



ASIC

Australian Securities & Investments Commission

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CAMAC Corporate Social Responsibility Discussion Paper (November 2005) ASIC Submission

The Australian Securities and Investments Commission (ASIC) made a submission to the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into corporate social responsibility (PJC Inquiry). That submission (a copy of which is attached) sets out ASIC's key observations on corporate social responsibility.

However, ASIC would like to comment further on some matters raised in CAMAC's *Corporate Social Responsibility* Discussion Paper (November 2005) (Discussion Paper). These comments are informed by ASIC's experience as an enforcement agency and a regulator of corporate disclosure.

Should the Corporations Act (Act) be revised to clarify the extent to which directors may take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions?

As stated in ASIC's submission to the PJC Inquiry, corporations law gives directors considerable freedom to consider the interests of a range of stakeholders, provided the directors' over-riding purpose is to act in the interests of the corporation as a whole. In ASIC's view this aspect of the law is clear and, assuming the Government wishes to retain the current policy settings, the Act does not require amendment.

In particular, ASIC thinks that an amendment based on clause 156 of the Company Law Reform Bill 2005 (UK) may, in fact, create uncertainty. Clause 156 lists a number of matters that directors "must (so far as reasonably practicable) have regard to". Such a list may create uncertainty because directors will, for example, be unsure about:

- the relative weight of matters on the list and, in particular, whether all matters on the list should be given equal weight; and
- whether they can have regard to matters not on the list and whether matters not on the list should be given the same importance as those on the list.

As stated in ASIC's submission to the PJC Inquiry, this sort of uncertainty is of particular concern to ASIC because it is difficult to enforce uncertain legislative provisions.

In general, ASIC considers that the range of matters that may have to be considered by directors are potentially so varied that it would be better to retain the flexibility of the current common law, rather than to force directors to have regard to a list of matters that may be inappropriate for the circumstances of their particular corporation.

Should the Act be revised to require directors to take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions?

The question of whether the law should be amended to require directors to take into account the interests of specific classes of stakeholders or the broader community when making corporate decisions is a fundamental question of policy. Such a fundamental question of policy is best addressed by the Government, not a regulator such as ASIC.

When addressing that question the Government should be aware that an amendment to directors duties along the lines suggested may affect ASIC's ability to successfully enforce the Act. Depending on its precise nature and drafting, such an amendment may create significant uncertainty. For example, it may be difficult for directors, ASIC and the Courts to:

- identify and define the various classes of stakeholders that might be considered to have a legitimate claim on the attention and resource of corporations; or
- establish an appropriate hierarchy of stakeholders' interests to resolve conflicting stakeholder claims on the attention and resources of corporations.

Such uncertainty would impact on ASIC's ability to enforce the law; the more uncertainty that exists as to the precise nature of a duty and to whom it is owed, the harder it is to prove that the duty has been breached. Where a duty is owed to a number of stakeholders with varying interests, it may be difficult for ASIC to establish that a given action was a breach of the duty, rather than the exercise of a judgment based on perceived merits of competing stakeholder interests.

In light of this, if CAMAC were to recommend that such an amendment be made, ASIC thinks it should be drafted in a way that, to the extent possible, avoids these practical enforcement difficulties. In ASIC's view, it is important that the law contain enforceable duties, rather than vague exhortations to behave responsibly.

Should the Act require certain types of companies to report on the social and environmental impact of their activities?

Again, the question of whether the law should be amended to require some or all companies to report on the social and environmental impact of their activities is a

fundamental policy question and should be answered by the Government, not a regulator such as ASIC.

Having said this, ASIC notes that requiring companies to report on the social and environmental impact of their activities is unlikely to negatively affect ASIC's ability to enforce the law. Therefore, from ASIC's point of view, disclosure may be a better regulatory tool, than directors' duties, to shape the environmental, social and economic impact of corporate behaviour.

Disclosure also has other advantages. It is flexible and arms stakeholders with the information they need to form judgments and make decisions that reflect their own interests and values. Various stakeholders will legitimately have different opinions about what corporate conduct is socially responsible and what consequences should flow if corporate conduct is not socially responsible. In this sense, corporate social responsibility is much like corporate governance and matters of ethics. It is best addressed by transparency and in a way that promotes flexibility for individual stakeholders and corporations.

If the Government decides that the law should be amended to require all or certain types of companies to report on the social and environmental impact of their activities, then ASIC considers it is important to ensure that the disclosure is:

- meaningful to shareholders and other stakeholders – this means the disclosure must be concise; lengthy disclosures are unlikely to be read or absorbed by stakeholders. Additionally, it should be easy for stakeholders to compare disclosures by different companies. It is likely that comparability will only be achieved if there are clear guidelines on what should be disclosed,
- accurate and reliable – this may mean that disclosures should be subject to external assurance; and
- cost-effective to produce – the benefit of the disclosure must outweigh the cost of producing it.

If you want to discuss any aspect of this submission, please contact Joanna Bird on (02) 9911 2384.

Yours sincerely

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16 March 2006



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29 September 2005

The Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
Canberra ACT 2600

By email: corporations.joint@aph.gov.au

Dear Sir,

Inquiry into Corporate Social Responsibility

The Australian Securities and Investments Commission (ASIC) welcomes the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into corporate social responsibility and appreciates the opportunity to contribute to the inquiry.

ASIC would like to make brief observations relevant to issues (c) and (d) of the Inquiry's terms of reference, that is:

- the degree to which the current legal framework permits directors to have regard to the interests of stakeholders, other than shareholders, and the broader community; and
- whether revision to the legal framework are required to enable or encourage companies or their directors to have regard to the interests of stakeholders, other than shareholders, and the broader community.

The Current Legal Framework

Australian corporations laws (that is, the *Corporations Act 2001* and relevant common law principles) do not prevent corporate officers from taking into account the interests of stakeholders other than shareholders. Corporate officers are entitled to take into account the interests of a wide group of stakeholders, provided that there is some benefit

to the company from doing so. (In this context, the company means the shareholders and, in certain circumstances, the creditors.)

Additionally, ASIC notes that laws other than corporations laws often require corporate officers to consider the interests of stakeholders other than shareholders (and creditors). For example, occupational health and safety legislation, consumer protection legislation and environmental protection legislation, require corporate officers to consider the interests of a range of important stakeholders in their decision-making.

Some Reform Implications

ASIC foresees potential practical difficulties were the Parliament to amend the *Corporations Act 2001* so that corporate officers were obliged, or explicitly encouraged, to take a wide range of stakeholders' interests into account. Depending on the precise nature and drafting of any such reform these practical difficulties might include:

- Difficulties in identifying and defining the various classes of stakeholders that might be considered to have a legitimate claim on the attention and resources of companies.
- Difficulties in establishing an appropriate hierarchy of stakeholders' interests to resolve conflicting stakeholder claims on the attention and resources of companies.

These potential difficulties would impact on ASIC's ability to successfully enforce the amended provisions. The more uncertainty that exists as to the precise nature of a duty and to whom it is owed, the harder it will be for ASIC to prove, to the requisite standard, that the duty has been breached. Where a duty is owed to a number of stakeholders with varying interests, it will be challenging to establish that a given action was a breach of the duty rather than the exercise of a difficult judgment based on the perceived merits of competing stakeholder interests.

The issues raised in this submission should not be taken as endorsement of the status quo. We raise these matters because we believe that it is important to consider the implications of revising the current framework regarding corporate officers' rights and obligations to pay regard to various stakeholders in their decision-making.

Thank you for the opportunity to make this submission.

Yours sincerely
Malcolm Rodgers
Executive Director, Regulation