Labor Members Minority Report on the

Corporations Amendment (Repayment of Directors' Bonuses) Bill 2002

1. Introduction

For Labor, this bill provides an opportunity to put a legislative spotlight on excessive executive remuneration.

Labor supports the principle that unreasonable payments to directors should be clawed back once a company becomes insolvent. However, this bill does not go far enough – as it fails to address the issue of excessive executive remuneration when a company is solvent.

Also, there are a number of loopholes that exist in the bill that Labor has attempted to address by moving amendments in the House.

2. Loopholes

The bill provides that a liquidator can reclaim an 'unreasonable director-related transaction' made within four years of a company appointing a liquidator.

The definition of what constitutes an unreasonable director-related transaction creates a loophole for certain benefits which escape this definition. The definition does not capture all transactions between directors and companies. In particular, the bill only refers to payments made by the company and not to benefits received by the directors. The effect is that options issued to a director are clearly captured by the definition but any profit made on the exercise of those options is not captured.

The Labor members urge the Government to support Labor's amendments which amend the definition of 'unreasonable director-related transactions' to capture this benefit.

The second loophole in the definition is that it is up to the courts to determine when a payment is considered unreasonable.

To give this legislation some real teeth, the Labor members recommend that the Government support Labor's amendments to proposed section 588FDA which set out the circumstances which the court should have regard to in determining whether a transaction is unreasonable.

Under Labor's amendments, the court would be required to consider the following:

- The payments and benefits received by directors relative to payments and benefits received by employees in the company;
- Whether the payments or benefits were subject to appropriate performance criteria; and

- The time the payments or benefits were received—in particular, their proximity to the time at which the company was placed into administration or liquidation and whether the company was insolvent at the time they were received.

The Committee's view that the proposed criteria in the bill are consistent with existing legislation misses the point.

The purpose of Labor's amendments is to provide *greater* guidance to the Court as to the circumstances that the Court should consider in determining whether a transaction is unreasonable.

2. Scope of the Bill

Executive Remuneration

A large number of submissions, including submissions from the ASA, AICD, ACTU, CPA and ICAA, noted that the bill was too narrow as it failed to address executive remuneration.

The Committee's view that such issues are being considered in CLERP 9 and the exposure draft of the *Corporations Amendment Bill* is feeble. The CLERP 9 paper released by the Government fails to adequately address executive remuneration - in spite of its 205 pages. The only proposal in the CLERP 9 paper on executive remuneration is that the IASB standard requiring expensing of share options will have the force of law on adoption by the AASB, in the second half of 2003. The exposure draft of the *Corporations Amendment Bill*, is similarly bereft. It proposes minimal changes that mostly relate to the disclosure and valuation of options and non-cash benefits.

The Howard Government refuses to legislate in relation to executive remuneration, and instead has adopted a self-regulatory approach.

In contrast, Labor has tried to amend section 300A of the *Corporations Act* by moving amendments to this bill that require companies to publish details of board policy on executive remuneration including performance conditions, the methods used to assess whether the performance conditions have been met, discussion of the relationship between the company's performance and the board's policy and graphs showing shareholder return for the past five financial years.

Labor has also moved amendments that allow shareholders to vote on the board policy on executive remuneration - through an annual non-binding resolution on executive remuneration at annual general meetings.

The Labor members urge the Government to re-consider this opposition to Labor's amendments in relation to this bill, which enhance the disclosure requirements in relation to executive remuneration under section 300A of the *Corporations Act*.

Subsidiaries

Although not strictly relating to this bill, Professor Baxt from the AICD raised a number of issues in relation to the provisions in the *Corporations Act* relating to executive remuneration.

One of those issues relates to the directors' duties in the context of a consolidated group.

Professor Baxt said:

> *"One of the problems that we had with the first version of this legislation was that it did not seem to catch the situation where payments were made not to the directors of a particular company but to another company that was related. Whilst the definition of associate might arguably pick this up, arguably it does not. The government has already before it a report from CASAC or CAMAC, as it is now known, dealing with corporate groups and the way in which that particular area should be dealt with. It has not responded to that report and it has not deal with those issues in the broader sense, so we have these problems spreading out as we get more and more complexity in the way in which the law is developing."*[1]

In relation to this bill specifically, Professor Baxt said:

> *"The way this bill is drafted, I think that if a payment were made to a director of a partly owned subsidiary it might not be caught by this legislation…my initial reaction …is that those sorts of payments would not be caught. If we are talking about evil here – if I can be a bit colourful – then those sorts of payments would not be caught. It would be terrible if we found that someone got off. We see so many cases of people getting off because there is a technical flaw in the legislation and the court says, 'Sorry, there is no case to answer'. We saw that recently in a tax issue."*[2]

The Labor members are of the view that:

- The *Corporations Act* should be amended to ensure that the provisions relating to executive remuneration apply to directors (and key executives) regardless of which company in a corporate group they work for.
- Consideration should be given to whether amendments are also required to this bill to ensure that unreasonable payments made to a director of a partly owned subsidiary are caught by the bill.

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[1] Committee Hansard, 6 March 2003, page E2

[2] Committee Hansard, 6 March 2003, page E10

Officeholders

The Labor members support the Committee's recommendation that the bill also apply to senior executives who are not directors.

3. Date of Commencement

The bill will only apply to transactions entered into on or after the bill receives Royal Assent. Any payments made to directors before this date will not be captured.

The Committee has said that the provisions of the Bill should not be retrospective on the basis that the Treasurer has said that to avoid constitutional doubt, the legislation should apply prospectively.

However, advice from the Parliamentary Library is that whilst it is a principle of statutory interpretation that in the absence of a clear statement to the contrary, an Act will be assumed not to have retrospective application, there is nothing in the Australian constitution to prevent Parliament from enacting retrospective laws.

The Labor members are of the view that the legislation should commence from the date of the Prime Minister's announcement that the law would be amended, that is, from 4 June 2001.

4. Other matters

The Labor members are concerned about the lack of consultation that took place in relation to this bill and recommend that the Government comply with their obligations under the *Corporations Agreement 2002,* to expose bills relating to the *Corporations Act* for public comment for at least three months before introduction.

Senator Jacinta Collins
Labor Senator for Victoria

Senator Ruth Webber
Labor Senator for Western Australia