A E F ROFE AM

12 April 2005

Dr Anthony Marinac
Acting Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
CANBERRA ACT 2600 **By email to:**
corporations.joint@aph.gov.au

Dear Dr Marinac

Exposure Draft of the Corporations Amendment Bill (No 2) 2005

I am attaching a copy of a submission on the above Exposure Draft Bill which I have forwarded to Treasury.

I apologise for not having been able to lodge it with you by last Friday.

I would be happy to discuss or expand upon any of the matters raised in the submission.

Yours sincerely

Ted Rofe

CORPORATIONS AMENDMENT BILL (NO.2) 2005

Submission by A E F Rofe

The following submission is made in response to the invitation published by the Parliamentary Joint Committee on Corporations and Financial Services ('the PJC' or 'the Committee') on 18 February 2005.

I have had the benefit of reading a number of the submissions currently published on the PJC website and will comment on these submissions where it appears relevant.

I note that the Exposure Draft Bill is intended to facilitate increased shareholder participation in corporate governance, while reducing its costs and that the Committee will consider:

(a) the need for the proposed amendments;
(b) the impact of the proposed amendments on corporate governance;
(c) the impact on shareholder participation of the Bill, including proposed amendments to the '100-member' rule;
(d) the impact of the proposed amendments to rules for proxy voting;
(e) possible alternative approaches; and
(f) any related matter.

For convenience this submission will address the issues raised in the order of the items listed in paragraph 1.8 of the Explanatory Memorandum ('the EM') accompanying the Exposure Draft.

* * *

Remove the 100 member rule from section 249D of the Corporations Act.

No compelling evidence has been provided in support of this proposed amendment.

No examples of allegedly vexatious use of section 249D have been cited or analysed in either the EM or any of the submissions published on the PJC website.

According to the ASX Share Ownership Survey 2004, 44% of Australia's adult population, or approximately 6.4 million people, own shares in Australian companies directly in their own name.

Encouraging increased direct share ownership by individuals is an important means of dealing with the economic problem of an ageing population.

Abolishing the 100 member rule would disenfranchise retail investors and mean that only institutional shareholders were in a position to request the calling of meetings

There are currently over 1,500 companies listed on the Australian Stock Exchange ('ASX').

The provisions of, inter alia, sections 249D, 249N and 249P of the Corporations Act were inserted in what was then the Corporations Law by the *Company Law Review Act 1998* which was assented to on 29 June 1998.

Prior to its amendment in 1998, section 246 of the Corporations Law provided that – in the case of a company having a share capital – at least 100 members holding shares in the company on which there had been paid up an average sum, per member, of at least $200 and – in the case of a company not having a share capital – at least 100 members, could require the directors of the company, as soon as practicable, to convene a general meeting of the company to be held as soon as practicable but, in any case, not later than two months after the date of the deposit of the requisition.

In the period of some seven years during which section 246 was in force and the further period of nearly seven years since section 249D came into operation, there have been only about half a dozen cases in which attempts to utilise these provisions have proved controversial.

This is hardly a significant figure.

The requisitions which have stimulated media controversy have tended to involve environmental, social and industrial relations matters.

That such matters can be of genuine concern and economic relevance to shareholders is illustrated by the costs incurred by BHP in relation to Ok Tedi and by Orica Ltd (formerly ICI Australia) in relation to the remediation of its Rhodes and Botany sites and by the James Hardie asbestos inquiry.

The Government has acknowledged the relevance of environmental issues to shareholders by declining to seek the repeal of paragraph 299(1)(f) of the Corporations Act: EM paragraph 1.9.

In *Turnbull v NRMA* [2004] NSWSC 577, a requisition had been lodged with the company to call a meeting to consider a resolution to amend the company's constitution by including objects which were, in broad terms, protective of the employment conditions of patrolmen and other employees of NRMA. It was argued that changes in the employment terms of patrol officers might result in a decline in the standards of the road service provided to members.

Campbell J held that this was a proper purpose although, as discussed below, for the reasons indicated in his judgment, he made an order that the meeting not be called or convened in response to the requisition.

The use of emotive terms such as "special interest groups" does not of itself assist the debate.

All of the parties who have made submissions to the PJC could be said to be representatives of "special interest groups" but that does not, of itself, render their actions and arguments any more or less valid.

There is significant judicial authority as well as a number of specific provisions in the Corporations Act which serve to limit possible abuse of section 249D (and of sections 249N and 249P) and minimise the costs of complying with those sections.

Proper purpose

Section 249Q provides that a meeting of a company's members must be held for a proper purpose. This section was inserted in the Corporations Law at the same time as sections 249D, 249N and 249P and was intended to limit any possible abuse of those sections.

In *Howard v Mechtler* (1999) 30 ACSR 434 Austin J expressed the view that section 249Q did not introduce any new substantive law, pointing out that in *Australian Innovation Ltd v Petrovsky* (1996) 21 ACSR 218, Whitlam J had been able to extract a similar principle from the general law without having to rely on any particular statutory text.

Austin J agreed with Whitlam J that in some circumstances calling a further meeting shortly after a meeting on substantially the same subject matter had been held could itself be sufficient to establish an intention to harass and consequently impropriety of purpose although he did not find that to be so in the instant case.

In *NRMA v Parker* (1986) 6 NSWLR 517, ie before the enactment of section 249Q, McLelland J held that members cannot convene a meeting of a company or propose a resolution if the subject matter of the meeting or resolution is a matter of management exclusively vested in the directors. See also *Queensland Press Ltd v Academy Instruments No 3 Pty Ltd* (1987) 11 ACLR 419.

In *Australian Innovation Ltd v Petrovsky* (supra) Whitlam J held that the meeting was not being requisitioned for a proper purpose and that the objective of the requisitioner was simply to harass the company and declared that the relevant request did not constitute a valid and effective requisition under section 246.

Power of court to order that meeting not be held

As indicated above, in *Turnbull v NRMA* Campbell J held that he had power under section 233 of the Corporations Act to order that a meeting requisitioned under section 249D not be called or convened on the grounds that it would be contrary to the interests of the members of the company as a whole for the meeting procedure to continue, even though the meeting had originally been requisitioned for a proper purpose.

Power of court to postpone meeting

Under paragraph 1322(4)(d) of the Corporations Act the Court has power to make an order extending the period for doing any act under the Corporations Act and may make such consequential or ancillary orders as the Court thinks fit.

This includes extending the time for calling and holding a meeting requisitioned under section 249D.

Pursuant to this power a court may extend the time for calling and holding a meeting requisitioned under section 249D to enable the meeting to be held in conjunction with the next scheduled annual general meeting of a company: see for example *NRMA v Snodgrass* [2002] NSWSC 590 and *ASIC v NRMA* [2002] NSWSC 1135.

Economic interest

A number of submissions have suggested that shareholders seeking to exercise rights under section 249D, 249N or 249P should be required to have a minimum economic interest in the company concerned.

Rule 8.10.2 of the ASTC Settlement Rules effectively prohibits the establishment of new holdings of securities of less than a marketable parcel, which is currently defined in the ASX Market Rule Procedures as a holding of not less than $500. The rule provides that a Participant must not initiate a Transfer of Financial Products if, by giving effect to that Transfer, a new CHESS or Issuer Sponsored Holding of less than a marketable parcel will be established unless:

(a) the Holding of less than a marketable parcel is expressly permitted under an Issuer's constitution; or
(b) the Transfer establishes a new Settlement Holding or Accumulation Holding. (Accumulation Holdings and Settlement Holdings are used by Market Participants to facilitate the settlement of transactions).

Thus it is within the control of listed companies whether they permit the creation of holdings of less than a marketable parcel.

Assuming that Rule 8.10.2 is enforced shareholders seeking to exercise their rights under the 100 member rule would be required to have a total economic interest of at least $50,000 and under the proposed 20 member rule at least $10,000, which in both cases is significantly greater that the figure of USD2,000 referred to in the ANZ submission.

Reduce the threshold allowing members' resolutions to be brought to Annual General Meetings already scheduled (Section 249N)

I am not convinced that there are strong reasons for opposing the proposed amendment of sections 249N and 249P.

In Telstra's submission it is stated that the purpose of section 249N is to allow "significant" shareholders, or significant groups of shareholders, to put resolutions to

the company's members and that if the section were to be amended in the manner proposed there is a risk that "small interest groups" would use the amended section to put numerous additional resolutions before a company's annual general meeting.

This begs the question.

Whether a resolution has been proposed by a "significant" shareholder or an "insignificant" shareholder is irrelevant to the validity of the proposal. What is relevant is whether or not it is supported by a majority of shareholders voting at a meeting of the company's members.

Whether or not a matter is of "legitimate interest" to a company's shareholders or is "frivolous and unnecessary" or is in the interests of the "wider shareholder base" is something which should be decided by the shareholders themselves or, in appropriate cases, by the courts and not by either Parliament or representatives of a company's management.

The inclusion of additional resolutions on the agenda of a company's annual general meeting will not of itself cause "mainstream shareholders" not to attend meetings nor cause such meetings to become dominated by "fringe issues".

The efficient conduct of company meetings depends to a large extent on the competence of the chairman. If a chairman is of the view that a particular matter is not of interest to or is not supported by the majority of the members present at the meeting, then there are appropriate procedures available to limit discussion of the matter such as the formal resolutions "That the question be now put", "That the meeting proceed to the next business" or "That the speaker no longer be heard", to prevent the proper conduct of the meeting being impeded.

Reduce the threshold for distribution of members' statements by the company along with the notice of meetings (Section 249P)

In arguing against the proposed amendment of section 249P, Telstra claims in paragraph 3.3 of its submission that small shareholders have a number of alternative means of communication with fellow shareholders available to them such as:

- Using mainstream media outlets, the internet and special interest groups to publicise their views to other shareholders.
- Submitting questions to a company prior to its annual general meeting.
- Asking questions and making comments on the management of the company at the annual general meeting.

This argument ignores the fact that:

- Many retail investors do not regularly read the financial press and access internet websites.
- As pointed out in paragraph 2.29 of the Explanatory Memorandum, most shareholders do not attend general meetings.
- The result of a general meeting is usually determined by the proxy votes lodged with the company at least 48 hours prior to the meeting.

The only way in which a shareholder can be sure that his or her views will be seen and considered by all shareholders is for them to be circulated to all shareholders prior to the meeting pursuant to section 249P.

Circulation of shareholder views pursuant to section 249P is likely to encourage a greater number of shareholders either to lodge a proxy or personally attend company meetings thus helping to achieve the Government's stated objective of facilitating increased shareholder participation in corporate governance.

As pointed out in paragraphs 2.15 and 2.17 of the Explanatory Memorandum, section 249P is a valuable mechanism for bringing issues to the attention of a company and its members which, like section 249N, does not impose the larger scale costs of calling and holding a special meeting on the company. Members' statements can assist unsophisticated shareholders to understand the complexity of some resolutions and any surrounding issues.

In paragraph 3.1 of Telstra's submission it is stated that if Telstra were required to circulate an additional one page statement, separately from the notice of meeting, it would cost Telstra approximately $1 million in printing and postage costs.

This represents approximately 60 cents per Telstra shareholder which is not a high price to pay to ensure that shareholders are properly informed of the matters to be considered at a shareholders' meeting.

But in any event both subsection 249O(1) and subsection 249P(7) are designed to ensure that a proposed resolution or statement is received by a company in sufficient time to enable it to be sent out with the company's notice of meeting.

Related matter – Time of receipt of notice or statement

Both subsection 249O(3) and subsection 249P(7) provide that a company is responsible for the cost of giving members notice of a resolution or distributing a statement, as the case may be, if the company receives the notice or statement in time to send it out with the notice of meeting.

Subsections 249O(4) and 249P(8) provide that if the company does not receive the notice of resolution or statement in time to send it out with the notice of meeting, the members making the request are jointly and individually liable for the expenses reasonably incurred by the company in giving members notice of the resolution or distributing the notice.

[Note that there is an error in the opening words of subsection 249O(4) which refer to the members "requesting the meeting"].

There is room for disagreement between a company and its shareholders as to whether or not a notice or statement has been received by the company in time to send it out with the company's notice of meeting.

One can imagine the concern which would be felt by a group of 100 Telstra shareholders who had lodged a section 249P statement with the company two months

before the company's annual general meeting (and indeed the resulting public outcry) if the shareholders were subsequently told by the company that they were jointly and individually liable to the company for costs of $1 million because the statement had not been received by the company in time to send it out with the notice of the annual general meeting.

In the case of a notice of a resolution, there is a further qualification in subsection 249O(1) which only requires a resolution to be considered at the next general meeting that occurs more than two months after the notice it given.

There is room for argument as to whether the date on which a notice is given to a company for the purposes of subsection 249O(1) is the same as the date on which it is received by the company for the purposes of subsections 249O(3) and (4).

Of more practical significance, however, is the case where a notice of a resolution is posted to a company and is received two months before the company's annual general meeting. Should the resolution be included on the agenda for the company's forthcoming annual general meeting or should it be considered at the company's next annual general meeting, perhaps 14 months hence, by which time it may be irrelevant?

It is suggested:

(a) that section 249O be amended to remove the requirement that the resolution be considered at a general meeting that occurs more than two months after the notice is given; and

(b) that both sections 249O and 249N be amended to provide that if the notice or statement is received at least, say, 42 days before the meeting the company will be responsible for the cost of distributing the document to members but that if it is received less than 42 days before the meeting the company must notify the shareholders of the cost of doing so and give them the opportunity to withdraw their request.

Facilitate the electronic circulation of members' resolutions and members' statements (Sections 249O and 249P)

I support the proposed amendments to sections 249O and 249P to enable shareholders to receive notices of resolutions and statements (limited by subsection 249O(5) to no more than 1,000 words) by electronic means.

On the other hand it is important that shareholders who have elected to receive notices of meeting by electronic means should not be compelled to receive all other documents distributed by a company by the same means.

Many retail investors still rely on dialup internet access and comparatively slow, expensive printers to access the internet.

While it may be feasible for them to receive notices of meeting and other short documents by electronic means, they may not wish, and it may not be feasible for them, to receive long, complex documents by the same means.

Ensure the voting intentions of members are carried out by appointed proxies by preventing the 'cherry-picking' of proxy votes (Subsections 250A(4) and (5))

Subject to the comments below under the heading ***Related matter – Direct voting***, I support the proposed amendment.

Prior to its approval, the wording of what is now section 250A of the Corporations Act was discussed at length by the Corporations Law Simplification Consultative Group in an attempt to provide an appropriate balance between the interests of a shareholder who had appointed a proxy and directed the proxy how to vote and the interests of the person appointed as proxy who may be unable or unwilling to attend the relevant meeting or may even unaware that he or she has been appointed as a proxy.

As pointed out in the Explanatory Memorandum, the proposed amendments close a loophole in the present legislation while still preserving a balance between the interests of the shareholder and the person appointed as proxy.

Related matter – Direct voting

A proxy is a person appointed to attend, and in most cases to vote, at a meeting of members of a company in the interest of the person by whom he or she was appointed. At common law a member of a company could appoint a proxy only if this was permitted by the company's constitution. Nowadays the right to appoint a proxy is governed by statute.

Since companies introduced the practice of permitting the form of appointment to include directions as to how the proxy is to vote, which is now required by ASX Listing Rule 14.2, the proxy form is commonly used as a form of postal voting.

If shareholders have decided how they wish to exercise their votes at a meeting, there seems to be no reason to require them to appoint a person to attend the meeting to exercise those votes on their behalf. In other words they should be able to notify the company of how they wish their votes to be exercised without the necessity to appoint another person, either a named individual or the holder of a specified office, eg the chairman of the meeting, to do so on their behalf.

On the other hand it should still be possible for a shareholder to appoint a representative to attend a meeting on their behalf, to listen to the discussion and debate and possibly to speak at the meeting and, having listened to the discussion and debate, to exercise the shareholder's votes, if the shareholder has not already done so.

In other words the position of a proxy holder should be equated to that of a body corporate representative appointed pursuant to section 250D. This could be achieved

by amending section 250D or inserting a new section 250DA along the following lines:

(1) A member of a company may appoint an individual as a representative to exercise all or any of the powers the member may exercise at meetings of a company's member. The appointment may be a standing one.

(2) The appointment may set out restrictions on the representative's powers. If the appointment is to be by reference to a position held, the appointment must identify the position.

(3) Unless otherwise specified in the appointment, the representative may exercise, on the member's behalf, all of the powers that the member could exercise at a meeting or in voting on a resolution.

Individual shareholders are currently at a disadvantage compared to corporate shareholders in relation to the appointment of representatives to attend company meetings on their behalf. A form of appointment of a proxy must in most cases be lodged with a company at least 48 hours prior to the time of the meeting or adjourned meeting: see subsections 250B(1) and (2). On the other hand the appointment of a body corporate representative does not need to be lodged with the company before the meeting.

Permitting individual shareholders to appoint a representative in the same manner as corporate shareholders can now appoint a corporate representative would equate the position of individuals to that of corporate shareholders and thus provide a level playing field for all shareholders.

Amend the requirements relating to the disclosure of proxy votes (Subsection 250J(1A))

I support the proposed amendment.

Subsection 250J(1A) currently provides that before a vote is taken the chair must inform the meeting whether any proxy votes have been received and how the proxy votes are to be cast.

The heading to section 250J contains the words *(replaceable rule – see section 135)* which means that it only applies as a replaceable rule to:

(i) a company that is or was registered after 1 July 1998; and

(ii) a company registered before 1 July 1998 that repeals or repealed its constitution after that day.

Furthermore subsection 135(2) provides that a provision of a section or subsection that applies to a company as a replaceable rule can be displaced or modified by the company's constitution.

Thus it is likely that subsection 250J(1A) applies to few, if any, companies currently listed on the Australian Stock exchange.

This has led to confusion at some listed company meetings when the chairman incorrectly announces that he is "required by the Corporations Act" to announce details of the proxies received.

This approach is sometimes used by chairmen to discourage discussion and debate at the meeting on the basis that the outcome is a foregone conclusion and such discussion and debate would be a waste of the meeting's time.

The preferred approach will normally be for the chairman to announce details of the proxies held at the conclusion of discussion, immediately before a resolution is put to a vote.

This is a matter more appropriately dealt with by best practice guidelines issued by such bodies as AIRA, the AICD or the BCA rather than by the Corporations Act.

Remove the requirement for companies to disclose information reported to overseas exchanges (Section 323DA)

No conclusive grounds have been made out for the repeal of section 323DA.

The disclosure requirements of the United States Securities and Exchange Commission have tended to be more detailed than those under Australian corporations legislation and ASX Listing Rules.

There have been a number of instances where information disclosed in the United States by companies listed on both the ASX and the New York Stock Exchange has been reported in the Australian media but not to the ASX.

Investors in companies listed on the ASX should not be forced to rely on third parties to be fully informed in relation to the companies in which they invest.

Where information has already been provided to the SEC or the New York Stock Exchange or some other financial market in a foreign country, there should be little incremental cost in providing a copy of the relevant document, possibly in electronic form, to the ASX.

Where companies choose to raise money from Australian investors by causing their securities to be listed on the ASX, they should be prepared to provide equivalent information to all investors.

In particular:

(a) Australian entities which choose to have their securities listed on overseas financial markets as well as on the ASX should be required to disclose the same information to the ASX as they disclose to the overseas market operator; and

(b) Foreign entities which choose to raise money from Australian investors by causing their securities to be listed on the ASX should be required to provide the same information to Australian investors as Australian entities are required to provide.

Related matter – Financial reporting by foreign entities

Currently there are about 69 foreign companies listed on the ASX.

In addition, Australian investors are being increasingly encouraged to invest in the securities of foreign entities listed on overseas exchanges through such services as ASX World Link.

I believe, as a matter of principle, that where foreign entities seek to raise funds from Australian investors by causing their securities to be listed on the ASX, Australian investors who acquire such securities, whether by subscription or purchase, should have the same protection under the Corporations Act as Australian investors who invest in securities issued by entities incorporated or formed in Australia.

In particular, such foreign entities should be required to provide to Australian investors:

(a) All information that they are required to provide to foreign investors; and

(b) Information, including financial statements and reports, of the same standard and within the same timeframe as the information that Australian entities are required to provide to Australian investors under the Corporations Act.

Section 323DA is relevant to the first point.

Prior to the enactment of the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004*, there were differences of opinion as to whether foreign entities whose securities were listed on the ASX were required to comply with Chapter 2M of the Corporations Act.

A "disclosing entity" is defined in Part 1.2A of the Corporations Act and includes an entity which is included in the official list of a prescribed financial market some or all of whose securities are subject to the market's listing rules.

Under section 111AO a disclosing entity is required to prepare financial statements and reports for half-years as well as full financial years in accordance with the requirements set out in Chapter 2M. In addition, it is subject to the continuous disclosure requirements of sections 674 and 675.

Prior to its amendment in 2004, paragraph 285(2)(a) provided that Chapter 2M covered all disclosing entities incorporated or formed in Australia "(whether or not incorporated or formed in this jurisdiction)".

Section 111AT provides that ASIC may, by writing, exempt specified persons from all or specified disclosing entity provisions, ie the provisions of Chapter 2M as it applies to disclosing entities and sections 674 and 675.

In 2004 section 111AO and paragraph 285(2)(a) were amended by the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004*, to effectively remove the requirement for foreign entities listed on the ASX to comply with Chapter 2M.

Section 601CK requires a registered foreign company, at least once in every calendar year and at intervals of not more than 15 months, to lodge with ASIC a copy of its balance sheet, a copy if its cash flow statement and a copy of its profit and loss statement, in such form and containing such particulars and including copies of such documents as the company is required to prepare by the law for the time being applicable to the company in its place of origin, but there is no requirement for such financial statements to comply with the provisions of Chapter 2M.

A current example of the problems this can cause for Australian investors is Erawan Company Limited, a company incorporated in Hong Kong, the shares of which are listed on the ASX.

The shares of the company were suspended from quotation by the ASX between June 2003 and 10 November 2003 and again from mid June 2004 to the present due to the company's failure to lodge audited accounts.

I understand a complaint has been made to both ASIC and the ASX who responded that they were unable to take any effective action to protect the interests of Australian investors.

I believe that sections 111AO and 285 of the Corporations Act should be amended to ensure that all entities whose securities are listed on the ASX are required to comply with the provisions of Chapter 2M.

Where an entity is already required by the laws of its place of incorporation to prepare financial statements and reports of a standard at least equal to those required under Chapter 2M (and this would no doubt apply to most companies incorporated in the United Kingdom and the United States) ASIC could grant an appropriate exemption under section 111AT.

Updating references to Patents/Trade Marks/Designs legislation – Section 279(5)

These amendments, which relate to the order of priority of registrable charges on the property of a company, appear to be uncontroversial.

PART 10.4 Transitional provisions

If the proposed amendments are enacted in the form proposed, these transitional arrangements appear appropriate.