



**CHARTERED SECRETARIES  
AUSTRALIA**

*Leaders in governance*

18 December 2006

Jennifer O'Donnell  
Executive Director Compliance & NSW Regional Commissioner  
Australian Securities and Investments Commission  
GPO Box 9827  
SYDNEY NSW 2001

Dear Ms O'Donnell

Deeds of cross guarantee  
ASIC Class Order 98/1481: Wholly Owned Entities

Chartered Secretaries Australia (CSA) is the peak professional body delivering accredited education and the most practical and authoritative training and information on governance, as well as thought leadership in the field. We represent over 8,000 governance professionals working in public and private companies, all of whom, due to their involvement in corporate administration and compliance, have a thorough working knowledge of the *Corporations Act*.

CSA is aware that the Parliamentary Secretary to the Treasurer has recently proposed, in the Corporate and Financial Services Regulation Review Proposal Paper released in November 2006, that the financial reporting relief for wholly-owned subsidiaries be incorporated into the *Corporations Act*.

CSA fully supports this proposal. Below we set out our thoughts on the policy objective that we believe will be served by implementing this reform. We would be keen to know if ASIC supports this reform, and to this end also set out below the practical difficulties attached to the current regime of filing deeds of cross guarantee.

We also recommend to ASIC some suggestions for reform that can be implemented immediately to provide relief for companies, given that legislative reform is unlikely to occur quickly.

In preparing this submission, CSA has drawn on the expertise of the members of its national policy committee, Legislation Review Committee.

We would be happy to meet with you to discuss these issues.

## Policy objective

The ASIC Class Order is designed to provide relief to wholly-owned entities from filing accounts. The public policy behind this mechanism is to allow a group structure to be viewed as one economic entity. The mechanism that the Class Order provides to achieve this outcome is a deed of cross guarantee between a parent company and one or more of its wholly-owned subsidiaries.

The larger question at stake in reviewing the current workings of deeds of cross guarantee is whether or not wholly-owned subsidiaries in corporate groups should be required to file separate accounts. CSA believes that the policy position and principle is, if the consolidated group files its own accounts and a deed of cross guarantee is in place, then there should be no need for the subsidiary companies party to the deed of cross guarantee to file separate accounts, because customers, creditors, suppliers etc can deal with the corporate group as one entity.

The current complexities associated with this mechanism have obscured this policy objective and ushered in other, unrelated complexities such as whether the subsidiary has filed accounts in the last three years. While it is understandable for ASIC to try to remind companies to file accounts, by meshing this unrelated requirement with the mechanism of ensuring that all subsidiaries and the parent company are treated as one entity, the original objective is hidden from view and a very significant administrative burden has been placed on a companies for little or no public benefit.

## History of Class Order

In June 2004, ASIC amended *ASIC Class Order 98/1418: Wholly Owned Entities (Class Order)*. The amendments removed the requirement that ASIC must approve the form of the executed deed of cross guarantee and included a new condition that certain certificates be given by a lawyer and auditor and be lodged with ASIC in relation to the deed. The certification by a lawyer and auditor gave rise to a number of problems and made it difficult for companies to be able to satisfy the pre-conditions for relief.

Following consultation, ASIC announced amendments to the Class Order on 20 June 2005. The amendments dealt with the level of certification required to be given by lawyer in relation to deeds of cross guarantee under the Class Order. The relevant deed of cross guarantee is in exactly the same form as the relevant ASIC Pro Forma Deed of Cross Guarantee (ASIC Pro Forma 24), and the lawyer must certify that:

- the deed of cross guarantee is in exactly the same form as the pro forma deed provided by ASIC
- the deed of cross guarantee, in relation to execution by a party that is a company, appears to be have been signed in accordance with s 127(1) of the *Corporations Act 2001*, and
- the lawyer does not know or has no reason to know that the deed has not been duly executed (even though a party may not be a company).

## Adding new entities to existing deeds of cross guarantee

Group entities will generally need to execute a new deed of cross guarantee before a new group entity can take advantage of ASIC's group accounting relief. ASIC was previously required to approve a new deed of guarantee entered into by group members. Most forms of cross guarantee provide that new group members can be joined as parties to them only under an assumption deed that has been approved by ASIC.

The amendments to the Class Order mean that ASIC will no longer approve deeds of cross guarantee and assumption deeds. The new ASIC pro forma deeds reflect this.

Therefore, to join a new group member to a deed of cross guarantee that requires ASIC pre-approval, it is necessary for all members of the group seeking to rely on the Class Order (including the proposed new group member) to enter into a new deed of cross guarantee in the current form of the ASIC Pro Forma 24.

In practice, this means that the only way in which companies can add new entities to existing cross guarantees is to revoke all existing cross guarantees and execute new ones, accompanied by a lawyer's certificate.

#### Compliance burden

Revoking existing deeds and executing new ones places an exceptionally onerous compliance burden on companies. For example, some top 200 companies can have more than 100 Australian registered wholly-owned entities, and the process involved in executing new deeds of cross guarantee for each company in the group each time an entity is added or removed consumes time, staff resources and money.

It is difficult to ascertain the policy objective that is being achieved by making it impossible to add new entities to or remove existing entities from existing cross guarantees, and forcing companies to execute new deeds of cross guarantee. We recognise that efforts have been made to deal with some of the complexities and relieve the administrative burden carried by ASIC in the process of approving deeds of cross guarantee, but contend that transferring that administrative burden to companies neither generates benefit for the people dealing with companies nor achieves the policy objective of ensuring that a group structure can be viewed as one economic entity. It also places considerable administrative burdens on companies without materially furthering the public policy objective.

For example, the certification currently required from a lawyer must note that the lawyer is satisfied that each entity has satisfied all its requirements under s 319 of the *Corporations Act 2001* in relation to the three financial years before the entity sought relief.

CSA notes that, if a company purchases a small company, it may not be aware whether the purchased company has complied with s 319 for the past three financial years. Alternatively, the company undertaking the purchase may know that the small company has not complied with all of its obligations under s 319 and still wish to purchase it.

CSA can see no benefit in ASIC seeking certification from a lawyer as to the satisfaction of an entity's requirements under s 319. CSA believes that the policy objective should be to ensure that the parent company takes responsibility for consolidated accounts and a lawyer's certification adds no value to this process.

#### Relief while legislative reform is being implemented

CSA believes that the fundamental question is whether or not subsidiaries need to file separate accounts. For those who would otherwise rely on separate accounts, the deed of cross guarantee is designed to allow them to look at the parent entity accounts.

CSA recognises that the proposed reform to the *Corporations Act* may not be implemented in the near future, given the need for public consultation on the proposal for various reforms put forward in the Parliamentary Secretary to the Treasurer's proposal paper, of which this is only one proposed reform.

CSA therefore recommends to ASIC that, until such time as financial reporting relief for wholly-owned subsidiaries is incorporated into the *Corporations Act*, the requirement for legal certification be removed immediately, with a statutory declaration signed by the company secretary of the holding entity lodged with ASIC advising the parties to the deed of cross guarantee and confirming all of the matters referred to in the current legal certification. There appears to be no benefit in providing a separate legal certification.

We further suggest that, for ease of execution, the solvency declaration be signed by the relevant company secretary following the passing of the relevant directors' resolution, rather than two directors as is currently required.

## Conclusion

Currently, the process involved in setting up a deed of cross guarantee, adding new entities to it and removing existing entities is remarkably difficult for no discernible public benefit.

The public policy objective relates to the filing of accounts, which for wholly-owned subsidiaries is dealt with when the parent company files its accounts and the directors provide the sign-off that members of the extended group can meet their obligations. The proposal put forward by the Parliamentary Secretary to the Treasurer recognises this and CSA fully supports the proposal to incorporate financial reporting relief for wholly-owned subsidiaries into the *Corporations Act*.

The government has noted that regulation is a major concern to all businesses. The Australian Government has stated it wishes to lead the way in reducing the burden of red tape to improve the economic environment further so that all businesses, large and small, can prosper and grow.

ASIC has noted in its publication *Better Regulation* that it is committed to:

- reducing the regulatory burden on business
- making its regulatory approach and processes more transparent
- minimising duplication
- better analysing the impact of what it does
- making it easier to deal with.

CSA believes that ASIC can provide immediate relief to companies in relation to deeds of cross guarantee. CSA is also keen to know if ASIC supports the proposal put forward by the Parliamentary Secretary to the Treasurer to incorporate financial reporting relief for wholly-owned subsidiaries into the *Corporations Act*. CSA believes that ASIC support of streamlining this process would assist ASIC to achieve its goal of reducing the regulatory burden on business.

As noted at the start of our submission, we would be happy to meet with you to discuss these issues.

Yours sincerely

Tim Sheehy  
CHIEF EXECUTIVE