

# Corporations Act reform for companies limited by guarantee in 2010

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The Australian Government recently released for comment an exposure draft of the *Corporations Amendment (Corporate Reporting Reform) Bill 2010 (draft Bill)* to amend the *Corporations Act 2001 (Cth) (Corporations Act)*. Among other things the Bill proposes two significant changes for companies limited by guarantee.

## Lessening reporting and auditing obligations of companies limited by guarantee

Currently, all companies limited by guarantee are required to comply with the full reporting and auditing requirements of the Corporations Act applying to public companies, regardless of their size or financial substance. This includes the preparation of an audited financial report in accordance with the Australian Accounting Standards and a directors' report in accordance with the Corporations Act.

To reduce reporting obligations on smaller companies limited by guarantee, the draft Bill proposes to introduce a three tiered differential reporting framework for them. The three tiers and reporting obligations are outlined in the below table:

Tier	Criteria	Reporting obligations
1	Small companies limited by guarantee with an annual revenue less than <b>\$250,000</b> which do not have deductible gift recipient ( <b>DGR</b> ) status under tax legislation.	Tier 1 companies would be exempt from reporting and auditing requirements.
2	Companies limited by guarantee with an annual revenue of less than \$250,000 that have <b>DGR</b> status and companies limited by guarantee with an annual revenue of <b>\$250,000</b> or more but less than <b>\$1 million</b> irrespective of whether the company has <b>DGR</b> status.	Tier 2 companies would be required to: <ul style="list-style-type: none"><li>• prepare a financial report, which they could elect to have reviewed rather than audited;</li><li>• prepare a streamlined directors' report, rather than a full directors' report; and</li><li>• be subject to a streamlined process for distributing the annual report to members.</li></ul>
3	Companies limited by guarantee with an annual revenue of <b>\$1 million</b> or more, irrespective of whether the company has <b>DGR</b> status.	Tier 3 companies would be required to: <ul style="list-style-type: none"><li>• continue to prepare an audited financial report;</li><li>• prepare a streamlined directors' report, rather than a full directors' report; and</li><li>• be subject to a streamlined process for distributing the annual report to members.</li></ul>

## Audits and review

The current framework requires companies limited by guarantee to have their financial reports audited by a registered company auditor in accordance with Australian Auditing Standards. Under proposed provisions, companies falling within the first tier will not require an audit and companies within the second tier would be given the option to have their annual report subject to a review, rather than an audit.

A review is not as involved or costly as an audit and involves the making of enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review would not provide all of the evidence that would be required in an audit. As stated in the draft EM, the review would be conducted in accordance with a standard on review engagements developed (and modified as appropriate) by the Auditing and Assurance Standards Board and 'could be undertaken by either a registered company auditor, or a member of a professional accounting body that holds a prescribed practising certificate'.

This measure is intended to reduce the time and costs associated with having financial statements audited for smaller companies limited by guarantee.

## Streamlined directors' report

Currently all companies limited by guarantee are required to prepare a full directors' report. Under the proposed laws, companies limited by guarantee that fall within the second and third tier would instead prepare a simplified directors' report containing:

- a description of the short and long term objectives of the entity;
- the entity's strategy for achieving those objectives;
- the entity's principal activities during the year;
- how those activities assisted in achieving the entity's objectives; and
- how the entity measures its performance, including any key performance indicators used by the entity.

Small companies limited by guarantee (those in the first tier) would not be required to prepare a directors' report at all.

In addition, the simplified directors' report would contain details of:

- the name of each person who has been a director of the company at any time during or since the end of the year and the period for which the person was a director;
- each director's qualifications, experience and special responsibilities;
- the number of meetings of the board of directors held during the year and each director's attendance at those meetings;
- for each class of membership in the company, the amount which a member of that class is liable to contribute if the company is wound up; and
- the total amount that members of the company are liable to contribute if the company is wound up.

## Distribution of annual reports

Whilst the Corporations Act currently allows companies limited by guarantee to distribute their annual reports via the Internet, smaller companies limited by guarantee who may not use a website are required to send members a hard copy of the annual report.

The draft Bill proposes that companies falling within the second and third tier will be required to write to members informing them that an annual report has been prepared and how they can obtain a copy. Members wishing to obtain a hard copy or an electronic copy of the company's latest annual report can elect to obtain this from the company free of charge.

## Exception for Commonwealth Controlled Companies

Commonwealth companies (being a Commonwealth Company for the purposes of the *Commonwealth Authorities and Companies Act 1997 (Cth)* (CAC Act)), subsidiaries of a Commonwealth company or subsidiaries of Commonwealth authorities are excluded from the proposed reforms and will be required to continue to prepare a full audited financial report in accordance with accounting standards and a directors' report in accordance with the current Corporations Act. The current reporting and auditing requirements would not change for these companies, including complying with the CAC Act in respect of providing to their responsible Minister the company's financial report, directors' report and auditor's report required by the Corporations Act for a financial year, as if the company were a public company under the Corporations Act.

## Exception for 5% of members and ASIC

It is proposed that ASIC or at least five per cent of members, may direct companies limited by guarantee to prepare a financial report or a directors' report.

## Prohibiting companies limited by guarantee from paying dividends

Currently the Corporations Act does not prohibit companies limited by guarantee from paying dividends, though this is a common prohibition in many company limited by guarantee's constitutions.

The draft Bill proposes to place a prohibition on companies limited by guarantee from paying dividends. Therefore any companies limited by guarantee who do pay dividends should consider if they would need to convert to a company with share capital, such as a proprietary company.

The reduced reporting requirements of the draft Bill may lessen one of the reasons why a number of small not for profit companies have elected to remain as incorporated associations under State and Territory legislation rather than converting to public companies limited by guarantee under the Corporations Act.

The draft Bill is undergoing a public consultation process for comment.

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