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## Re-modelled CLERP 9 lifts the bar on corporate governance

### Introduction

The **Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004** force on 1 July 2004. More commonly known as 'CLERP 9', its final passage into law in time for the new year designed to restore confidence in the market after a number of high profile corporate collapses both in Australia and overseas.

CLERP 9 is a substantial piece of legislation that includes reforms relating to:

- disclosure of directors' remuneration
- financial reporting
- auditors independence
- continuous disclosure and
- enhanced penalty provisions.

What follows is a brief, but not exhaustive, overview of the main reforms.

Transitional provisions apply to some of the reforms and the timing of the effect of the reforms varies greatly. **and their advisers should familiarise themselves with the CLERP 9 timeframes so that any requirements can be made to company procedures in a timely fashion.**

### Shareholders to vote on directors' pay packets

Shareholders of listed companies will have the opportunity to express their opinion on the remuneration and senior managers, as well as the board's policy on remuneration. They are also required to give appropriate payments for directors and executives that exceed certain specified limits.

The chair of the AGM must allow shareholders a reasonable opportunity to ask questions about, or make a remuneration report which is to include a description of the directors' and senior managers' remuneration for listed companies. At the AGM shareholders must vote on the remuneration report. The vote on the resolution is only advisory and does not bind the directors or the company.

### CEO & CFO declarations

The directors' report for listed entities must include a declaration from the directors that they have received from the CEO and CFO regarding the company's financial reports. **This declaration must state that the records and annual financial statements are in compliance with the Corporations Act and accounting standards.** It must also include a section stating that the financial statements give a true and fair view of the company's financial affairs.

### Company secretaries' qualifications

Listed companies must disclose the qualifications and experience of the company secretary in the directors' report.

### Auditor's attendance and questions at the AGM

Previously shareholders who attended the AGM were only entitled to ask questions of the auditor concerning the audit and the contents of the audit report and then only if the auditor chose to attend the AGM.

**CLERP 9 requires the auditor of a listed company, or representative, to attend the company's AGM Meeting.** All shareholders, not just those in attendance at the AGM, are able to ask questions of the auditor that shareholders can ask about extends beyond the audit's conduct and the audit report to include the policies and the independence of the auditor. New procedures exist under which shareholders are entitled to ask written questions to the auditor prior to the AGM. This provides a process for all shareholders, not just those in attendance at the AGM, to ask questions of the auditor.

### **Independence of auditors**

CLERP 9 establishes a general standard for auditor independence, which states that independence will be maintained if:

- a) A "conflict of interest situation" exists in relation to the audit client at a particular time;
- b) the auditor is aware that the situation exists, and
- c) the auditor does not ensure that the conflict of interest situation ceases to exist.

CLERP 9 also prohibits nine specific employment relationships and ten specific financial relationships between the auditor and a client and an audit firm or a member of the audit firm (and in certain circumstances, their immediate family members).

### **Audit Partner rotation and cooling off periods**

Other important independence restrictions introduced by CLERP 9 include:

- an individual who plays a "significant role" in the audit of a listed company must rotate off that audit after two successive years and not return for a further two years. The rotation applies only to individual auditors and not to audit firms. The "significant role" definition will mean in practice that this requirement only applies to lead and review auditors.
- a cooling off period of two years is required for partners after they leave the audit firm before they can return to the audit client; and
- no more than one former partner of an audit firm can be an officer of an audit client.

### **Auditor's Independence Declaration**

The auditor of a disclosing entity must give a declaration that, to the best of the auditor's knowledge and belief, there have been no contraventions of the auditor independence requirements of the Corporations Act or any provisions of the Act in relation to the audit. This declaration must be included in the directors' report of the relevant annual or half-year financial report.

### **Disclosure of non-audit services**

Listed companies must prepare a "non-audit services" disclosure to be included in the annual report. This disclosure must include the amount to be paid for each type of non-audit service, a statement as to whether the director or auditor's provision of these services has or has not compromised the independence of the auditors and the reasons for this.

### **Proportionate Liability**

CLERP 9 replaces joint and several liability with proportionate liability in respect of certain civil actions under the Trade Practices Act, ASIC Act and the Corporations Act. The new legislation provides that, in relation to certain actions for damage to property, where a claim is made under the relevant provisions of these Acts, the damages that may be held responsible for is proportionate to the loss caused by their actions.

### **Continuous Disclosure**

Individuals who are involved in a breach of the continuous disclosure provisions of the Corporations Act may be liable to litigation. However a person who is sued under these provisions can respond by invoking the defence ("the defence") that they took all steps that were reasonable to ensure that the entity complied with its continuous disclosure obligations and, after this, believed on reasonable grounds that the entity was complying with its obligations.

ASIC has the power to issue infringement notices to entities for breaches of the continuous disclosure provisions. Infringement notices, which are intended to be used only in regard to less serious breaches, can only be issued if the entity has gone through a private hearing process. The penalties that can be applied through these notices range from \$10,000 to \$100,000.

### **Auditors duty to report to ASIC**

The position before the passage of CLERP 9 was that auditors were required to notify ASIC in writing if they had reasonable grounds to suspect a contravention of the Corporations Act and believed that the contravention would not be detected or corrected.

dealt with by commenting on it in the auditor's report or bringing it to the attention of the directors.

CLERP 9 requires an auditor to also notify ASIC in writing if there has been an attempt to unduly influence, manipulate or mislead a person involved in the conduct of the audit. This significantly expands auditor duties to notify ASIC of suspected contraventions of the Corporations Act.

### Future Developments

The government's requirement to enact this legislation prior to 30 June 2004 meant that some of the recommendations of the Joint Parliamentary Committee into the bill could not be incorporated. The most significant of these include:

- alternative accounting treatments - disclosure in audit reports of the reasons for choosing more favourable accounting treatments where alternative treatments are available
- voting on "multi-chairs" - non-binding resolution of shareholders at the AGM where the chair of the meeting is also the position of chair at another Top 300 listed company
- political donations – disclosure in annual reports of listed companies of the board's policy on making political donations

The government has signalled that the majority of remaining recommendations of the Committee will be considered in the next parliamentary session.

### Further information:

CLERP 9 represents a significant development in the corporate law framework. This summary only provides a high-level overview of its complexities, some of which will require careful planning by companies and their advisers.

Companies need to consider matters such as the increased financial statement disclosure requirements, the processes to enable the CEO and CFO declarations and their preparedness for new voting requirements and the implications of the changes to the Corporations Act.

For a more detailed analysis of the implications of CLERP 9 and advice on its implications for your company, contact your client service representative at Deloitte or:

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