Department of Industry

Liquor & Gaming

Review of Club Amalgamation and De-Amalgamation Framework

Review Report – August 2017

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Executive Summary

The NSW registered club laws provide a framework for registered clubs to amalgamate (merge) and de-amalgamate (de-merge). Mergers and de-mergers are regulated under the *Registered Clubs Act 1976*, the *Liquor Act 2007*, and the *Gaming Machines Act 2001.* Clubs must also adhere to relevant requirements under the *Corporations Act 2001* (Cth).

The 2014 Memorandum of Understanding (MOU) with ClubsNSW – *Resilient Clubs, Resilient Communities* – committed the NSW Government to a review of the State's merger and de-merger requirements, with a view to streamlining these processes. This was aimed at helping clubs more readily merge and de-merge as their local situation requires.

Liquor & Gaming NSW (L&GNSW) completed the Review in August 2017. It primarily focussed on opportunities to streamline the merger and de-merger processes, in line with the Government's MOU commitment. It also considered the suitability of related controls that aim to promote transparency and protect the interests of club members and local communities.

The Review included the release of a discussion paper on 28 June 2017 and call for public submissions by 26 July 2017. Seven submissions were subsequently received, including from ClubsNSW, the Independent Liquor & Gaming Authority (ILGA), law firm Thomson Geer and four club members. L&GNSW also met with key stakeholders, including ClubsNSW.

The Review found that the merger and de-merger frameworks are largely meeting their objectives. However, some improvements could be made to make both processes less onerous on clubs by reducing red tape to lessen the associated costs and time.

In particular, a number of amendments have been identified to remove some regulatory barriers so clubs can more flexibly and proactively consider and pursue mergers that suit their local needs. If implemented, these changes could make mergers more accessible and attractive, helping to preserve key social and leisure facilities for communities across NSW.

This will assist clubs in the current environment, where it has been reported that a large proportion are experiencing financial distress (approximately 33 per cent according to a 2015 NSW club census). The Review considers there is a compelling case to improve the existing frameworks to encourage further industry consolidation that help sustain clubs, the jobs they provide and other benefits for the NSW economy.

Recommended amendments to improve the merger process include:

- ***Recommendation 1: Make it easier for clubs to merge with others from further afield*** – remove restrictions under Section 17AH(1) of the Registered Clubs Act, and clause 4 of the Registered Clubs Regulation, so that a club can initially call for expressions of interest (EOIs) and later choose any merger partner – including beyond their immediate local area (i.e. within 50km) – if they consider it suits their needs.
- ***Recommendation 2: Support clubs to proactively pursue mergers*** – amend clause 4 of the Regulation to clarify that clubs may enter into preliminary discussions about potential mergers before a call for EOIs is made; and to introduce a transparent process to enable clubs to submit an unsolicited EOIs to other clubs at any time.
- ***Recommendation 3: Adjust the existing 10 club amalgamation limit*** – adjust the restriction under section 17AF of the Registered Clubs Act to provide that the limit of merging with 10 clubs refers to 10 clubs at any point in time, rather than a cumulative maximum total of mergers that a club can undertake in its lifetime.

With these proposed changes, it is important there is a balanced approach that continues to recognise clubs are community-owned and operated for the benefit of their members. In this regard, the Review found existing controls can be strengthened to ensure mergers and de-mergers are conducted transparently and in the interests of club members.

More could be done to help clubs make firmer agreements about what will happen to major assets in mergers (such as a dissolved club's premises) and to transparently convey associated risks so members are well informed before approving a merger. This will help clubs set expectations around mergers, limiting unexpected predatory behaviour and 'asset stripping' by larger clubs.

Recommended amendments to strengthen protections for members include:

- ***Recommendation 4: Enable clubs to agree to longer, enforceable periods for maintaining assets of 'dissolved clubs'*** – amend section 17AI of the Registered Clubs Act to enable clubs to agree that major assets of a dissolved club must remain intact for longer than the current maximum period of 3 years.
- ***Recommendation 5: Require a MoU to address risks and treatments relating to major assets*** – amend clause 7 of the Regulation to require clubs to specify in a MOU the risks associated with undertakings about major assets and their intentions about how they will be treated.

The Review also identified various other changes to address potential inconsistencies with corporations law and improve the processes for the determination of club transfer applications that underpin mergers and de-mergers by ILGA (the final step in the merger/de-merger process). The related recommended changes include:

- ***Recommendation 6: Better facilitate club 're-amalgamations'*** – streamline the process for a club to re-amalgamate with a new parent club by enabling the direct transfer of a club's licence from one parent club to another, while retaining sufficient controls to promote transparency and protect member interests.
- ***Recommendation 7: Undertake a further review of club membership issues*** – examine the operation of sections 17AC(2) and 17AN of the Act and their relationship to corporations law, with a view to addressing any ambiguities or potential inconsistencies.
- ***Recommendation 8: ILGA to determine merger and de-mergers within 120 days*** – ILGA should continue to seek to process licence transfers for club mergers and de-mergers within 120 days, inclusive of the 30-day public submissions period.
- ***Recommendation 9: Ensure ILGA has the information it needs to make decisions*** – identify practices, in consultation with ILGA and the club industry, to better inform ILGA about how a proposed merger or de-merger complies with statutory requirements, while seeking to minimise extra time and costs for clubs.

The nine recommendations outlined above are targeted at ensuring the merger and de-merger frameworks continue to deliver on their objectives in a more refined manner.

Collectively, the proposed reforms could provide clubs with more freedom to consider and settle mergers and de-mergers to suit their local needs, within a framework that offers strengthened transparency and protections for members. This would help to underpin a more sustainable and resilient club sector in NSW.

Key Findings & Related Recommendations

FINDING 1 – While the policy objectives of the legislative framework for club mergers and de-mergers remain valid, there is scope to improve its operation.

Club industry feedback to the Review confirmed the framework has largely been meeting its objectives. Since provisions enabling clubs to merge were introduced under the Registered Clubs Act over 30 years ago, many clubs have successfully merged.

Mergers have helped many clubs to avoid closure, preserving important social and leisure facilities for their members and local communities. Industry feedback also noted they have been used effectively by clubs to build offerings to members; share staff, expertise and resources; respond to competitive pressures; and leverage increased bargaining power and economies of scale.

Since 2007, 63 clubs have reportedly merged and survived. Yet over the same period, 114 clubs also closed, with regional clubs representing half of these.

The industry's peak body, ClubNSW, highlighted many more clubs are facing viability challenges, with its 2015 NSW club census showing approximately 33 per cent of clubs are experiencing financial distress.

The same census also found that 78 clubs, or 72 per cent of clubs that commenced a merger, failed to complete the process. ClubsNSW suggested this has been due to a range of cultural, commercial and regulatory barriers to the club amalgamation process.

Some barriers are difficult to address, particularly those relating to cultural differences between clubs. However, the Review considers some amendments can be made to regulatory framework make the merger process easier, less time consuming and costly, and more flexible for clubs.

The Review also found more can be done to ensure mergers and de-mergers are conducted transparently and in line with relevant statutory requirements. Certain controls can also be strengthened to respond to core concerns of smaller clubs seeking to merge about what will happen with a club's major assets following a merger.

Stakeholder feedback to the Review also indicated that the de-merger provisions introduced in 2011 have helped clubs de-merge in a controlled manner. However, the process for a child club seeking to de-merge and then re-merge with a different parent club is overly onerous and should be streamlined.

FINDING 2 – There should be greater incentives for clubs to merge including more flexibility to proactively seek and negotiate mergers as their needs require, with regulatory barriers removed where appropriate

Industry feedback to the Review suggested industry consolidation via mergers should be encouraged, particularly in light of the viability issues affecting a large proportion of clubs. ClubsNSW considers this to be vital to ensuring a sustainable club industry in NSW.

The Government's 2014 MOU commitment also recognised the process should be streamlined so clubs can more readily merge and de-merge as their local situation requires.

In this context, the Review identified opportunities to streamline the merger process and provide clubs with more freedom to seek out and negotiate mergers. A diagram of the proposed future merger process is provided at Appendix 1.

In its submission to the review, ClubsNSW proposed the introduction of a five-year 'tax holiday' for newly merged clubs where a child club had past gaming machine revenue of less than $1 million (and as such, currently pay no tax). It is suggested such an arrangement would help to lift the overall viability of smaller, struggling clubs by incentivising stronger

clubs to merge and make the substantial investments needed to improve their operations and revenues.

It was suggested the tax holiday would particularly benefit clubs that are financially weaker and hence experience greater difficulty in attracting merger partners. Given these small clubs currently pay no tax, further examination of the proposal could be undertaken to assess relative risks and benefits.

Recommendation 1 – Make it easier for clubs to merge with others from further afield

Remove restrictions under Section 17AH(1) of the Registered Clubs Act, and clause 4 of the Registered Clubs Regulation, so that a club can initially call for expressions of interest (EOIs) and later choose any merger partner – including beyond their immediate local area (i.e. within 50km) – if they consider it suits their needs.

The policy intent of the 50km rule was to foster mergers between nearby and like-natured clubs, to help ensure important social and leisure facilities remain accessible to both clubs' members and the local community. It requires any club contemplating a merger to first call for EOIs and then consider potential merger partners within 50km. Where a local merger is not possible, they can look across NSW for suitable clubs with similar objectives / activities. If none are identified, clubs with different objectives / activities can be considered.

In practice, the Review found little evidence to suggest mergers between clubs located farther away, or not of a like nature, should always be a last resort. In fact, the Review was alerted to 15 examples of successful mergers between clubs that operate sites outside the 50km radius.

A notable example included the Mingara Leisure Group, which has five club sites spanning from the far north of NSW to Sydney's southwest. Industry feedback suggested the Group has shown a strong commitment to maintaining local community assets and improving the financial viability of its partner club sites.

Whether or not there will be additional risks around the preservation of a club's facilities will be highly dependent on its individual circumstances and the clubs involved in a merger.

ClubsNSW notes that in the case of local mergers, the limited pool of revenue and members in a particular area can drive predatory behaviour. Local parent clubs may merge with another club and, after a few years, close it down while retaining all members. As a result, some clubs may prefer to seek merger partners across NSW at the outset, rather than being required to look for partners locally first.

Additionally, the 50km rule can also present a barrier to clubs finding a suitable merger partner in a timely fashion. In remote towns, viable partners inside a 50km radius can be scarce, particularly one with the necessary resources to invest in turning around any that are struggling financially.

Removing the 50km rule will mean a club has more flexibility to make its own decisions at the outset about how and where to find potential merger partners. Similarly, clubs are best placed to consider whether merging with a club with similar objects is preferable. Club industry feedback suggested clubs may at times prefer to merge with others that can offer something different to members through the facilities and services they provide.

Importantly, existing member protections and requirements for potential mergers will continue. For example, members of a club contemplating a merger need to approve of it at an Extraordinary General Meeting, taking into account associated benefits and risks articulated in a MOU. This will include any risks relating to the club operating more remotely or not having similar objects. ILGA also needs to be satisfied that the merger is in the interests of the members of each club.

Rather than completely removing the EOI requirement, the Review considers clubs should still be required to undertake an EOI process but have a choice about whether they only call

locally within 50km or across a broader area. This will ensure clubs contemplating a merger appropriately canvass and consider a variety of merger options (and associated benefits, costs and risks) before putting a formal merger proposal to members.

Recommendation 2 – Support clubs to proactively pursue mergers

Amend clause 4 of the Regulation to clarify that clubs may enter into preliminary discussions about potential mergers before a call for EOI is made; and to introduce a transparent process to enable clubs to submit an unsolicited EOIs to other clubs at any time.

Currently, a call for EOIs from clubs in the same area must occur before any 'agreement' or 'understanding' to merge with another club is reached.

Industry feedback suggested this requirement can hamper merger activity, because club directors fear that a preliminary or informal discussion about a merger may be deemed an 'understanding', placing them in breach of the requirement. Some have also received legal advice advising against entering into any discussions with other clubs.

Purportedly, the requirement can also discourage mergers because some club directors can be reluctant to disclose their club's financial situation by publically calling for EOIs, without first being able to explore and advise members about potential merger opportunities.

The Review notes that it was not intended that preliminary discussions would be prohibited under the existing arrangements, and there is no compelling reason why this practice should be banned. It is reasonable to consider that such discussions could help club directors demonstrate they are taking investigatory steps with a view to managing and securing the future of their club, before 'going to market' with a formal call for EOIs.

The Review also considers that a club should also be permitted to make an unsolicited EOI to another at any time so they can more proactively express their interest in merging. This could encourage clubs to proactively convey what they can offer, including any potential benefits, in a relatively informal and non-threatening manner.

However, it would be important to balance this new freedom with appropriate controls to ensure transparency to members. Where a club receives an unsolicited EOI for a merger, clubs should be required to notify their members at the next annual meeting of these proposals received in the last 12 months. If the club wishes to pursue a merger, it should also be required to disclose all EOIs received in the past 12 months when a MOU is put to members for approval.

Recommendation 3 – Adjust the existing 10 amalgamation limit

Adjust the restriction under section 17AF of the Registered Clubs Act to provide that the limit of merging with 10 clubs refers to 10 clubs at any point in time, rather than a cumulative maximum total of mergers that a club can undertake in its lifetime.

Clubs are currently prevented from merging more than 10 times. This aims to prevent club groups growing too large and becoming disconnected from their local communities.

The Review notes that this requirement has previously been relaxed from the original limit of four to the current limit of 10, and that this occurred in recognition that several club groups had reached the original limit and were in a position to merge with further clubs.

Stakeholder feedback suggests that the current approach unnecessarily constrains some merger activity, because it means a club that completes 10 mergers is prevented from ever merging again despite their being compelling or positive reasons to do so. With the introduction of the de-merger provisions in 2011, club groups can also now significantly reduce in size yet still be prevented from growing again within the cap.

An example includes the Panthers Group, which has reached the cap, but now only operates six other sites following a series of past de-mergers. Despite this, and its potential ability to

undertake other mergers to the benefit of other clubs, it is prevented under the current arrangements.

Therefore, the Review considers the cap can be adjusted to allow clubs to be merged with up to 10 others at any one time. Importantly, this will still ensure the stated intent of the cap is preserved, while allowing clubs to make critical decisions about sites without fear affecting future merger activity.

FINDING 3 – Merging clubs ought to be able to agree to longer enforceable periods for preserving the assets of a 'dissolved club' for members and local communities

Protections exist under the current framework to discourage predatory behaviour (e.g. asset stripping by larger clubs) whereby the major assets of a dissolved club in a merger must generally be kept intact by a parent club for three years following a merger, unless the disposal is approved by members and ILGA. Major assets include the core property – premises, facilities used by members and guests, and other property that has been declared by resolution to be core property.

ILGA can only approve of the disposal if satisfied it is necessary to ensure the financial viability of the parent club, and it has been approved by most of the dissolved club's members. This additional safeguard operates to ensure the dissolved club's members are supportive of the sale and that it is needed to ensure the parent club can stay afloat.

The Review notes that these provisions have largely worked as intended to preserve club assets. However, stakeholder feedback suggested there is a need for increased protection in certain circumstances; particularly where merged clubs are of the understanding they have negotiated a longer asset preservation period than the mandatory three years.

For example, some mergers have included undertakings in MOUs for major assets to be preserved over a period greater than the existing three year requirement.

This was highlighted in a recent high profile dispute between the Easts Group and the Waverley Bowling Club, which merged in 2009. In this case, the Review was advised that the MOU contained several undertakings that sought to ensure the preservation of the Waverley Bowling Club premises for a period of 20 years, unless the ongoing financial viability of the Club was at risk. It also indicated the MOU contained undertakings committing Easts Group to invest in the Club to ensure its success. Despite this, claims were made that undertakings were not being honoured when a proposal to sell that Club site was later put forward.

While the Review notes that clubs are free to commit to these types of undertakings, there appears to be a high level of uncertainty about the degree of enforceability of MOU commitments to preserve major assets beyond the statutory three year period. The members of dissolved club, which no longer exists as its own corporate entity, have little means to seek to enforce the MOU commitments without access to the same resources or backing as the larger parent club or club group.

Additionally, ILGA has no statutory obligation or power beyond the mandatory three year period to approve of the disposal of major assets where a commitment to preserve them for a longer period is specified in a MOU.

While the Review did not seek to examine or address the specific circumstances that applied in the above dispute, it is recognised that a core concern of smaller clubs merging with larger clubs is that their core assets remain available for use by members and the local community.

Therefore, the Review considers an opportunity exists in future to help clubs merging have more certainty about the enforceability of undertakings made to preserve a dissolved club's major assets beyond three years. In settling MOUs for mergers, parent clubs could also provide increased transparency about the risks associated with any promises made about a club's major assets and their intentions as to how they will treat them.

Recommendation 4 – Enable clubs to agree to longer, enforceable periods for maintaining assets of 'dissolved clubs'

Amend section 17AI of the Registered Clubs Act to enable clubs to agree that major assets of a dissolved club must remain intact for longer than the current maximum period of 3 years.

Recommendation 5 – Require a MoU to address risks and treatments relating to major assets

Amend clause 7 of the Regulation to require clubs to specify in a MOU the risks associated with undertakings about major assets and their intentions about how they will be treated.

FINDING 4 – There is a case for streamlining the club 're-amalgamation' process

It is possible for a child club to de-merge from a parent club while at the same time seeking to 're-amalgamate' with another parent club. However, stakeholder feedback suggests the process to achieve this re-amalgamation is too complex, long and costly.

It requires a club to undergo the full de-merger process and then the merger process again, usually in quick succession. In combination, this process results in duplication of effort, time and resources. For example, separate meetings of each club's members must be coordinated to initially approve the de-merger, and then for the re-amalgamation, and clubs must comply with separate notification and disclosure requirements for both processes.

Additionally, an anomaly exists requiring a de-merged club to be established as a new club (i.e. new entity) for a short period of time before its licence is transferred to the new parent club. From an operational perspective, stakeholder feedback suggests this 'time in limbo' can create commercial uncertainties for a de-merged club.

The Review appreciates these concerns and also considers that a re-amalgamation should not be so onerous to achieve. In its current form, it is apparent that some merged clubs are likely to have chosen not to embark on a re-amalgamation due to these barriers, or as suggested to the Review, chosen or considered to cease trading at the particular club site.

It would therefore be appropriate to address these issues by reducing the unnecessary duplication that presently exists, and to ensure that the transfer of a de-amalgamating club's licence from one parent club to another is effected as efficiently as possible.

Recommendation 6 – Better facilitate club 're-amalgamations'

Streamline the process for a club to re-amalgamate with a new parent club by enabling the direct transfer of a club's licence from one parent club to another, while retaining sufficient controls to promote transparency and protect member interests.

FINDING 5 – Any ambiguities or potential inconsistencies that exist between the Registered Clubs laws and Australian Corporations law should be addressed

As companies limited by a guarantee, clubs must comply with the *Corporations Act 2001* (Cth), in addition to complying with the requirements of the *Registered Clubs Act 1976*.

In each of their submissions, ClubsNSW and law firm Thomson Greer highlighted several instances where they consider clubs should simply be required to comply with corporations law where both Act's requirements are similar. In particular, they advocated for the removal of certain public disclosure and notification requirements under registered clubs laws.

However, the Review did not consider it appropriate to defer to corporations law, predominantly to ensure a higher level of transparency is maintained. Clubs should continue to notify members about merger and de-merger proposals on their noticeboard and website, as additional means to get the message out that a merger is being proposed. It is not

considered that this duplicate corporations law requirements, but complements them to provide additional means of getting the message out to members to promote awareness.

It was also identified that there are some ambiguities between both Acts that should be addressed to provide clubs with greater certainty. In particular, stakeholder feedback indicated that under corporation laws club members must each explicitly consent to becoming a member of a de-amalgamated club, as it is a new legal corporate entity, despite being deemed members under registered clubs laws.

Additionally, concern was raised about the ability of members to hold multiple classes of membership between amalgamated clubs. While the Review notes that this issue has at times been addressed via a series of complex amendments to a club's constitution or rules, it could potentially be dealt with differently to provide greater regulatory certainty to amalgamated clubs and their members.

Recommendation 7 – Undertake a further review of club membership issues

Examine the operation of section 17AC(2) and 17AN of the Act and their relationship to corporations law, with a view to addressing any ambiguities or potential inconsistencies.

FINDING 6 – There should be greater certainty around timeframes for assessing licence transfer applications for mergers and de-mergers

Industry feedback suggested there was scope to reduce the time taken for ILGA to make determinations on mergers and de-mergers. In particular, there have been instances of delays in the final stage of the merger process where ILGA must approve the licence of the 'child' club being transferred to another 'parent' club.

To address this, ClubsNSW recommended ILGA's maximum 120-day period for considering applications (in accordance with ministerial directions) encompasses the 30-day period to seek public submissions about the transfer of the club's licence.

Processing delays for these transfer applications have been reduced in recent times. Feedback to the Review indicated that they are now typically prioritised and processed well within 120 days inclusive of public consultation, whereas this has not always been the case. Accordingly, the Review considers that applications should continue to be processed within this timeframe to help provide greater certainty to clubs intending to merge or de-merge.

ClubsNSW also proposed that people with no standing in a merger or de-merger should be excluded from making a public submission. It submitted that this would prevent unnecessary disruptions and delays to the process by excluding industry detractors from the process.

However, the Review found little evidence this has occurred in practice. Rather, it continues to be an important mechanism that ensures there is a transparent and open process for the public to have its say about club mergers and de-mergers.

Recommendation 8 – ILGA to determine merger and de-mergers within 120 days

ILGA should continue to seek to process licence transfers for club mergers and de-mergers within 120 days, inclusive of the 30-day public submissions period.

FINDING 7 – Practices that help inform ILGA decision-making on mergers and de-mergers could be strengthened

ILGA proposed that clubs should be required to seek an independent verification of the advice they provide with a licence transfer application about how a proposed merger/de-merger complies with statutory requirements – for example, via an accounting firm.

This could strengthen the framework by better informing ILGA decisions. In particular, it could help ILGA to ensure mergers and de-mergers are undertaken in full compliance with relevant

controls that ultimately seek to protect the interests of clubs and their members. For example, ILGA must be satisfied that:

a) a parent or de-merged club will meet the requirements set out in section 10(1) of the Registered Clubs Act (i.e. requirements that must be met by all clubs in NSW),
b) a parent or de-merged club will be financially viable,
c) a proposed merger/de-merger is in the interests of the members of each club, and
d) a proposed merger/de-merger has been in-principally approved at separate extraordinary general meetings.

While this is a worthy objective, the Review also considers that independent verification would introduce additional time, cost and complexity into processes that can already be onerous for clubs to complete. Other measures might be implemented to achieve the same result, while minimising any additional burden imposed that could inadvertently discourage clubs from pursuing mergers or de-mergers.

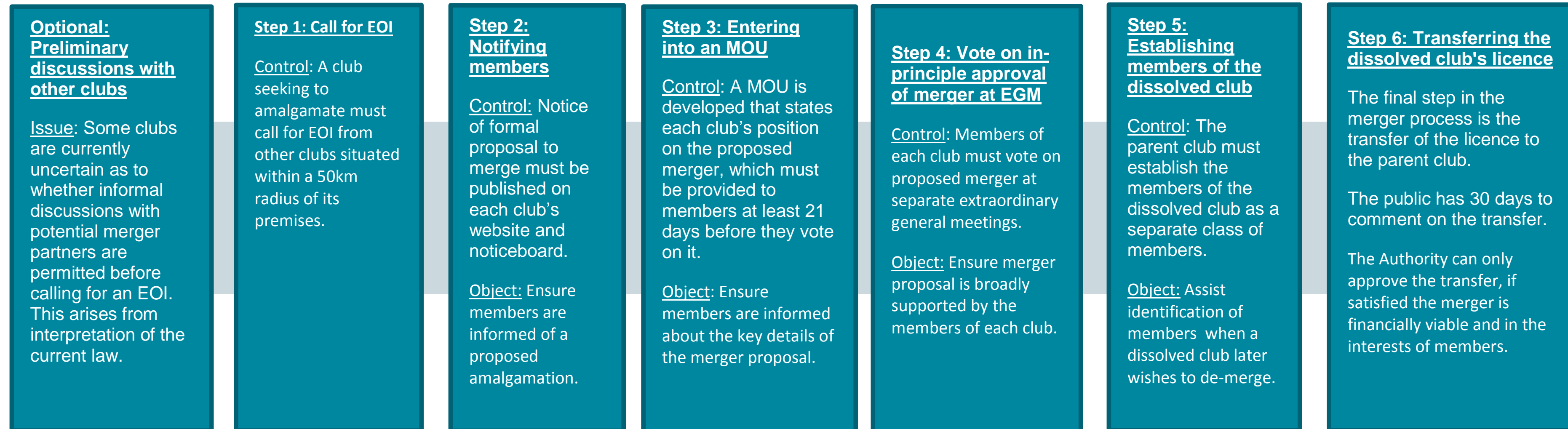
For example, a standardised 'checklist' might be introduced for clubs to demonstrate how they meet statutory requirements, to be lodged and publicly advertised as part of the licence transfer application underpinning a merger or de-merger. Clubs' legal representatives already typically produce their own checklists to support decision-making for proposed mergers and de-mergers, however they do not form part of the transfer application.

This type of approach could increase transparency and enable the general public (including a club's members) to scrutinise any claims made. It could also ensure more standardisation in the way clubs demonstrate that key statutory requirements have been met to support decision-makers. Clubs would be committing an offence under NSW liquor laws if they were to make false or misleading claims, or omit material matter, from a checklist that formed part of a liquor application itself.

Recommendation 9 – Ensure ILGA has the information it needs to make decisions

Identify practices, in consultation with ILGA and the club industry, to better inform ILGA about how a proposed merger or de-merger complies with statutory requirements, while seeking to minimise extra time and costs for clubs.

Appendix 1: Diagram of End-to-End Club Merger Process



Following recommended reforms…