

Review of the Governance Provisions in the

Gaming Machine Act 2004

Issues Paper

April 2010

Contents:

1. Background to the Review.....	1
1.1 Introduction.....	1
1.2 Conduct of the Review.....	1
1.3 Consultation Process.....	2
1.4 How to make a submission	2
2. Current Framework – Clubs and Associated Organisations.....	3
2.1 What is a club?.....	3
2.2 Benefits of club status	3
2.3 Principles of establishing an eligible club.....	4
2.4 Club governance	4
3. Risks and Responsibilities	6
3.1 Club governance risks.....	6
3.2 Responsibilities of club directors.....	6
3.3 Responsibilities of club members	7
3.4 Role of the gaming regulator	7
4. Possible Approaches to Governance Provisions.....	8
4.1 Status quo – rely on existing provisions in corporations law	8
4.2 Amend the governance provisions in the <i>Gaming Machine Act 2004</i>	9
4.3 New regulatory powers to require changes to constitutions	10
5. Other Governance Issues	10
6. Next Steps.....	10

1. Background to the Review

1.1 Introduction

The *Gambling and Racing Control Act 1999* provides for the Gambling and Racing Commission (the Commission) to review the ACT's gaming laws as part of its functions. In reviewing such legislation, subsection 8(1) of the *Gambling and Racing Control Act 1999* requires the Commission to consult the community.

On 2 March 2010 the Minister for Gaming and Racing requested that the Commission review the provisions in the *Gaming Machine Act 2004* (the GMA) relating to the governance of clubs. This followed the Commission's report on its investigation into possible breaches of the GMA by the Canberra Labor Club Ltd in respect of the proposed sale of the Canberra Labor Clubs.

The Minister requested that the review should cover, but not necessarily be limited to:

- whether the Commission should have powers to require changes to a licensee's Memorandum and Articles of Association where they conflict (or potentially conflict) with the GMA;
- clarifying the relationship between clubs and their associated organisations in terms of the rights, powers and obligations of the associated organisations; and
- the operation of the club control aspects of the GMA in relation to relevant aspects of the Corporations Law (C'th).

The Commission has decided that it would be appropriate to include in the review consideration of other governance matters contained within the GMA such as sections 13, 14, 53, 55, 145 and 146. Many of these provisions are designed to ensure that clubs are established and operated for the benefit of members generally and not for commercial or private gain.

Therefore the Commission is seeking comment or feedback from stakeholders on these or any other provisions that relate to the governance of clubs.

1.2 Conduct of the Review

The review will focus on the efficacy and appropriateness of the governance provisions for clubs in the GMA.

The conduct of the review will be consistent with the ACT Government's commitments under the Council of Australian Governments to regulatory reform. These commitments recognise that effective regulation is essential to ensure markets operate efficiently and fairly and to protect consumers. However, the benefits from each regulation must not be offset by unduly high compliance and implementation costs or restrictions on competition.

1.3 Consultation Process

There will be two stages of consultation as part of this review. In the first instance the Commission is seeking feedback and comments from the community on the issues and approaches outlined in this paper.

The second stage of consultation will be a shorter targeted process with industry that will occur once the Commission has analysed first stage submissions and has developed draft conclusions as part of its review.

The Commission's recommendations will ultimately be forwarded to the Minister for consideration and it will be a matter for Government whether or not the recommendations are adopted, modified or rejected.

1.4 How to make a submission

Submissions may be presented in hard copy, in disc form or by email, however electronic submissions are preferred. For accessibility reasons, please use Word or RTF format. (An additional PDF version may also be submitted.) Submissions must include a contact name and address.

Arrangements can be made to accept submissions from persons who are unable to express their views by any of these means.

The Commission will make submissions publicly available unless you specifically indicate that you would like all or part of your submission to remain in confidence.

CLOSING DATE FOR SUBMISSIONS: COB 11 JUNE 2010

Email: grc@act.gov.au

Post: Chief Executive
ACT Gambling and Racing Commission
PO Box 214
CIVIC SQUARE ACT 2608

Inquiries: Inquiries can be directed to Jane Nielson on 02 6207 2086

2. Current Framework – Clubs and Associated Organisations

The Commission considers that the essential characteristics and fundamental requirements for establishing and operating a club are central to a review of club governance arrangements.

2.1 What is a club?

A club is a group of like-minded people that wish to pursue a common social purpose. A club is a not-for-profit organisation focused on providing facilities for its members. As a club is established for the benefit and purposes of its members, the club's operations must be conducted in a democratic manner that provides for an equitable distribution of benefits to all members.

Clubs operate as not-for-profit mutual entities. Under the mutuality principle, members contribute to a common fund created and controlled by them for a common purpose.

The GMA defines a club as:

a corporation established for the benefit of members to achieve eligible objects.

2.2 Benefits of club status

In addition to access to gaming machines as not-for-profit community organisations, clubs benefit from a number of tax concessions. Significantly, the principle of mutuality provides substantial benefits in the form of income tax exemptions. The extract below from the ATO guidelines for registered and licensed clubs describes how and why the principle of mutuality applies to clubs.

The principle of mutuality provides that where a number of persons contribute to a common fund created and controlled by them for a common purpose, any surplus arising from the use of that fund for the common purpose is not income. This principle, of course, does not extend to include income that is derived from sources outside that group. Where the principle aim of a Club is to provide and improve facilities to its members, the principle of mutuality will apply to all transactions between that club and its members.¹

Clubs also benefit from a lower gaming machine tax rate compared to hotels and taverns under the GMA. The smaller clubs with monthly gross gaming machine revenue below \$15,000 do not pay any gaming machine tax.

¹ Extract from the ATO Guidelines for registered and licensed clubs available at http://ato.gov.au/nonprofit/content.asp?doc=/content/17832.htm#P24_1633

2.3 Principles of establishing an eligible club

To obtain a gaming machine licence in the ACT clubs must be “eligible” clubs as defined by the GMA. For the purposes of this review, the relevant elements of this definition are that clubs must:

- be incorporated (either as a corporation under the *Corporations Act 2001* or as an incorporated association under the *Associations Incorporation Act 1991*);
- have eligible objects as their main objects;²
- be conducted mainly to achieve their eligible objects; and
- keep and maintain the club and its facilities for the benefit of members generally.

These provisions ensure that only not-for-profit organisations which have been established for a common purpose for the benefit of members may operate gaming machines. This is the core of the community gaming model in the ACT – the revenue from gaming machines must be returned to the community through the services and facilities provided by clubs to their members and more broadly through contributions to community organisations.

2.4 Club governance

In general terms, governance refers to the system through which an organisation is directed and controlled. It includes the mechanisms through which the people who control the organisation are appointed and held to account in running the organisation effectively and efficiently. Transparency and accountability are important concepts in good governance.

Relevant to this review, the governance of a club refers to the mechanism by which directors are selected and appointed, whether it is by the voting membership or by direct appointment through an associated organisation. Also relevant to a club’s governance arrangements is how many of its members are voting members and therefore have a say in the nomination and selection of directors.

2.4.1 Role of the membership

The membership of a club is the fundamental foundation of the organisation. It is the reason that a club exists ie to provide benefits to those that join so that they can enjoy or achieve their common purpose.

While the members of a club must ultimately control their organisation, the membership structure, such as the classes of membership, can have a significant influence on how this is achieved.

Although some clubs have what might be termed a “democratic” approach to the voting rights of their membership, this is not a requirement of the GMA. The GMA only requires that a club has at least 300 voting members.

² Eligible objects are outlined in Section 145 of the GMA and include anything that furthers or promotes recreation, social, religious, political, literary, scientific, artistic, sporting or athletic purposes and cultural or educational purposes.

Many clubs significantly restrict the number of eligible voting members. For example, it is not uncommon for clubs with a total membership in the tens of thousands to have only a few hundred members with voting rights. The Commission understands that people joining clubs as social or ordinary members are usually aware that they will not have voting rights. In this context it is fair to say that many people who join a club may not want to participate in the governance of that club but merely wish to utilise the club's social facilities.

2.4.2 Role of associated organisations

The GMA provides for certain approved external parties, defined as associated organisations, to have a significant influence over the governance of a club. For example, associated organisations can control the appointment and removal of a club's directors. Associated organisations may also have rights in relation to approving changes to a club's constitution. In corporate terms, clubs can operate as subsidiaries of their associated organisation.

Associated organisations must be established under the same organisation principles as the club itself, including having eligible objects. To be approved as an associated organisation the organisation must be associated with the club and the Commission must be satisfied that its approval would help the club to achieve its eligible objects.

Allowing an external party to have this kind of control is designed to protect the purpose or objects of the club by preventing a takeover that may result in a change to the club's original purpose.

The rationale for permitting this governance model is based on the fact that the club and the approved associated organisation would essentially have the same objects or purpose and therefore would be striving for the same goals. As outlined below, this rationale may not always be valid.

3. Risks and Responsibilities

3.1 Club governance risks

The GMA currently allows for a club's board to be appointed by the approved associated organisation rather than the voting membership of the club. This situation gives rise to the problem being examined in this review. It is possible that a club and its associated organisation may have a significant disagreement or conflict over a particular matter or competing interest. In these circumstances, directors who have been appointed by the associated organisation (and in particular who can be removed or sanctioned in some way by that organisation) may experience significant pressure to act in a way that they may consider is not in the club's best interests.

In this regard, there is a possible risk to a club board's compliance with the requirement in the GMA³ to have complete control over the club's business or operations and the requirements under corporations law⁴ for directors to act in the best interests of the club (where the club is a corporation).

The governance provisions contained in the GMA and those in corporations law should be complementary and work together to ensure the appropriate operation and control of club corporations. It is felt by the Commission that some of the GMA governance provisions as currently drafted do not enhance or encourage the achievement of some of the governance goals that are being sought by corporations law.

Some consider that the current GMA governance provisions significantly add to the risk that directors may not perform their duties to the club as they should and may leave them vulnerable to prosecution under corporations law.

In addition, the current system involving associated organisations and restricted voting eligibility could be considered less transparent and less democratic than contemplated by the best practice set up of a club as a not-for-profit mutual entity established for the benefit of its members.

3.2 Responsibilities of club directors

The issue of control over a corporation's Board of Directors occurs not only in the Territory's club industry but more broadly in the corporate sector. While there are some unique elements to this issue in terms of particular provisions in the GMA, the issue of external influence is an issue for all corporate boards. Corporations law clearly recognises this and enshrines a duty of care and loyalty on directors which includes the requirement for directors to exercise their powers and discharge their duties in good faith and in the best interests of the particular corporation on behalf of which they are currently exercising their decision making powers.

³ See Section 14(1)(h) of the GMA.

⁴ See Part 2D.1, Division 1 of the *Corporations Act 2001*.

The lobbying of directors and attempts to influence their decision making are all part of normal corporate activity. However, an issue arises where a director is placed in a position where their responsibilities conflict and in discharging their responsibilities to the associated organisation they may be forced to act in a way or take into account matters that may not be in the best interests of the club.

Of key relevance to this review, the GMA can currently allow situations to arise where conflicts may develop between a club's board and the associated organisation due to potential competing interests. As noted above, this can place significant pressure on directors of a club's board to make decisions that are not consistent with the GMA and may potentially breach corporations law in relation to their fiduciary duties.

3.3 Responsibilities of club members

As outlined in Section 2.4.1 of this Paper, members are the foundation of a club. Members of a club, as opposed to the shareholders of a company, usually have their liability for a club's debt limited to the member's subscriptions payable under the club's constitution or Articles. Therefore members typically do not have the responsibility to cover a club's debts and obligations. However, club members do not have access to the proceeds of the sale of assets or surplus funds in the event of the club winding up.

In relation to the role of members in a club's governance, it is acknowledged that a common difficulty faced by many clubs is the general apathy of members in relation to participation in club governance matters.

However, the important issue from a governance perspective is that the membership has the opportunity to have a say in the governance of their club. Members therefore have a responsibility to exercise their voting rights if they are sufficiently interested in the operations and management of their club.

3.4 Role of the gaming regulator

The ACT Gambling and Racing Commission as gaming regulator in the Territory has a role to ensure the enforcement of the GMA including the various provisions relating to club governance. The Commission has little power to influence club governance other than to undertake disciplinary action or prosecution for specific breaches of the GMA.

There may be an argument for greater powers in this area as a means of preventing breaches of the GMA.

It should be noted that responsibility for compliance in relation to corporations law remains with the Australian Securities and Investments Commission and corporations law itself is not part of this review.

4. Possible Approaches to Governance Provisions

The Commission is considering the efficacy and appropriateness of the governance provisions for clubs in the GMA and whether any changes to these provisions are required. The overarching policy objective is to ensure that the regulatory provisions in the GMA support the good governance of clubs, which includes transparent club management arrangements and decision processes to the extent that these are feasible and appropriate.

The Commission is seeking feedback and comments on alternative approaches some of which are outlined below. The Commission is particularly interested in any information from stakeholders about the impacts such as costs, benefits and any potential unexpected consequences of the approaches.

The approaches outlined below, including the option of no change, are not the only possibilities but have been raised as matters for consideration and comment. They cover the various roles from a governance perspective of club directors, club membership and the gaming regulator. Alternative approaches are also possible and comments are sought on these as outlined in Section 5 of this Paper.

4.1 Status quo – rely on existing provisions in corporations law

While the GMA requires a club board to have complete control over the club, the status quo relies on director knowledge and the significant personal penalties under corporations law to ensure proper governance.

As noted above, corporations law requires directors to exercise their powers and discharge their duties in good faith and in the best interests of the corporation. This is a civil obligation and it is also a criminal offence for a director to fail to act in this manner.

A significant majority of the current club licensees are corporations and are therefore covered by these requirements. However it is not a requirement that licensees are corporations under the Corporations Act and 14 of the current 60 licensees are incorporated associations and therefore not subject to corporations law.

Maintaining current arrangements as outlined under this approach would not change the existing requirements regarding the transparency of club management arrangements and decision processes. The current approach would also continue the existing relationship between the GMA governance provisions and corporations law.

4.2 Amend the governance provisions in the *Gaming Machine Act 2004*

An alternative approach to club governance would be to amend the GMA to require clubs to have truly independent boards appointed by the voting membership, with all members afforded equal capacity to become voting members. This would directly address the risks created by the current governance framework and mean that associated organisations (or a small percentage of members) could not appoint or remove directors of a club.

A number of clubs already use these appointment arrangements often with the entire membership having voting rights. The Commission is aware, however, that some clubs may be concerned that such changes could enable the objects of a club to be changed too easily. For example, if enough of the voting membership wanted a “rugby league” club to become a “soccer” club, then in the absence of any restrictions on changing the objects, this could occur.

Feedback is therefore sought from stakeholders on what further changes, if any, were desirable or necessary to protect the major or core objects of the club if the above changes removing the role of associated organisations were made.

For example, the GMA could:

- prohibit changes to the core objects unless they were agreed by a majority of voting members at two or three successive AGMs; or
- provide for a class of objects (such as core objects) that once a club is established could not be changed (except after a transfer of licence). Secondary or lower order objects could be changed by the membership through changes to the Memorandum or Articles of Association.

It would also hold that an external party could not have any power relating to the change of a club’s constitution or Memorandum and Articles of Association. This could only be undertaken by voting members.

The Commission notes that the NSW Independent Pricing and Regulatory Tribunal (IPART), as part of its 2008 review of the Registered Clubs Industry in NSW, considered that clubs should be encouraged to remove restrictions on board membership and voting eligibility from their constitutions. IPART recommended that a model club constitution template be developed which did not contain any board membership or voting eligibility restrictions.

IPART recognised the concern of some clubs that these changes to a club’s constitution could result in a club’s core features (or objects) no longer being protected. To address this, IPART proposed another way of protecting a club’s core objects that would see the core features of the various types of clubs (for example “RSL clubs” or “leagues clubs”) being defined in legislation.

4.3 New regulatory powers to require changes to constitutions

The role of the gaming regulator could be enhanced to provide for powers that would allow the Commission to require changes to a licensee's Memorandum and Articles of Association where they conflict (or potentially conflict) with the GMA. The purpose of such an intervention would be to minimise the risk that a club's governance arrangements resulted in non-compliance with the GMA.

This approach, which could be used in conjunction with other measures, could be utilised where there is a power in a constitution which if exercised would be a breach of the GMA. For example, if a club's constitution allowed an external body to overrule decisions of the club's board of directors; or if a club's constitution provided for non-members that weren't signed in and accompanied by a member to play gaming machines.

The exercise of this power by the Commission would be a reviewable decision and clubs would therefore have the right to seek an independent review of such a direction.

This approach does not change existing requirements regarding the transparency of club management arrangements and decision processes for clubs generally, although it does provide a means for the Commission to respond to individual situations that are brought to the Commission's attention.

5. Other Governance Issues

In addition to comments on the above possible approaches, the Commission welcomes feedback on any other possible approaches and/or other governance issues that may be impacting on the operation or control of clubs in the ACT. The Commission is also seeking submissions on any other proposals which stakeholders consider would improve or enhance the current governance arrangements.

6. Next Steps

The Commission will draw on stakeholder submissions in developing the findings of its review and will consult with industry on the draft conclusions. The final review report will include an assessment of the relative advantages and disadvantages of each proposal against the overarching policy objective of ensuring that the regulatory environment for clubs supports good governance.
