprets this provision does require environmental audits. In fact, some companies, such as banks, are reporting that they do not need to disclose under this circumstance because they have no environmental issues attached to their function.

Mr Crabb—Obviously my comments are directed from the viewpoint of mining or industrial companies, where obviously they are subject to environmental matters. But, as I see it, unless they undertake at least a first, complete audit they are not going to know whether they are subject to any particular and significant environmental regulation. I am not really sure what is meant by 'particular and significant': the use of the word 'particular' is odd to me, because it could really mean that it is only in the nature of a condition that has been particularly imposed upon that company. I think that possibly restricts the application of the section, which might be counterproductive if parliament intends it to apply.

I assume that 'significant' is something more than 'material'. Generally the law talks about material disclosure and material omissions, and we have this word 'significant', which I think in general use is something higher. Again, perhaps the level of obligation imposed is not terribly high, but I am concerned that we will find that a mining or industrial company will say, 'Okay, here is a list of environmental regulations that are particular and material to our operations,'—and there will be a lot of them: in this state there are probably nine pieces of legislation that apply to a mining operation—'and we have to put details about our performance.'

In many cases they will say, 'We have performed adequately or well,' and so you have a whole list that says, 'Yes, we are very good,' whereas I think the rest of the law, whether state or federal, already covers this area. If they are not performing, they are going to be required to fix up their non-performance.

Senator MURRAY—But, in the reporting environment, it is directed towards informing the shareholder of financial risk—obviously, material financial risk—not compliance with general regulation or law.

Mr Crabb—Yes, that is my very point, in that the disclosure provisions and the listing rules in the accounting standard and in section 1001A require you to disclose anything that would have a material impact on your share price. Obviously, if a noncompliance with environmental regulations creates a contingent liability it may have an effect on your price so you must disclose it.

To clarify what I have said, the existing disclosure obligations are always aimed towards the price of the stock. This section is not. It just requires you to put in the details of your performance in relation to environmental regulation. In most cases, if you decide it is particular and significant, you are obliged to say, 'We have performed.' Let us see what happens in the next few months as these annual reports come out; but that is my concern. It is unnecessary, and it is black letter provisions which are covered elsewhere in more appropriate general provisions which are consistent with the whole thrust of the act.

On the matter of AMEC comments, they make a reference to a proportional voting system. I do not know how significant this point is.

ACTING CHAIR—If this were considered to be an option available to companies, would AMEC still be opposed to it?

Mr Crabb—Yes. We are not entirely sure what it means, but the assumption is that, if a person holds 20 per cent of a company's shares, they are entitled to have one director on a board of five: that is my assumption as to what is meant by proportional voting.

Senator CONROY—So it can be a smooth and efficient beast, like the Senate!

Mr Crabb—Yes.

ACTING CHAIR—We do not have time to go into that, I am afraid!

Mr Crabb—But that seems to the contrary to the general principle that directors have to look after all shareholders. Whilst at the moment there are directors who might be said to represent particular shareholders, they should be very conscious of the fact that they cannot make decisions just on behalf of that shareholder.

ACTING CHAIR—They have fiduciary duties.

Mr Crabb—That is right. It will create a parliamentary type of system which, like most democracies, is not efficient. It might be fair, though.

Senator MURRAY—Really, what we are looking for is a solution to a problem. What happens if there are shareholders who are not represented, because either a majority or a 30 per cent shareholder effectively controls 100 per cent of the board or maybe because a minority or 20 per cent has no influence: how do you deal with that?

Mr Crabb—There is usually a threshold of somewhere between 30 and 40 per cent where that one holder may be able to have elected to the board all their nominees, but it really depends on the strength of the other shareholding. It is fairly rare, in my experience, for there not to be independent directors on the board. You really could not seriously promote your company in the marketplace if it were clear that it simply comprised nominees from one shareholder. Again, the marketplace prevails. Rather than implement this proposal in the form of a proportional voting system, it may be better if there were some requirement that there had to be independent directors; so I take your point about ensuring that there are truly independent directors.

Senator MURRAY—Would you establish that as a rule—in other words, that the ASX would require any listed company to show that it had independent directors and leave it to a judgment?

Mr Crabb—I know from experience that for any proposal to list a new company the ASX would require independent directors. It does scrutinise that. I do not think it has power to do much in the case of an ongoing listed company unless the change is quite dramatic and triggers what we call a chapter 11 change of activity. I would have to think the concept through a bit more. It is probably a fair principle to be explored as to how it might be implemented, but I do not think that a proportional voting system as such should be the method.

Senator MURRAY—One suggestion for a way of fixing the problem—and that is what the committee is asking witnesses to do—would be for witnesses, if they accept the problem, to perhaps consider other solutions.

Mr Crabb—I agree with the principle in general. If people think there is a problem I would like to see them point to specific examples, because I cannot think of any, where it has been quite clear that a company has been controlled by a board nominated by a shareholder that holds less than 50 per cent.

Senator CONROY—Like Coles Myer. Would that be one that falls into any category that you are referring to?

Mr Crabb—But the point is that you have to assume that directors who say they are independent and so on are not. That is the loop.

Senator CONROY—You have privilege: feel free.

Mr Crabb—Coles Myer is too big a company for me to worry about. I do not know enough about that example.

ACTING CHAIR—You are suggesting that the overriding obligation of directors is to act in the interests of all shareholders. You have to undermine that proposition for a start.

Mr Crabb—I think the reality in the marketplace is that if you want to seriously promote your company you have to have the appropriate board and that is, to their credit, something that the broking community forces upon companies at the moment.

Senator MURRAY—It took many years, and at much cost, for the Coles Myer problem to be resolved; whereas a pre-existing rule may have saved that.

Senator CONROY—The Crown Casino.

Mr Crabb—Yes. I certainly take your point—rather than something as rigid as a proportional voting system. You would still be left with the question of whether people who say they are independent are or not, but they would have to convince a smaller group of shareholders. It probably would have some benefit. I will give it some thought.

ACTING CHAIR—I have looked at the AMEC list and in most instances it seems to have been covered—unless there is anything specific you want to bring our attention to?

Mr Crabb—No, I think we have covered everything.

ACTING CHAIR—Mr Crabb, thank you very much for your submission and your time this afternoon. Can you also pass on our appreciation to AMEC for taking the time to prepare a submission and for your attending on their behalf?

Mr Crabb—I will.

Committee adjourned at 2.55 p.m.