

*Amendments to the  
Corporate Governance*

*Principles*

*and*

*Recommendations 2<sup>nd</sup> Edition*

Response Paper to Submissions  
ASX Corporate Governance Council

*30 June 2010*

## ABOUT THE ASX CORPORATE GOVERNANCE COUNCIL

The ASX Corporate Governance Council (Council) was formed in August 2002 and has been chaired by the Australian Securities Exchange (ASX) since its inception. The Council is a diverse body, bringing together 21 business, investment and shareholder groups. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be a practical guide for listed companies, their investors and the wider Australian community. The Council's diverse membership is one of its strengths, and its modus operandi of seeking a consensus facilitates a balanced approach to regulatory and reporting affairs under the *Corporate Governance Principles and Recommendations*.

The *Corporate Governance Principles and Recommendations* provide a non-prescriptive and principles-based framework for corporate governance for listed companies. Where a listed company considers that a particular recommendation(s) is not appropriate for its circumstances, it has the flexibility under the "if not, why not?" approach not to adopt the recommendation(s), provided an explanation is disclosed. Consistent with ASX's disclosure-based approach, listed companies are required in the ASX Listing Rules to publish a statement in their annual reports outlining the extent to which they have adopted each recommendation.

Council representatives include:

- Association of Superannuation Funds of Australia Ltd
- Australian Council of Superannuation Investors
- Australian Financial Markets Association
- Australian Institute of Company Directors
- Australian Institute of Superannuation Trustees
- Australian Securities Exchange
- Australian Shareholders' Association
- Australasian Investor Relations Association
- Business Council of Australia
- Chartered Secretaries Australia
- CPA Australia
- Financial Services Institute of Australasia
- Group of 100
- Institute of Actuaries of Australia
- Institute of Internal Auditors Australia
- Investment and Financial Services Association
- Law Council of Australia
- National Institute of Accountants
- Property Council of Australia
- Stockbrokers Association of Australia
- The Institute of Chartered Accountants in Australia

## 1. Introduction: what this Response Paper is about

- 1.1 In its first release of the *Corporate Governance Principles and Recommendations* (Principles and Recommendations) in March 2003, Council acknowledged the evolving nature of the corporate governance debate. Accordingly, the Council committed to reviewing emerging corporate governance issues to ensure the Principles and Recommendations remain relevant and appropriate to the Australian business community.
- 1.2 In August 2007, following an extensive review, Council released its second edition of the Principles and Recommendations.
- 1.3 Over the past 12 months, three significant independent reviews have been undertaken at the request of the Australian Government. The reviews focused on issues that included corporate governance practices of Australian-listed entities and resulted in the following reports with recommendations relevant to the Principles and Recommendations:
- The Corporations and Markets Advisory Committee (CAMAC) Report *Aspects of Market Integrity*, dated June 2009;
  - The CAMAC Report *Diversity on Boards of Directors*, dated August 2009; and
  - The Productivity Commission Inquiry Report *Executive Remuneration in Australia*, dated January 2010.
- 1.4 Council has followed the policy debate on the issues under review and has examined the merit of amending the second edition of the Principles and Recommendations to implement relevant recommendations. In April 2010, Council released an Exposure Draft of its proposed changes to these Principles and Recommendations. The Exposure Draft requested feedback from interested parties. Council's proposed amendments to the Principles and Recommendations were designed to:
- Improve gender diversity in the workforce, in senior executive positions and on the board of directors;
  - Provide further guidance to companies on communicating to shareholders about briefings; and
  - Enhance governance structures by introducing higher requirements for the composition of remuneration committees.
- 1.5 The amendments to the Principles and Recommendations are not intended to operate as a review of the second edition of the Principles and Recommendations or as a new edition. It is anticipated that the next full review of the Principles and Recommendations will commence in 2012 and, following public consultation, result in the release of the third edition of the Principles and Recommendations by mid 2013, after four full years of operation of the second edition.

## 2. The review process

- 2.1 Council received 23 submissions on the Exposure Draft. Annexure 1 to this Response Paper contains the list of those who made a submission. When reviewing these submissions, Council took into account its mission to develop and deliver an industry-wide, supportable and supported framework for corporate governance, which provides a practical guide for listed companies, their investors, the wider market and the Australian community. Council also considered the differing size, complexity and operations of listed companies, and the need for flexibility in the structures adopted to optimise individual performance, tempered by accountability: the obligation to explain to investors why an alternative approach to that outlined in the Principles and Recommendations is adopted - the "if not, why not" obligation.
- 2.2 In addition, when considering amendments to the Principles and Recommendations, Council was conscious that any amendment should: have a clear policy objective; be the appropriate way for the policy objective to be achieved; and result in a net benefit to the community. Where Council considered that an amendment was necessary, it then considered the language and drafting of the amendment to ensure that the meaning of the amendment is clear and that it has no unintended consequences.

### **3. Effective date**

- 3.1 It is intended that the reporting requirement for each of the amendments to the Principles and Recommendations will apply to an entity's first financial year commencing on or after 1 January 2011. Accordingly, for example, where an entity's financial year begins on 1 January, disclosure will be required in relation to the financial year ending 31 December 2011 and will be made in the annual report published by the end of April 2012. Where a company's financial year begins on 1 July, disclosure will be required in relation to the financial year ending 30 June 2012 and will be made in the annual report published by the end of October 2012.
- 3.2 While the formal commencement date of operation of the amendments to the Principles and Recommendations is 1 January 2011, Council considers that, especially in the case of the recommendations on diversity, listed entities with a balance date of 30 June 2010 should be able to establish a diversity policy and report against the new recommendations in respect of the year commencing 1 July 2010. Accordingly, Council encourages listed entities to make an early transition to the changes.

### **4. The contents of this Response Paper**

- 4.1 Council received feedback from listed companies, investors and other stakeholders on the changes to the Principles and Recommendations proposed in the Exposure Draft. Council has considered this feedback and has determined its policy position considering the amendments put forward in the Exposure Draft and the issues raised in submissions.
- 4.2 This Response Paper sets out Council's final determinations on these issues and its rationale for these determinations.

### **5. Acknowledgements**

- 5.1 Council expresses its appreciation to those who participated in the review and made submissions. This interaction ensures that the Principles and Recommendations will remain relevant and appropriate.

## COUNCIL'S RESPONSE BY PRINCIPLE

### 1. Council's Response by Principle

- 1.1 Council received 23 submissions to the Exposure Draft, from companies, industry groups, law firms, individuals, government and non-government organisations. The submissions ranged from one page documents to more lengthy submissions with detailed comments on the drafting, and were notable for their quality.
- 1.2 The majority of submissions expressed strong support for the proposed changes to the Principles and Recommendations, and the approach taken by Council in the Exposure draft. Submissions also expressed strong support for gender diversity initiatives.
- 1.3 Council has considered each of the submissions and amended the proposed changes to the Principles and Recommendations, where relevant and appropriate. A summary of the key points addressing issues outlined in the submissions and the Council's response are outlined below.

### 2. Principle 2 – Structure the board to add value

- 2.1 A number of submissions suggested that it was more appropriate for each company's board to determine whether the board or an appropriate committee should have the responsibility for gender diversity. Council has agreed with this suggestion and included relevant additional Commentary in Recommendation 3.4. Support remained for the charter of the board or appropriate committee to include an obligation to monitor the proportion of women at all levels of the company, and suggested Commentary to this effect also has been included in the commentary under Recommendation 3.4.
- 2.2 One submission proposed an inclusion of measures to bring about greater disclosure on board processes in board search and selection. Council has decided to include additional Commentary in Recommendation 2.4 to enhance transparency and disclosure regarding these processes. The types of disclosure that could be considered includes the development of skills matrices, the process of how candidates are identified, whether professional intermediaries are used, steps taken to ensure a diverse range of candidates is considered, and factors taken into account in the selection process.
- 2.3 One submission expressed the view that Recommendation 2.5 in its current form is sufficiently flexible to allow boards to determine their own processes for evaluating performance and as such should not include a list of specific board performance measures such as diversity. Council agrees with this view and has decided not to include specific reference in this recommendation to gender diversity as a performance measure. Council notes that this is not intended to diminish the significance of gender diversity as a part of performance measurement, but that it would not be appropriate to identify one component, without listing others, which Council felt was best left for companies to determine themselves. Greater clarity also was sought to the addition of director "meeting arrangements and director interaction" in director induction programs. Council has amended the wording to outline the types of director interaction intended, that being "director interaction with each other, senior executives, and other stakeholders".
- 2.4 In the "Guide to reporting on Principle 2", companies have been asked to provide a "statement as to the mix of skills and diversity which the board of directors is looking to achieve in membership of the board". Council notes in this regard that genuine statements are being sought from listed entities to ensure consideration of candidates from a diverse pool, and transparency around the appointment process.

### 3. Principle 3 – Promote ethical and responsible decision making

#### *Trading Policies*

- 3.1 Submissions were supportive of deleting Recommendation 3.2 and the associated Commentary, and Box 3.2 - "Suggestions for the content of a trading policy", to avoid any overlap and duplication between the Principles

and Recommendations and the proposed new ASX Listing Rules. The deletion will be synchronised with the commencement of the relevant amendments to the Listing Rules, namely with effect from 1 January 2011.

### *Diversity*

- 3.2 The majority of submissions strongly supported the proposed amendments in relation to diversity. A number of submissions commented that it would be unusual for details such as measurable objectives to be included in the diversity policy itself, which is less flexible and capable of amendment, whereas measurable objectives are updated with regard to changing circumstances. There was also support for requiring boards to report on progress towards achieving measurable objectives, so as to facilitate greater transparency and communications of whether tangible progress is being made. Council accepts these submissions and has revised Recommendation 3.2 to include these two considerations, which now reads “the policy should include requirements for the board to establish measurable objectives for achieving gender diversity and for the board to assess annually both the objectives and progress in achieving them”. Commentary to Recommendation 3.2 also has been amended to ensure that companies can seek to define diversity according to their particular circumstances, being “diversity includes but is not limited to gender, age, ethnicity and cultural background.”
- 3.3 Council also has amended Recommendation 3.3 to include disclosure of the progress towards achieving the measurable objectives, for the reasons highlighted in paragraph 3.2.
- 3.4 Submissions on Recommendation 3.4 suggested that the recommendation should not include a requirement to report on a full-time equivalent basis, as such reporting may not be appropriate given different types of work arrangements that currently exist. Submissions supported the intent of the proposal, but suggested deleting the proposed new material in the Recommendation and instead amending the Commentary to address the issue. Council has agreed with this suggestion and has included in the second paragraph of the Commentary the suggestion that companies should consider “how best to report to achieve an accurate and not misleading impression of the relative participation of women and men in the workplace” and also “...whether the participation is in a leadership, management, professional specialty or supporting role, or by relative participation of men and women at different remuneration bands.”
- 3.5 One submission asked that research mentioned in the Commentary to Recommendation 3.4 be footnoted so that companies could have access to the material. Council has decided to footnote the research which was used including a report from Goldman Sachs - *Australia's Hidden Resource: The Economic Case for Increasing Female Participation* - and a report from Catalyst - *The Bottom Line: Corporate Performance and Women's Representation on Boards*
- 3.6 One submission suggested that the diversity policy could require the achievement of measurable objectives to be linked to Key Performance Indicators for the board, the CEO and senior executives. Council has agreed with this suggestion and included wording to this effect in Box 3.2.
- 4. Principle 6 – Respect the rights of shareholders**
- 4.1 Submissions on proposed changes in Box 6.1 in relation to analyst briefings asked for greater clarity on the types of briefings covered, and also expressed some concern over the record keeping requirements, including difficulties in recording names from webcasts or large annual shareholder meetings. Council has decided to amend the wording to include “significant group briefings (including but not limited to results announcements)”, and to clarify that the record-keeping requirements include one-on-one briefings as well as group briefings. The summary record to be kept is intended only for internal use, and the company can record attendees based on “names or numbers where appropriate”. Council has placed the new wording on briefings in the Commentary under Recommendation 6.1.
- 5. Principle 8 – Remunerate fairly and responsibly**
- 5.1 There was general support for the proposal to elevate the existing guidance relating to the composition of a remuneration committee to an “if not, why not” recommendation”. The Principles and Recommendations will now include a recommendation that ASX-listed entities establish a remuneration committee comprised of a majority of independent directors, chaired by an independent director, and with at least three members.

- 5.2 Commentary under recommendations 8.1 and 8.2 was intended to highlight that executives should not be involved in decisions on their own remuneration. Some submissions highlighted that the proposed new material in the Commentary addressing this issue was not clear and could capture directors who determine their own salaries subject to shareholder approval. Council amended this Commentary under Recommendations 8.1 and 8.2, and replaced it with the Commentary which is more specific to senior executive involvement in the process. This Commentary in Recommendation 8.1 now reads: "The remuneration committee may seek input from senior executives on remuneration policies, but no senior executive should be directly involved in deciding their own remuneration."
- 5.3 One submission suggested the inclusion of wording in Principle 8 to address concerns of remuneration inequity on the basis of gender. Council has amended the Commentary under Recommendation 8.1 so that the responsibilities of the remuneration committee should include a review of, and recommendation to the board on, "remuneration by gender".

## Annexure 1

### Alphabetical list of submissions

- 1 Australian Financial Markets Association (AFMA)
- 2 Australian Human Rights Commission
- 3 Australian Institute of Company Directors (AICD)
- 4 Australasian Investor Relations Association (AIRA)
- 5 Business Council of Australia (BCA)
- 6 Chartered Secretaries Australia (CSA)
- 7 Chief Executive Women (CEW)
- 8 CPA Australia / The Institute of Chartered Accountants in Australia
- 9 Equal Opportunity for Women in the Workplace Agency (EOWA)
- 10 Freehills
- 11 Government of South Australia
- 12 Grant Thornton
- 13 Group of 100
- 14 Insurance Australia Group
- 15 Law Council of Australia (LCA)
- 16 National Australia Bank
- 17 Partha Sarathy
- 18 QBE Insurance Group
- 19 Telstra Corporation
- 20 The Westpac Group
- 21 Women on Boards (WOB)
- 22 Woolworths Limited
- 23 YWCA Australia