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15 March 2013

Dear Sir

Re: Corporations Legislation Amendment (Remuneration Disclosures and Other Measures) Bill 2012

We appreciate the opportunity to respond to the Exposure Draft "Corporations Legislation Amendment (Remuneration Disclosures and Other Measures) Bill 2012" ("ED").

Overall, we support Treasury's intention to further strengthen Australian companies' remuneration disclosures, reduce the regulatory burden on companies and clarify the operation of the dividends test under the Corporations Act. However, we have certain concerns in relation to the practical application of the amendments proposed under the ED, which we set out below.

1. Requirements for paying dividends

Test for payment of dividends based on net assets

In our response dated 7 February 2012, to the Discussion Paper – Proposed Amendments to the Corporations Act, we expressed our concern that the test for assets having to exceed liabilities after the dividend is declared is not in essence a 'solvency test' although described as such in the Discussion Paper. Due to the constraints of the financial reporting framework certain assets may not be carried at fair value, for example inventories and certain categories of financial assets, and, therefore, an entity's financial position may not always be fully reflective of its solvency. We believe that the directors of an entity should be allowed to consider the fair value of its assets as part of their solvency assessment.

We note that whilst the ED introduces a requirement for the directors to reasonably believe that an entity shall remain solvent after the declaration or payment of a dividend, the ED continues to maintain the additional requirement that assets exceed liabilities and the excess balance be sufficient for the payment of the dividend.

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We continue to strongly believe that requiring assets to exceed liabilities is unnecessary and will continue to restrict companies from being able to pay dividends even when, notwithstanding the payment of the dividend, the company remains solvent.

We encourage the Treasury to include only one test, a test based on solvency, for the determination of whether a company is able to pay a dividend.

Should, however, Treasury proceed with legislating the proposed amendments in relation to the net assets test we have the following additional comments:

- We welcome the proposed amendment to section 254T of the Corporations Act 2001 to enable companies that are not required to prepare a financial report to calculate assets and liabilities for the purpose of this section in accordance with the financial records of the company (required to be kept under section 286 of the Corporations Act 2001) however we have certain concerns over the practical application of this proposed amendment, including :

  - Whether the term 'required' is intended to mean only (i.e. 'exclusively') those financial reports required by section 292 of the Corporations Act 2001, or whether the term is intended to have a broader meaning. For example, is the term intended to also capture those financial reports required to be prepared under sections 293 and 294 of the Corporations Act 2001 (which we note would only comply with Accounting Standards to the extent specified in the relevant direction)?

  - Is the application of the proposed amendments to section 254T of the Corporations Act 2001 intended to preclude companies from calculating assets and liabilities in accordance with Accounting Standards in circumstances where the company is not 'required' to prepare a financial report? For example, if a company voluntarily prepares a financial report in accordance with Accounting Standards, is it permissible to calculate the assets and liabilities for the purposes of this section with reference to that financial report? In our opinion, companies should have the option to calculate assets and liabilities in accordance with Accounting Standards in circumstances where a financial report is not 'required' to be prepared for the relevant financial year.

    We note that companies may change their classification between 'small proprietary' and 'large proprietary' from one financial year to the next by application of section 45A of the Corporations Act 2001. Such determination is generally made at the end of the financial year. This being the case it may be difficult for some proprietary companies to ascertain whether a financial report will be required *"for the financial year in which the time occurs"* where companies plan to declare/pay an interim dividend. We believe that further consideration should be given to the interaction between section 45A of the Corporations Act 2001 and the proposed amendments to section 254T.

Timing of application of the dividends test

We support the proposed amendment in relation to the timing of the application of the dividends test based on our understanding that the test is to be performed only once, either at the time of declaration of the dividend or at the time of payment. Our understanding of the proposed amendment is that if a company pays a dividend without a process of declaration it shall only perform the test at the time of payment while those companies declaring dividends do not need to re-perform the dividend test at the time of payment. If our understanding is inconsistent with Treasury's intention we recommend that the drafting of the legislation be clarified.

Interaction of the dividends test with the capital maintenance provisions under the Corporations Act

We note that the discussion paper *Proposed Amendments to the Corporations Act* contained a comment that *"[t]he Treasury considers that the test for paying a dividend in section 254T of the Act is a circumstance where a reduction in capital is 'otherwise authorised' by the law."* However in Section 1.16 of the Explanatory Memorandum to the ED, it has been stated that *"[t]he new dividends test does not displace the existing requirements in relation to conducting share capital reductions and share buy-backs under Part 2J of the Corporations Act"*. Given the importance of the interaction between section 254T and Part 2J of the Corporations Act 2001, we encourage the Treasury to provide greater clarity in this area, particularly given that Section 1.5 of the Explanatory Memorandum to the ED states that shareholders have raised concerns about such interaction.

2. Remuneration disclosures

We support the intention of the Treasury to introduce greater transparency to the users of remuneration reports in respect of the remuneration of key management personnel of companies. However, we are concerned that the nature of the disclosures that are being proposed to be added to the existing requirements of section 300A of the Corporations Act, may not achieve in enhancing the users' understanding of the various forms of remuneration of the key management personnel, for example by adding additional disclosures the complexity of the Remuneration report may further increase. In today's complex reporting environment when significant volumes of information are available to users from multiple sources we believe that now may be an opportune time for the Treasury to assess, from a holistic perspective, whether the current requirements in respect of remuneration disclosure result in meaningful disclosure that adds value and transparency to the users and are serving the users' needs.

In relation to the specific amendments being proposed to remuneration disclosures we have the following observations:

Limiting the requirement to prepare a remuneration report to only listed disclosing entities that are companies

We support the proposal to limit the application of section 300A of the Corporations Act 2001 to listed disclosing entities that are companies.

Requiring disclosure of a general description of the company's remuneration governance framework

Given that the proposed requirement replicates the existing practice of many listed companies, we do not believe that requiring the disclosure of the 'remuneration governance framework' will enhance the quality of the disclosures or assist users in their understanding of key management personnel remuneration. We are not supportive of remuneration disclosure requirements being lengthened any further as this creates unnecessary clutter.

of the amendments is consistent with the underlying intent of the Treasury.

- the proposed new disclosures are in addition to those already required under Items 6 - 11 of regulation 2M.3.03 of the Corporations Regulations 2001, which include amounts relating to post-employment benefits and termination benefits. We are concerned that the additional information required to be disclosed under the proposed amendments, without explanation or reconciliation to the amounts disclosed under Items 6 - 11 of regulation 2M.3.03 of the Corporations Regulations 2001, may confuse the readers of the remuneration report. We believe that further
- consideration should be given to whether the additional information, and the manner in which it will be presented, will result in the disclosure of information that is complementary to the information already required to be disclosed.

Requiring disclosure of the remuneration of each KMP in three separate categories; granted before the year and paid during the year; granted and paid during the year; and granted during the year but not yet paid

We are not supportive of this proposal as we believe the proposals have the potential to create greater confusion for readers of the remuneration report. Our key concerns relate to the following:

- the proposed new disclosures are in addition to those already required under Items 6 - 11 of regulation 2M.3.03 of the Corporations Regulations 2001. We believe that the inclusion of, in effect, two sets of remuneration disclosures that are prepared largely on different bases and with no requirement to reconcile the information between the two sets of disclosures is likely to confuse users of the remuneration report.

- the proposals lack guidance as to the meaning of 'granted' and 'paid', in the context of the different forms in which benefits may potentially be provided to key management personnel (e.g., monetary benefits, non-monetary benefits and share-based payment arrangements).

As stated above, we believe that it may be appropriate to perform an overview of whether the current requirements in respect of remuneration requirements are serving users' needs rather than simply adding to such disclosures.

Requiring additional disclosure of details of payments made to key management personnel (KMP) in relation to their retirement from the company

We agree that there is a need for greater transparency in relation to benefits provided to key management personnel in relation to retirement/termination.

We are, however, concerned with certain practical applications of this requirement, especially relating to the following:

- the proposed amendments to section 300A of the Corporations Act 2001 (by way of the insertion of subsection (1) (ea)) requires the disclosure of *"benefits to be given"*, which implies that forward looking information is required to be disclosed, whereas Section 2.18 to 2.25 of the Explanatory Memorandum to the ED refers to *"amounts paid"* and *"benefits paid"*, which implies that the intention of the Treasury is to capture the actual (i.e., historical) amount of benefits paid. We believe that further consideration should be given to whether the proposed wording

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- the proposals lack guidance as to the basis on which the amount of remuneration is to be measured (e.g., cost to the company, value to the employee, or measured in accordance with Accounting Standards).

We strongly recommend that this proposed amendment to section 300A of the Corporations Act 2001 be withdrawn or adequate practical guidance be provided to address the above noted concerns.

Proposal to disclose only the number of options forfeited and the year of grant rather than disclose the value of forfeited options

We welcome any attempt by the Treasury to simplify and/or reduce the disclosure burden in relation to remuneration of key management personnel. We note that this amendment is a step towards achieving the objective of uncluttering the remuneration disclosures.

3. Relieving public companies from appointment of auditors

Currently all public companies, including companies limited by guarantee, must appoint auditors. The ED provides relief from the obligation to appoint auditors for small companies limited by guarantee however we understand that the new reporting framework being proposed by the Australian Charities and Not-for-profits Commission ("the ACNC") will follow a similar revenue tiered approach to that of companies limited by guarantee, to determine whether an audit or review is required. We recommend that consideration be given to other public entity types registered with the ACNC that may no longer require an audit.

We believe that the ED and the Explanatory Memorandum currently do not provide guidance on the transition requirements in relation to the above; i.e. whether the existing auditor of a company which is not required to appoint an auditor will deem to have resigned or whether the auditor needs to follow the resignation process.

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We look forward to providing future input to the Treasury as you continue your reforms to the corporate regulatory framework. If you have any questions concerning our comments, please contact me on (02) 9322 7177.

Yours faithfully

Anna Crawford
Partner
Deloitte Touche Tohmatsu