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The CPRS Exposure Draft Team
Emissions Trading Division
Department of Climate Change
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Email: emissions.trading@climatechange.gov.au

Dear Sir/Madam,

CARBON POLLUTION REDUCTION SCHEME LEGISLATION

The Australian Institute of Company Directors (AICD) welcomes the opportunity to make a submission about the Scheme legislation.

AICD is the peak organisation representing the interests of company directors in Australia. Our current membership consists of over 24,000 individuals drawn from large and small organisations, across all industries and from private, public and the not-for-profit sectors.

We are concerned about the short timeframe provided for consultation on the legislation and the effectiveness of the process. Unique and innovative legislation requires a far more extensive consultation period. Although the White Paper and the work of the Garnaut Review have foreshadowed its content and structure, the legislation itself requires proper assessment, particularly since it is a substantial legislative package.

AICD notes the estimate that approximately 1000 entities will be directly subject to the legislation. However, the legislation will have a flow-on effect for all companies and the economy generally.[1]

As the peak organisation for directors and corporate governance, our submission deals only with the liability of officers of companies.

Part 20—Liability of executive officers of bodies corporate

AICD believes that directors make an important contribution to economic growth through their oversight and monitoring of companies. The laws that apply to directors, as to other citizens, should be "principled laws" – they must be fair, clear, consistent and stringent with appropriate penalties.

[1] Carbon Pollution Reduction Scheme White Paper- Summary, Scheme Coverage: 15 December 2008

At its meeting on 29 November 2008 Council of Australian Governments (COAG) agreed to a new National Partnership to deliver a seamless national economy to benefit businesses and strengthen the economy. COAG agreed to increased harmonisation in relation to directors' liability and asked the Ministerial Council for Corporations to report back to COAG on further reforms by mid 2009.[2] AICD supports this process and strongly urges that the COAG outcomes reflect "principled laws" as should the provisions in this Bill affecting directors.

The Corporations and Markets Advisory Committee (CAMAC) is the Federal Government's principal adviser on corporations and securities law. In its Report on Personal Liability for Corporate Fault, CAMAC identifies the practice in some statutes of treating directors or other corporate officers as personally liable for misconduct by their company unless they can make out a relevant defence. Provisions of this kind are objectionable in principle and unfairly discriminate against corporate officers compared with the way in which other people are treated under the law.

Provisions deeming corporate officers to be liable, and subject to penalties, for corporate conduct that they could not reasonably have influenced or prevented might be seen as delivering a form of justice in the context of a one-person company. However, they do not reflect the realities and complexities of governance of larger firms, including the board model of a majority of non-executive or independent directors who are not involved in day-to-day operations of the company.[3]

CAMAC's Report is the genesis for the COAG initiative. Despite the clearly expressed CAMAC views which AICD supports, and COAG's reference to MINCO, the Bill has a different and far less cogent approach to director liability (see our comments below in relation to clause 324).

"Principled laws" do not reverse the burden of proof in court proceedings; they uphold the fundamental pillars of a democratic society and the rule of law. Directors like any other citizens in Australia should not be required to prove their innocence. However, the onus of proof appears to be reversed, for example, in section 336 in relation to a person who argues a mistake of fact as a defence to a civil penalty order. This type of provision should be removed from the Bill.

There is also a need for a broad-based defence or safe harbour in statutes for directors when they make commercial decisions in good faith having informed themselves about subject matter of a decision and have acted in best interests of company. If directors' actions meet the criteria they should not, with benefit of hindsight, be liable for errors of judgment. Such law reform would enable the majority of directors, who carry out their duties diligently, to better focus on strategic decision-making, thereby enhancing company performance. The Bill should include such a safe harbour provision.

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[2] Council of Australian Governments Meeting Canberra 28 November 2008 Communique: Seamless National Economy 9

[3] Corporations and Markets Advisory Committee, Personal Liability for Corporate Fault Report, September 2006: Clause 1.5.1: The concerns. Although the Report places some emphasis upon criminal liability it canvasses liability in civil and criminal contexts. The entire Report needs to be considered as it deals the issue of personal liability in a detailed and practical context.

We make specific comments on some sections of the Bill below:

323 Simplified outline

The outline is not correct in stating that contravention will result if the executive officer "was involved" in the contravention by the body corporate. This expression implies direct conduct by the executive officer but clause 324 does not require involvement.

324 Civil penalties for executive officers of bodies corporate

The term "body corporate" is not defined in the Bill and is clearly intended to encompass a wide a range of incorporated entities. The term "liable entity"[4], which is defined, includes a body corporate by necessary implication. The Bill anticipates a constitutional challenge through use of the defined term "constitutional corporation"[5] and the provisions of clause 382 of the Bill. Clause 383 is also a factor in the Bill's constitutional reach. The doubtful constitutional reach and use of disparate terminology will most likely lead to uncertainty in application and interpretation of the Bill.

The definition of "executive officer" is unusual as it is focussed upon directors and three specific office bearers. The inclusion of directors who are non-executive is inconsistent with the thrust of the definition and it should be amended to include executive directors only. Inclusion of three specific office bearers may not necessarily reflect the management structure of a body corporate including its responsibility and reporting lines.[6] These vary from company to company. The use of the definition of "officer" from section 9 of the *Corporations Act 2001* may be a more practicable solution.[7] AICD also considers that for the sake of consistency, the term "executive officer" should be used throughout clauses 324 and 325.

AICD has reservations about the way in which clause 324 would work in practice. AICD strongly agrees with CAMAC's view noted before that, as a general principle, individuals should not be penalised for misconduct by a company except where they have personally assisted or been privy to the misconduct.[8] The provision should be redrafted in line with this important principle. However, dealing with the wording of the clause as it is presented, "being in a position to influence" the conduct of a body corporate is an inexact standard. Being in a position to influence is not necessarily being in a position to prevent or affect a decision to do or not do something which leads to a contravention. The word "influence" in clause 324(1)(c) should be replaced by the word "prevent". This would then be consistent with clause 324(1)(d).

325 Reasonable steps to prevent contravention

It is not entirely clear whether this clause places the burden of proof upon the executive officer. There is an implication that it does, but no precise language deals with the point. In the absence of express language it may be argued that the burden of proof is on the Australian

[4] Clause 5. The definition is unhelpful as it means a person who is a liable entity under the Bill. The definition of "person" in Clause 5 includes a body corporate but not a liable entity. These multiple definitions are a source of confusion.
[5] Clause 5
[6] See CAMAC's view in Clause 4.4 of the Report cited in footnote 3
[7] Appendix 5 of the CAMAC Report discusses the term 'executive officer" and may be a useful point of reference
[8] Clause 1.5.2 of the CAMAC Report

Climate Change Regulatory Authority [9], but for the sake of certainty and fairness, a new sub-clause (3) should be added as follows:

> "...(3) In determining whether an executive officer failed to take all reasonable steps the evidential burden shall be upon the Authority[10]..."

The reasonable steps criteria outlined are predicated on the basis that an executive officer has responsibility for, or control over, the matters listed.[11] That will depend upon the management structure and responsibilities in each firm. Compliance steps or programs will vary from company to company.

The word "ensuring" should be deleted from the outset of clause 325(1)(a). It is not possible to ensure compliance with any statutory requirement and no compliance program can meet that standard. Compliance steps may cover many circumstances and this Bill has a range of civil penalty provisions of different effect and application. Statutory provisions may be open to interpretation or an accepted interpretation may later be found wrong by judicial decision.

There needs to be a balance between reasonable regulation and reasonable compliance for companies. That balance is not often struck providing unfair and inappropriate challenges to companies and directors. Directors often point out that board meetings are dominated by legal compliance processes rather than commercial decision making designed to maximise business performance and profitability for the benefit of the economy.

Compliance obligations arise in a wide range of legislative areas such as corporations, trade practices, taxation, occupational health and safety, environment protection and payroll tax. There is also ongoing oversight by regulatory bodies such Australian Securities and Investments Commission, Australian Taxation Office, Australian Securities Exchange, Australian Competition and Consumer Commission and the occupational health and safety and state revenue regulators in the various jurisdictions. The Australian Climate Change Regulatory Authority, which will administer the scheme legislation, will be an addition compliance burden to the already complex regulatory environment for companies.

Clause 325(1)(a)(i)

The reference to "professional assessment" implies external assessment. It should be made clear that an assessment may be an internal assessment. Most companies covered by the legislation will have the in-house expertise to conduct such assessments and may prefer to do it that way. Some may prefer external assessment. Companies should have the option to choose the assessment method. The word "professional" should be replaced with the words "internal or external".

Clause 325(1)(a)(iii)

This clause should be confined to employees. If agents and contractors have direct obligations under the Bill those obligations should be within their responsibility. It would be unnecessary duplication for a body corporate to have obligations of knowledge and understanding.

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[9] Clause 328 provides that only the Authority may apply for a civil penalty order
[10] "evidential burden" is defined in Clause 5 of the Bill
[11] See footnote 6

Clause 325(1)(b)

Clause 325(1)(b) has some elements of inconsistency with clause 324 which has four tests which must be satisfied before the executive officer contravenes the subsection.

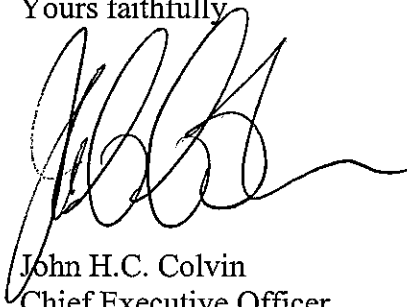
The words "was contravening" suggest an ongoing form of contravention and what action (if any) the executive officer takes when he or she becomes aware of the contravention. This is not necessarily consistent with knowing that the contravention would occur. At that point it would not be possible to take reasonable steps to prevent the contravention.

Federal Court

Clause 325(1) may be too restrictive in that it provides the matters the Federal Court "is to have regard to". On a strict interpretation that means only the matters set out in paragraphs (a) and (b) and limits the reasonable steps that might be taken. AICD considers that the Federal Court should be given a wider discretion by using the words "the Federal Court may have regard to" at the outset of the clause and include a "catch all" paragraph i.e. any matters the Federal Court may consider relevant. Clause 325(1) should also enable the Federal Court to take into account circumstances where no reasonable steps were available to the executive officer under the circumstances. These amendments may remove the need for clause 325(2) which has uncertainty about its meaning and intention.

Thank you for the opportunity to make a submission in relation to this important Bill. Should you have any questions in relation to our submission please contact me or Gabrielle Upton on (02) 8248 6600.

Yours faithfully



John H.C. Colvin
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