

30 January 2012

The Manager
Corporate Reporting and Accounting Unit
Corporations and Capital Markets Division
Australian Treasury
Langton Crescent
PARKES ACT 2600

Email: corporatereportingreforms@treasury.gov.au

Dear Sir or Madam

Re: Submission to the Treasury, Discussion Paper – Proposed amendments to the Corporations Act (Test for payment of dividends)

We refer to the Australian Treasury's Discussion Paper in relation to proposed amendments to the dividends test following the new reforms under the *Corporations Amendment (Corporate Reporting Reform) Act (No.66) 2010* (Cth).

1. Application of section 254T(1)(b)

In accordance with the new section 254SA of the *Corporations Act 2001* (Cth) ("Corporations Act") a company limited by guarantee incorporated on or after 28 June 2010 must not pay a dividend to its members. Section 254SA of the Corporations Act will only apply to companies limited by guarantee incorporated on or after 28 June 2010. Therefore, a company limited by guarantee incorporated before 28 June 2010 may still pay a dividend to its members by applying the dividends test set out in section 254T(1) of the Corporations Act.

By virtue of section 254T(1) a company must not pay a dividend unless:

- (a) the company's assets exceed the liabilities immediately before the dividend is declared; and
- (b) the payment of the dividend is fair and reasonable to the company's shareholders as a whole; and
- (c) the payment of the dividend does not materially prejudice the company's ability to pay its creditors.

Although a company limited by guarantee can test for the requirements set out in sections 254T(1)(a) and (c) above, a company limited by guarantee cannot test the requirement in section 254T(1)(b).

A company limited by guarantee has members who each hold an interest in the company instead of holding shares. As the requirement in section 254T(1)(b) only makes reference to what is fair and reasonable to "shareholders", it raises the following possibilities of whether a company limited by guarantee should:

- (a) ignore this requirement; or
- (b) automatically fail from paying dividends because they cannot test this requirement; or
- (c) assess the requirement in the context of members, not shareholders.

2. Definition of "shareholder"

Item 9.1 of the *Corporations Amendment (Corporate Reporting Reform) Act (No.66) 2010* (Cth) states that dividends are payments to shareholders. The Corporations Act does not provide guidance about, or a definition of, the term "shareholder".

A shareholder is commonly defined as a person registered in a company's register of members as the holder of shares (*Minsoul Pty Ltd v FCT* (1974) 3 ALR 251;48 ALJR 283). It does not include an unregistered beneficial owner (*Federal Commissioner of Taxation v Patcorp Investments Ltd* (1976) 140 CLR 247;10 ALR 407).

Based on the above it would be reasonable to suggest that a member of a company limited by guarantee is not the same as a shareholder as the members of a company limited by guarantee cannot hold shares.

3. Conclusion

It is unclear whether a company limited by guarantee incorporated prior to 28 June 2010 may now be able to pay dividends to its members, as it cannot satisfy all three tests in section 254T. Alternatively, it is unclear whether a company limited by guarantee may disregard the requirement set out in section 254T(1)(b), as it cannot test whether a dividend payment would materially prejudice shareholders.

Although the discussion paper suggests that the new provision is supposed to operate as an exception to the maintenance of capital rules, the provision is actually drafted as a prohibition on payment of a dividend unless all three tests are met.

We believe the new legislation needs to provide further clarity on the interpretation of section 254T(1)(b) to the extent the test would apply to companies limited by guarantee.

Given the grandfathering provision, we believe it is an unintended consequence, due to drafting oversight, that companies limited by guarantee would automatically fail the test and therefore, would be prohibited from paying a dividend. We benefit from the grandfathering provision and accordingly, require certainty as to the proper application of this test prior to

the payment of a dividend to our members.

Yours faithfully,



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General Counsel and Company Secretary

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