



03 August 2018

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**Submission on review of ASX Corporate Governance Council's
Principles and Recommendations**

Dear Ms Tan

Thank you for the opportunity to take part in the public consultation on the proposed fourth edition of the Corporate Governance Principles and Recommendations (Principles and Recommendations).

The Business Council, which represents more than 130 of Australia's business leaders, takes a leadership role on governance and conduct, as a member of the ASX Corporate Governance Council, and through the work of our Governance and Citizenship Committee, which focuses on identifying systemic issues that harm business reputation, and providing guidance to Business Council members to lift standards of conduct.

The Principles and Recommendations have served corporations well to date. The Business Council is supportive of their role, particularly in assisting boards with their disclosure obligations. We also support the work of the ASX Corporate Governance Council in reviewing, revising and consulting on the Principles and Recommendations on a regular basis to ensure they remain fit for purpose.

In the current review, we are concerned that the proposed changes to the Principles and Recommendations extend their scope in a way that risks detracting from their usefulness.

Our main comments on the draft Principles and Recommendations can be summarised as follows:

1. The Principles and Recommendations should not attempt to prescribe corporate culture.
2. The scope of obligations on directors has been broadened well beyond their key legal obligations.
3. There is ambiguity about the meaning of social responsibility and "social licence to operate" in Principle 3 and the accompanying recommendations.
4. There is over-prescription within the recommendations and associated commentary. An "if not, why not" approach to reporting on such a level of prescription will lead to the recommendations being regarded as minimum standards to be reported upon.
5. Some of the recommendations duplicate or potentially conflict with existing legal obligations.

Identifying and addressing the problem

It is critical that any changes to the Principles and Recommendations are responding to a clearly identified problem with current practice and a deficiency in the existing principles.

The consultation paper states that the primary change to the principles – which is the expansion of Principle 3 to cover corporate culture and socially responsible behaviour – responds to various enquiries and reviews that have highlighted governance issues arising from poor conduct or culture and a perceived lack of accountability.

Recent high-profile cases of corporate misconduct have highlighted that there are problems to be addressed, and subsequent enquiries and reviews have revealed that the causes vary. Where appropriate, legislation and regulation respond to systemic failures. The Business Council does not believe that it should be the role of the Principles and Recommendations to anticipate or prescribe a solution to issues of corporate misconduct, but instead should provide guidance on how organisations can disclose these issues.

Corporate culture cannot be prescribed by a set of rules, and the Principles and Recommendations should not seek to do so. Culture is a distillation of countless factors inherent within a business, and will change over time in response to community expectations and changes in leadership.

The Business Council suggests that the appropriate role of the Principles and Recommendations is to encourage organisations to describe how they determine and maintain a culture that is appropriate to the business they are in. Concerns around poor corporate governance could be better addressed by giving boards the flexibility to determine the best and most appropriate governance approach for each unique company situation.

Expansion of directors' obligations

The Business Council is concerned that the expectations established by the Principles and Recommendations that boards will get more involved in operational detail and detailed management of compliance requirements adds to an increasing regulatory burden on directors in Australia, and could divert boards from their core functions under the law.

An organisation must be free to put in place appropriate governance structures, with the board focused on the business's compliance with legal obligations and company policy and strategy, and management responsible for day-to-day operations.

We question the need to prescribe the structures, via committees or otherwise, that a board puts in place to deal with key areas. Committees should not result in a dilution of total board oversight and accountability. Nor should board committees divert from the central relationship between the board and the chief executive.

Social licence to operate

Principle 3 is proposed to be redrafted as “[a] listed entity should instil and continually reinforce a culture across the organisation of acting lawfully, ethically and *in a socially responsible manner*” (emphasis added).

The associated commentary states that “[p]reserving an entity’s social licence to operate requires the board and management of a listed entity to have regard to the views and interests of a broader range of stakeholders than just its security holders, including employees, customers, suppliers, creditors, regulators, consumers, taxpayers and the local communities in which it operates.”

The Business Council is concerned about potential conflict between the above quoted commentary, and the legal obligation of directors and officers to exercise their powers and discharge their duties in good faith in the best interests of the corporation.¹ Should the commentary be regarded as a minimum

¹ Section 181, Corporations Act 2001 (Cth).

standard for an entity to follow, directors and management may find themselves conflicted where stakeholder considerations do not align with the best interests of the corporation.

Social responsibility is impossible to define in a consistent way and will be subject to continually shifting community expectation. While we acknowledge that there is a place for it to be discussed as part of guidance material on corporate culture, it should not form part of the Principles, which should focus on acting lawfully and ethically.

Some of the commentary accompanying Principle 3 used in the context of defining an entity's social licence to operate is potentially problematic. As an example, the reference to the practice of "*paying a living wage to employees*" is a complex concept globally, and unnecessarily prescriptive for the broader desired behaviour of "*respecting the human rights of its employees*". There is also reference to "*social risks*" in Recommendation 7.4, with little explanation as to the meaning of this.

To illustrate the breadth of understanding of these concepts, an ESG investor may view legal industries such as gambling, liquor and mining as "socially irresponsible". The Business Council assumes that the Principles and Recommendations are not seeking to prevent ASX-listed companies from operating in such industries.

Proposal 1: Any reference to operating in a socially responsible manner should be removed from the Principles, with the focus instead on legal and ethical behaviour. Accompanying guidance material is the appropriate place for a discussion of the concept of social responsibility.

The guidance material on corporate culture should make it clear that in preserving an entity's social licence to operate, the legal obligation of the directors and management to act in good faith in the best interest of the listed entity must always take priority.

Level of detail in proposed changes

The Business Council is concerned about the level of prescription in the proposed additions to the Principles and Recommendations. While it is understood that much of the detail is posed as recommendations rather than rules, it sets an expectation for ASX-listed businesses to meet particular standards, or report on an "if not, why not" basis.

The "if not, why not" approach has the effect of creating standards to be reported upon, which is appropriate when applied to the high-level Corporate Governance Principles, but when combined with many new prescriptive recommendations, runs a risk of organisations being effectively sanctioned for their decisions not to follow recommendations, should the ASX or other interested stakeholders publicly take issue with their decision-making and disclosure. An entity could be in a position of having to justify why it has not done something that may not be in the best interests of the corporation, and may in fact dilute its governance responsibilities.

The increased degree of detail in the draft Principles and Recommendations marks a shift from the principles-based approach of earlier editions, which provided a more flexible framework for adoption by listed companies as appropriate to their size, sector and other specific circumstances. In the foreword to the 2nd Edition in 2007, then-Chair of the ASX Corporate Governance Council Eric Mayne stated:²

This document cannot be the final word. It is offered as guidance and will be reviewed again. Nor is it the only word. Good corporate governance practice is not restricted to adopting the Council's Recommendations. The arrangements of many entities differ from the Recommendations but amount equally to good practice. What matters is disclosing those arrangements and explaining the governance practices considered appropriate to an individual company's circumstance.

A contrasting view to the draft Principles and Recommendations was also taken by the UK Financial Reporting Council in its recent review of the Corporate Governance Code: "*The Code encourages*

² <https://www.asx.com.au/documents/asx-compliance/final-revised-principles-complete.pdf>.

companies to achieve high standards. To do this it needs to be clear and concise. To this end we have looked to shorten and sharpen the revised Code.”³

Over-prescription raises a concern about the cost of compliance with the changes, which should be quantified and taken into account as part of the consultation period. Smaller listed companies will likely struggle to absorb additional costs and reporting burdens, and will be unfairly impacted.

Perversely, prescriptive regulation can turn disclosure into a tick-the-box exercise, rather than setting high-level expectations about corporate culture.

The language of the commentary supporting the Principles and Recommendations has also become more prescriptive, using terminology such as “companies **should**...” (emphasis added). Some of the commentary throughout the document is at odds with the high-level principle to which it relates, and some does not explain the principle with sufficient clarity.

We question whether the Principles and Recommendations are the appropriate place for such a level of prescription to be housed. As an alternative, the Business Council intends to work with its members to improve corporate governance and culture through the use of best practice guidance and self-regulation.

The Business Council considers good governance practices are in the best interests of all companies and their investors. Investment will flow towards listed companies with good governance practices, while those entities who do not display appropriate governance will likely find that investors will sell shares and/or seek to replace boards. This is an effective incentive for self-regulation and is arguably preferable to a highly prescriptive regime.

Proposal 2: The ASX Corporate Governance document should be pared back to a strong statement of intent about its purpose, together with the eight high-level principles. Associated recommendations and commentary should be reframed as guidance and housed in a separate guidance document.

Avoiding unnecessary legislative duplication

Recommendations 3.3 and 3.4 will largely replicate the impending legislative obligations to have and disclose a whistleblower policy and an anti-bribery and corruption policy.

However, the Business Council understands that Recommendations 3.3 and 3.4 will go further than the pending laws in these areas, because the new recommendations include a requirement for the board of a listed entity to be informed of any material incidents reported under its whistleblowing policy and any material breaches of its anti-bribery and corruption policy

The Business Council also understands that approximately 10 per cent of ASX listed entities are established in places other than Australia and so they will not necessarily be subject to the new whistleblower, anti-bribery and corruption laws.

While the Business Council understands the Council’s desire to cover the field in these important areas of the law, we suggest that Recommendations 3.3 and 3.4 should not unnecessarily duplicate existing and impending legal obligations.

Therefore, the only new additional substantive aspects of Recommendation 3.3 and 3.4 should relate to the additional obligation for listed entities to *“ensure that the board is informed of any material concerns raised under that policy that call into question the culture of the organisation.”* Guidance as to what would constitute a “material concern” would also assist.

Proposed gender diversity target

Recommendation 1.5 proposes that entities in the S&P/ASX 300 set a measurable objective to have a minimum of 30 per cent of directors of each gender on their boards by a specified date.

³ Corporate Governance Council *Proposed Revisions to the UK Corporate Governance Code* (Dec 2017), p. 2.

The Business Council acknowledges that this is an important issue, but notes that the UK Financial Reporting Council's proposed guidance on board effectiveness states that "[d]iversity of psychological type, background, gender and ethnicity is important to ensure that a board is not composed solely of like-minded individuals."⁴

The Business Council considers that Recommendation 1.5 should be less prescriptive as to how diversity goals are achieved. Determining the desired characteristics of board members and how and when diversity milestones are reached should ultimately be left to an organisation to determine, based on the company's individual circumstances.

Recommendation 1.5 should be drafted to be less prescriptive, reflecting that listed entities need to have and disclose their own diversity policy, with measurable objectives for achieving diversity in the composition of its board, senior executives and workforce generally.

Prescribing how risk management should be disclosed

Recommendations 7.1 and 7.2 emphasise the importance of ensuring listed entities have robust risk management frameworks in place. While the Business Council supports using such a framework and the benefits of disclosure in this regard, specific aspects of these Recommendations prescribe unnecessary detail.

For instance, the requirement under Recommendation 7.2(a) to annually review the risk management framework may not be necessary for some businesses where the risk profile remains unchanged over a 12-month period. The board and the relevant risk committee of the listed entity (if applicable) should be free to determine how often risk management frameworks need to be reviewed, based on the circumstances of each listed entity and changes to the market in which they operate.

Disclosure of "appropriate information"

The proposed new Recommendation 4.4 requires listed companies to disclose their process for validating that their corporate reports "*provide investors with appropriate information to make informed investment decisions.*"

The Business Council is concerned that this recommendation goes beyond the requirement in the *Corporations Act 2001* (Cth) for a directors' report for a listed entity to provide information "*that members of the listed entity would reasonably require to make an informed assessment of:*

- (a) *the operations of the entity reported on; and*
- (b) *the financial position of the entity reported on; and*
- (c) *the business strategies, and prospects for future financial years, of the entity reported on.*"⁵

The legislative framework for disclosure through directors' reports also allows for information to be omitted if it is likely to result in unreasonable prejudice to the disclosing entity.

In their current format, the proposed Principles and Recommendations go further than this, and would be virtually impossible to satisfy, as "appropriate" information will mean different things to different people. A professional investor would want any available commercial information in order to make a fully informed investment decision, including details of future plans and strategies that would be of use to competitors; this would likely come at the cost of a competitive market.

We also query the scope of the reference in Principle 4 to "corporate reporting" and "any other corporate reports". It is unclear if this extends, for example, to market announcements, non-financial reporting, and other ad hoc or non-periodic reporting. If so, the focus proposed for some of this reporting may be inappropriate.

⁴ Corporate Governance Council *Proposed Revisions to the UK Corporate Governance Code, Appendix B – Revised Guidance on Board Effectiveness* (Dec 2017), p. 16.

⁵ Section 299A(1), *Corporations Act 2001* (Cth).

Recommendation 4.4 should focus on entities explaining how they ensure that corporate reports are accurate, balanced and understandable.

Investor and analyst presentations

Recommendation 5.3 states that “[a] listed entity that gives a new investor or analyst presentation should release a copy of the presentation materials on the ASX Market Announcements Platform ahead of the presentation.”

The Business Council is of the view that listed entities’ continuous disclosure obligations are already adequately defined by Listing Rule 3.1 and Guidance Note 8, and that these provisions should determine whether an investor or analyst presentation should be released to the market. An investor presentation with few changes to one previously released to the market should not, in our view, be required to be released. Listed entities should make such a determination in accordance with their existing continuous disclosure obligations.

We would be very pleased to discuss the above matters further, at your convenience. If you wish to contact the Business Council about any matter raised in this submission, please contact Sarah Phillips, Reputation Manager, at sarah.phillips@bca.com.au or 02 8224 9219.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Jennifer Westacott', written in a cursive style.

Jennifer A. Westacott AO
Chief Executive