CHARTERED SECRETARIES
AUSTRALIA

Leaders in governance

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Green paper:
The EU corporate governance

Chartered Secretaries Australia (CSA) welcomes the opportunity to comment on the green paper, *The EU corporate governance* (the paper). The paper explores the possible ways forward to improve existing corporate governance mechanisms in Europe, and CSA believes that the Australian corporate governance framework provides an excellent comparative viewpoint from which to engage in this review.

Chartered Secretaries Australia (CSA) is the independent leader in governance and risk management. As the peak professional body delivering accredited education and the most practical and authoritative training and information in the field, we are focused on improving organisational performance and transparency. Our Members are all involved in governance, corporate administration and compliance with corporate and other laws. They drive and advise on best practice in governance; champion the compliance framework to safeguard the integrity of the organisation; promote high standards of ethical and corporate behaviour; and bridge the interests of the board or governing body, management and stakeholders. Some of our Members also work in dual-listed companies, and thus have experience of the governance regimes in other jurisdictions. We have drawn on the experience of our Members in the formulation of our submission on the matters canvassed in the paper.

General comments

CSA is aware of the governance issues associated with the negative impacts felt by the global financial crisis (GFC), particularly in Europe, the United Kingdom (UK) and the United States and believes it is timely to examine the existing corporate governance regimes across Europe and review if there are measures that could be taken to improve the actions of boards of directors, shareholder engagement or, more generally, the 'comply or explain' regime.

Of developed economies around the world, Australia has emerged as among the least affected by the GFC. Australia largely escaped the worldwide recession. Australia's banking sector was also less adversely affected than elsewhere, with no failures and profitability remaining strong, although down somewhat from previous levels and with increased bad debt levels. However, there was some failure of listed financial/investment companies and large investor losses from structured products and investment funds, prompting concerns about financial market practices and investor protection. The Australian Securities and Investments Commission (ASIC) has addressed these concerns through a number of targeted consultations and the issue of revised guidance. The Australian Prudential Regulatory Authority introduced amendments to its governance standards (applicable to financial institutions) on remuneration relating to risk management to highlight board responsibilities in this area.

Notwithstanding the fact that Australia's financial system continued to function well throughout the GFC, Australia has followed with interest the review of corporate governance frameworks in the UK and Europe. The Walker Review was discussed at length by non-executive directors, company secretaries, investors and other stakeholders, as was the Stewardship Code which sits alongside the UK Corporate Governance Code, governing best practice in corporate governance in the UK. The June 2010 European Commission consultation on corporate governance in financial institutions was also closely followed.

ASX Corporate Governance Council's Corporate Governance Principles and Recommendations

The Australian Securities Exchange (ASX) Corporate Governance Council's *Corporate Governance Principles and Recommendations*, (Principles and Recommendations) are a flexible framework for corporate governance which provides a practical guide for listed companies, irrespective of their size or industry, their investors, the wider market and the Australian community. As one of the requirements of listing, all public listed companies are required to report to shareholders against the Principles and Recommendations, which operate on a 'comply or explain' basis, which in Australia is known as the 'if not, why not' regime (Listing Rule 4.10).[1] The second edition of the Principles and Recommendations is attached to this submission.

The Principles and Recommendations are not prescriptive. If a listed company considers that particular Recommendations are not appropriate to its circumstances, it has the flexibility — under the 'if not, why not' approach — not to adopt them, as long as it explains the reason(s) why. Listed companies are required to disclose in their annual reports the extent to which they have followed each Recommendation.

CSA Members firmly support a principles-based approach to corporate governance, rather than a rules-based approach, as there is often no one 'right answer' to many governance issues facing companies. A principles-based approach provides insight into board decision-making, allowing companies to meet the 'spirit' of the Principles through whatever means they believe are most appropriate to their business, provided they explain their approach. CSA believes that it is for shareholders to test directors' thinking and behaviour through shareholder engagement and for boards to be accountable to justify their decisions to shareholders. Each company is unique and its circumstances may change dramatically and suddenly. Companies need the

[1] ASX conducts supervision of all entities listed on the exchange, to ensure compliance with the Operating Rules including the Listing Rules. This supervision capacity is enforceable through the contract between ASX and the company (the Listing Rules). The role of the ASX Corporate Governance Council is to ensure that the principles-based framework it developed for corporate governance continues to be an effective practical guide for listed companies, their investors and the wider Australian community. It is independent of ASX, bringing together 21 business, investment and shareholder groups.

freedom to organise themselves and respond most effectively to the needs of the day. However, transparency as to decision-making is paramount.

Strong support has been evidenced for the Principles and Recommendations by all stakeholders. The history of the Principles and Recommendations is one of practical statements on governance that have brought meaningful change to governance practice since their release in 2003, by providing greater transparency of existing practices and encouraging boards and investors to consider the appropriateness of governance practices for their companies.

In 2010, the Principles and Recommendations introduced amendments on gender diversity and analysts' briefings. The amendments relating to gender diversity were the first of their kind under the 'if not, why not' regime. Entities listed on the ASX are required to develop a diversity policy, and disclose in their annual report their achievement against gender objectives set by their board, and the proportion of women on the board, in senior management and employed throughout the whole organisation. CSA notes that the UK Government has now introduced similar gender diversity requirements for listed entities in the UK, following the recommendations of the Davis Report.

In 2011, the ASX Corporate Governance Council has also been taking soundings from all stakeholders in the market as to whether the Principles and Recommendations should proceed to another edition to deal with any further governance issues not already covered. After a series of discussions with stakeholders, the Council has concluded that the Principles and Recommendations withstood the GFC well and, at this stage, no systemic corporate governance problems have been identified that require revisions to the Principles and Recommendations. There was no call or appetite from stakeholders to introduce further Recommendations or amend existing Recommendations against which listed entities must report.

It was strongly agreed by the ASX Corporate Governance Councils that a 'one-size-fits-all' approach is not appropriate to corporate governance, and that the great strength of the Principles and Recommendations is their flexibility, as they encourage companies to explain to investors why their corporate governance frameworks and processes are suitable to the circumstances of the individual company and bring value to shareholders.

Legislation

While Australia did not suffer the excesses of executive remuneration apparent in other jurisdictions, the issue of the regulation of director and executive remuneration was triggered by community and political concern with the levels and structure of executive remuneration following the GFC. The community, and its political representatives, were keen to examine to what extent remuneration is a private matter to be agreed between executives and companies, applying whatever governance processes properly protect the interests of owners, and to what extent there should be a community or public right to intervene in remuneration arrangements. The Australian Government introduced the Corporations Amendment (Improving Accountability on Termination Payments) Act 2009, providing that termination benefits for company directors and senior executives cannot exceed one year's average base salary unless approved by shareholders at a general meeting, and the Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011, introducing a range of measures intended to grant shareholders greater powers over scrutiny of executive remuneration. This Act includes the 'two-strikes' rule, under which shareholders will be able to demand a vote on whether to spill the board if more than a quarter of votes oppose the remuneration report at two successive annual general meetings. This provision is the first of its kind in the world.

The Corporations and Markets Advisory Committee (CAMAC)[2] has also undertaken a review in response to the government's request for advice on the scope to reduce the complexity of reporting on executive remuneration, and concluded that it is up to each company to determine the incentive and other components of remuneration. The report contains sensible recommendations on reducing complexity in reporting, and also refrains from recommending a substantially new approach to remuneration reporting on the basis that the 'two strikes test' legislation that has just been introduced will have an impact that needs to be assessed before further change is introduced.

Our comments on the specific questions raised in the paper follow.

Yours sincerely

Tim Sheehy
CHIEF EXECUTIVE

[2] The Corporations and Markets Advisory Committee was set up in 1989 to provide a source of independent advice to the Australian Government on issues that arise in corporations and financial markets law and practice.

Comments on specific questions raised in paper

(1) Should EU corporate governance measures take into account the size of listed companies? How? Should a differentiated and proportionate regime for small and medium-sized listed companies be established? If so, are there any appropriate definitions or thresholds? If so, please suggest ways of adapting them for SMEs where appropriate when answering the questions below.

CSA Members strongly support all Australian listed entities, no matter how small, being subject to the same corporate governance disclosures. The Recommendations in the Principles and Recommendations may be aspirational for smaller companies earlier in the organisational life cycle, but should form a touch-point for an ongoing, meaningful discussion about the organisation's governance framework as the company evolves.

Small to medium-sized listed companies comprise a large portion of the Australian market. However, the great strength of the Principles and Recommendations in their current form (the 'if not, why not' disclosures) is that they provide the flexibility required to optimise individual performance, tempered by accountability.

CSA Members note that it may be appropriate to tailor the Listing Rules to the differing size, complexity and operations of listed companies in Australia and that the ASX is currently engaged in consultation on this issue. To a certain degree, this process has begun, with only the top 300 ASX-listed companies subject to mandated requirements for the composition, operation and responsibility of the audit committee, and more recently, mandatory composition requirements for the remuneration committee. However, all companies require the discipline of knowing what governance frameworks will be required as the company evolves in size and complexity. For example, it may not be either feasible or appropriate for a small exploration company to have a board comprised of a majority of independent directors, given that it is likely that the directors will be executive directors when a company is in the initial stage of company development, and will not have the resources to expand the board. However, as the company evolves in size and complexity, it will need a larger board comprising more non-executive directors. The flexibility of the 'if not, why not' disclosure (or the 'comply or explain' disclosure) is that the company can explain to its investors why its board composition is appropriate for the company and adds value to shareholders.

The first Implementation Review Group's Report on the Principles and Recommendations noted that[3]:

> …there is no typical organisation and no single readily identifiable model for corporate governance... At different times and stages in a company's life, some governance structures may be better for the generation of wealth for investors than others...
>
> It [is] important to distinguish between the purpose of the …Principles and the purpose of the Recommendations. The Principles embody the broad concepts which underpin effective corporate governance. They encapsulate 'common sense' ideas with broad relevance. By contrast, the Recommendations given for each Principle suggest one framework for implementing the Principles within an organisation.
>
> Disclosure of a company's corporate governance practice, rather than conformity with a particular model is central to the ASX Corporate Governance Council's approach.

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[3] Implementation Review Group Report on ASX Corporate *Governance Council's Corporate Governance Principles and Recommendations*, released 31 March 2004 page 1ff.

CSA strongly recommends that EU corporate governance measures not differentiate according to the size of the company, but provide a set of principles embodying broad concepts that underpin effective corporate governance and require listed companies to disclose their practices within this context. Such disclosures will provide a window onto board decision-making, which provides for far greater transparency and accountability as to how a company implements its governance than a company ‘ticking a box’ against a tiered set of rules.

(2) Should any corporate governance measures be taken at EU level for unlisted companies? Should the EU focus on promoting development and application of voluntary codes for non-listed companies?

The Principles and Recommendations have become the aspirational framework for corporate governance in unlisted companies, the not-for-profit sector and the public sector in Australia. Notwithstanding this, many aspects of disclosure are different for unlisted companies than for listed companies, as it is a different market. Private equity may be undertaken as a means of enhancing company performance in a context where decisions can be taken quickly and the process of setting such decisions before shareholders for either scrutiny or approval may not be conducive to the need to move rapidly to protect shareholder value.

In Australia, the listed company market is irrevocably entwined with the superannuation system, as the superannuation funds (pension funds) are major, long-term investors in listed entities. This means that all working Australians are indirect shareholders, even if they are not direct shareholders. Therefore, the impact on society and the community as a whole of the decisions of boards of listed entities is very important and should be subject to a high level of scrutiny.

For self-evident reasons, the public sector can look to the Principles and Recommendations as a model for governance, but will need to adapt their ‘spirit’ to the particularities of the government sector. The not-for-profit sector also adapts the Principles and Recommendations. The corporate governance model set out in the Principles and Recommendations is designed to facilitate shareholder engagement and to assist investors to examine the statutory reports and financial accounts and governance of the company to ascertain the deployment of and return on their investment, whereas the members (and stakeholders) of not-for-profit organisations, while wanting to know the financial position of the organisation and that the organisation is being managed prudently, are primarily concerned that the allocation of resources is aligned with the values and objectives of the organisation as set out in its constitution.

In Australia, there is a plethora of guidelines on governance to which organisations in the unlisted, not-for-profit and public sectors can refer. These include the Principles and Recommendations, but also the governance standards released by the Australian Prudential Regulatory Authority (APRA) for authorised deposit taking institutions and general and life insurance companies[4] and guidelines issued by various industry associations. [5] Unlisted companies can refer to such guidance to assess what is most appropriate for each company’s circumstances.

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[4] Australian Prudential Regulatory Authority, *Prudential Standard APS 510 Governance*, November 2009

[5] See, for example, Investment and Financial Services Association, *IFSA Guidance Note No. 2.00 Corporate Governance: A Guide for Fund Managers and Corporations*, May 2009. This Guide is commonly known as the IFSA Blue Book.

CSA is of the view that it is not appropriate to develop corporate governance measures for unlisted companies for these reasons. Moreover, CSA is sure that, in Europe as in Australia, sufficient voluntary codes exist to which unlisted companies can refer, and that therefore there is no need for the European Union to also promote the development and application of additional voluntary codes for non-listed companies.

CSA recommends that the EU not develop corporate governance measures specifically designed for unlisted companies.

Boards of directors

(3) Should the EU seek to ensure that the functions and duties of the chairperson of the board of directors and the chief executive officer are clearly divided?

In Australia, the principle of independence is central to the governance framework. The ASX Corporate Governance Council's Principles and Recommendations recognise that the same person holding the role of chairman and chief executive can result in a fundamental conflict of interest, as the chief executive, being a member of management, could reasonably be perceived to be in a position that could materially interfere with the independent exercise of his or her judgment.

Recommendation 2.3 of the Principles and Recommendations states that: 'The roles of chair and chief executive officer should not be exercised by the same individual'. The commentary notes that:

> There should be a clear division of responsibility at the head of the company. The division of responsibilities between the chair and the chief executive officer should be agreed by the board and set out in a statement of position or authority. The chief executive officer should not go on to become chair of the same company. A former chief executive officer will not qualify as an 'independent' director unless there has been a period of at least three years between ceasing employment with the company and serving on the board.

However, CSA Members note that Australia has one legal and regulatory framework for listed companies, whereas Europe has different historical structures and legal frameworks regulating listed entities. For example, companies can have very different legal structures in Europe. It is therefore not appropriate to impose one model on Europe where different legal and regulatory frameworks operate.

CSA recommends that the EU should ensure that boards clearly explain to shareholders why the functions and duties of the chairperson of the board of directors and the chief executive officer are either held by the same person or are clearly divided, rather than prescribe one approach that may not be suitable for all companies or local jurisdictions.

(4) Should recruitment policies be more specific about the profile of directors, including the chairman, to ensure that they have the right skills and that the board is suitably diverse? If so, how could that be best achieved and at what level of governance, i.e. at national, EU or international level?

CSA Members are of the view that the issue of board renewal is best left to the board itself, as boards are best placed to take into account the financial and operational circumstances of the company, which over time may demand different skills/experience in directors. A board is best placed to undertake a skills/experience gap analysis and board matrix setting out the required skills/experience at any particular time.

Boards will also approach director recruitment in a fashion best suited to the needs of the individual company. For example, one board may target particular individuals who are seen to possess the skills required, whereas another board may seek access to a pool of candidates. A board may take either of these approaches at different time, and should be free to choose the approach best suited to the needs of the company at any given time.

Therefore, CSA Members do not support a prescriptive approach that mandates recruitment policies for companies.

However, opportunities should be provided to shareholders to engage with companies on long-term strategic and governance issues to provide a real test to the thinking and behaviour of boards and management, and to ensure that boards properly oversee management. Shareholders should be provided with the opportunity to assess board decision-making in relation to board composition and renewal.

CSA strongly recommends that the board of a company should provide transparency to shareholders of the process that the individual company adopts to foster board renewal. This provides a mechanism for the review of decisions taken by directors.

This transparency is enshrined in Australia in Principle 2 of the Principles and Recommendations, which provides a good (although not exclusive) model for holding the board accountable for board composition and renewal, and disclosing its decision-making processes to shareholders. Principle 2 holds the board accountable for decisions about the necessary and desirable competencies of directors; review of board succession plans; the development of a process for the evaluation of the performance of the board, its committees and directors; and the appointment of directors. The board is also enjoined to ensure that there is a formal and transparent procedure for the selection, appointment and re-appointment of directors to the board, and this is specifically noted as helping promote investor understanding and confidence in that process. The board may delegate these processes to a nomination committee, which will make recommendations to the board.

The Principles and Recommendations note that the important issues to be considered as part of the process include:[6]

- Disclosure of board selection processes — companies are encouraged to provide greater transparency of the processes which the board adopts in searching for and selecting new directors to the board and to report to shareholders on the processes. Such reporting could include the following:
  - details as to whether the company develops a board skills matrix and uses this matrix to identify any ‘gaps’ in the skills and experience of the directors on the board
  - the process by which candidates are identified and selected including whether professional intermediaries are used to identify and/or assess candidates
  - the steps taken to ensure that a diverse range of candidates is considered and the factors taken into account in the selection process.

[6] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, amended 2010, pp18-19

(5) Should listed companies be required to disclose whether they have a diversity policy and, if so, describe its objectives and main content and regularly report on progress?

Australia was the first jurisdiction to introduce diversity recommendations to the corporate governance framework on an 'if not, why not' basis. Research shows that boards operate most effectively when at least three directors on a board of eight to ten are the least represented gender. Significant business and other benefits accrue when gender ceases to become a focal point and men and women are empowered to bring diverse technical and behavioural skill sets to the board of a company. In addition, companies where there are more women on the board are most likely to have a larger percentage of women at senior management/executive level.[7]

The Principles and Recommendations include a recommendation that entities listed on the ASX develop and make publicly available a diversity policy and disclose in their annual report:

- the gender diversity objectives set by their board and progress towards achieving them, and
- the proportion of women on the board, in senior management and employed throughout the whole organisation.

The commentary attached to the Recommendations on diversity provides guidance to boards to:

- determine the appropriate committee for recommending strategies to address board diversity, considering diversity in succession planning, and having a charter that regularly reviews the proportion of women at all levels in the company
- disclose the mix of skills and diversity they are looking for in their membership, and
- ensure that there is an accurate and not misleading impression of the relative participation of women and men in the workplace.

The changes relating to gender diversity took effect for the first financial year of listed entities beginning on or after 1 January 2011. The ASX Corporate Governance Council encouraged listed companies to be early adopters of the gender diversity recommendations as from July 2010. A number of major listed companies did make an early transition to disclosing diversity policies and measurable objectives as set by the board.[8]

CSA has developed a Good Governance Guide to assist boards to develop diversity policies suitable to the circumstances of their companies, and boards and management to develop measurable objectives for gender diversity. It is attached as Appendix B.

CSA recommends that the EU require listed companies to disclose whether they have a diversity policy, describe its objectives and main content and regularly report on progress against the objectives in the policy, on a comply or explain basis.

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[7] Carter NM and Silva C, 2010, *Pipeline's Broken Promise — The Promise of Future Leadership: A Research Program on Highly Talented Employees in the Pipeline,* Catalyst; Coffman J, Gadiesh O and Miller M, 2010, *The great disappearing act: Gender parity up the corporate ladder,* Bain & Company; Goldman Sachs JBWere, 2009, *Australia's Hidden Resource: The Economic Case for Increasing Female Workforce Participation,* Research Report

[8] See, for example, http://www.nabgroup.com/0,,33874,00.html; http://www.woodside.com.au/Investors-Media/Corporate-Governance/Pages/Policies-Procedures.aspx; http://www.telstra.com.au/abouttelstra/company-overview/governance/documents/;http://www.anz.com.au/about-us/our-company/corporate-governance/; http://www.woolworthslimited.com.au/phoenix.zhtml?c=144044&p=irol-govhighlights

(6) Should listed companies be required to ensure a better gender balance on boards? If so, how?

CSA is firmly of the view that a focus on a more robust and open approach to board appointments and initiatives to encourage the development of women in executive management are the most effective ways to foster a governance culture that embraces diversity in the composition of corporate boards.

CSA is of the view that requiring listed companies to develop and disclose a diversity policy, describe its objectives and main content and regularly report on progress against the objectives in the policy, on a 'comply or explain' basis, will be a catalyst for the board to show that it is managing gender diversity for the benefit of shareholders.

In Australia, since the introduction of the gender diversity recommendations in 2010, the percentage of women on boards of ASX 200 companies and the proportion of women comprising new appointments has increased significantly. Research shows that women have comprised 30 per cent of new appointments to ASX 200 boards to date in 2011 and comprised 25 per cent of all new appointments to ASX 200 boards in 2010, compared to only five per cent in 2009 and eight per cent in 2007 and 2008. Thirty-three women have been appointed to ASX 200 boards in 2011 to date, and 59 women were appointed to ASX 200 boards in 2010, a substantial increase on the 10 appointed in 2009.[9]

CSA does not support boards being required to meet prescribed quotas in relation to gender diversity. CSA Members are of the view that if quotas are set, boards of listed companies will not develop the culture that actively considers the development of a policy on diversity not as a compliance issue, but as a means of improving the performance of the business. The process of developing a diversity policy and setting measurable objectives against which the board must report in relation to gender diversity is much more likely to result in boards articulating what diversity means to their companies, as part of their promotion of processes within the companies they govern that are intended to deliver long-term economic advantages to the organisation.

CSA recommends that the EU not introduce gender diversity quotas for boards, but require listed companies to disclose whether they have a diversity policy, describe its objectives and main content and regularly report on progress against the objectives in the policy, on a comply or explain basis.

(7) Do you believe there should be a measure at EU level limiting the number of mandates a non-executive director may hold? If so, how should it be formulated?

CSA Members, who work closely with boards in companies of all sizes, note that the demands of boards differ from company to company. A small listed company with a single business focus and no board committees will place very different demands and impose a substantially different workload on its board members than a large multinational company operating diversified businesses. A not-for-profit board seat may place more demands on the time of a non-executive director than a listed company board seat. Similarly, an individual may sit on a number of board committees on one board and not sit on any on another board. Seeking to prescribe the number of mandates that a non-executive director may hold does not take account of the particular circumstances of each individual, company or individual position within that company.

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[9] Statistics for 2004, 2006 and 2008 are drawn from the Equal Opportunity for Women in the Workplace Agency's 2008 *Australian Census of Women in Leadership*. Statistics for 2010 and 2011 are based on the Australian Institute of Company Directors research.

It is for the board under the guidance of the chairman to monitor its members' ability to properly carry out their duties. Properly prepared letters of appointment will assist directors to have clarity as to the company's expectations attached to the role and also provide an opportunity for directors to assess if any of their other commitments will have an impact on fulfilling the role. Similarly, ongoing assessment of the board, its committees and directors should monitor the ability of individual directors to manage their workload.

CSA recommends that an arbitrary specification of the number of directorships that an individual may hold is not good governance. The onus of responsibility must be on boards under the guidance of the chairman to ensure that the board is fit for purpose, which includes ensuring that each director has sufficient time to undertake the role.

(8) Should listed companies be encouraged to conduct an external evaluation regularly (e.g. every three years)? If so, how could this be done?

In Australia, Recommendation 2.5 states that: 'Companies should disclose the process for evaluating the performance of the board, its committees and individual directors'.[10]

The supporting commentary providing guidance on this Recommendation states that: 'The performance of the board should be reviewed regularly against appropriate measures.'[11]

The Council's Principles and Recommendations do not specify either the measures that are to be utilised in the board review, or the exact periods in which board reviews should take place, but do require disclosure of the board evaluation process undertaken. CSA agrees with this approach, as it provides flexibility to boards to decide the best process and timeframe for its board evaluations, subject to disclosure to shareholders as to the board's decision-making on this issue.

In the UK, the Corporate Governance Code has introduced a new requirement that an evaluation of the board of FTSE 350 companies should be externally facilitated at least every three years. This has been the subject of robust discussion in Australia, with non-executive directors, company secretaries and shareholders all in agreement that a set period for conducting a board review is not required in this jurisdiction.

CSA recommends that the process and timeframe for board evaluations should not be mandated, but that all companies should be required to disclose the process for evaluating the performance of the board, its committees and individual directors.

(9) Should disclosure of remuneration policy, the annual remuneration report (a report on how the remuneration policy was implemented in the past year) and individual remuneration of executive and non-executive directors be mandatory?

Disclosure of the remuneration framework, the annual remuneration report (which is part of the annual report) and the remuneration of the key management personnel (KMP) has been mandatory in Australia for some years. The remuneration report must disclose a breakdown of performance-related components, non-performance related components and the value of any securities issued as part of a person's remuneration. If any of those KMP are employed under a contract, the remuneration report must also detail the duration period of the contract, notice periods required for termination and any termination benefits payable (s 300A of the Corporations Act).

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[10] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, amended 2010, p 19

[11] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, amended 2010, p 19

In addition, where a chief executive officer is appointed (or where a managing director is appointed to a company that does not have a chief executive officer) ASX Listing Rule 3.1 will require that a summary of the terms and conditions of employment be disclosed. The ASX has set out some examples of what type of information entities may disclose upon a CEO's appointment, which include:

- what proportion of pay is base pay
- what proportion of pay is related to performance (and the applicable time frames)
- what proportion of pay is related to share price (and the applicable time frames)
- what proportion of pay is equity based, and
- whether there are any add-ons for longevity.

Companies are also expected to disclose any other components of remuneration and the nature of termination entitlements. The disclosure does not necessarily need to include dollar amounts, although in practice most companies choose to include dollar amounts.

In addition, the ASX Corporate Governance Council's Principles and Recommendations call for entities to provide disclosure in relation to the entity's remuneration policies to enable investors to understand the cost and benefits of those policies and the link between remuneration paid to directors and key executives and corporate performance.[12]

CSA is of the view that boards should make every effort to explain their remuneration decisions. CSA also notes that remuneration is a complex and dynamic process. Plans are regularly adjusted to achieve particular performance outcomes sought by boards on behalf of shareholders, reflecting changes in the circumstances in which company activity takes place. Notwithstanding this, CSA is of the view that the complexity of remuneration frameworks is no excuse for boards to resile from clear and transparent disclosures to shareholders. Directors need to make the effort to clearly explain their remuneration decisions, particularly if they are complex.

The Corporations and Markets Advisory Committee (CAMAC)[13] undertook a public consultation in 2010 in response to a request from the Australian Government for advice on the possibility of reducing the complexity of executive remuneration reports. It is widely accepted by all stakeholders that the remuneration report has become largely incomprehensible to many ordinary shareholders. It is not unusual for the statutory remuneration reports of large listed companies to run to 20 pages or more of detailed disclosures which can be largely impenetrable to the lay reader. The statutory requirements attached to the remuneration report in Australia are such that companies require substantial legal advice to ensure that all requirements are met — this in turn means that remuneration reports are often highly legalistic.

A highly legalistic remuneration report does not tell the company’s story in its own words and can hinder understanding on the part of the investor. Investors are seeking information as to why certain decisions concerning remuneration have been made, in what context and for what purpose. The remuneration report needs to tell the ‘why’ as well as the ‘what’ of remuneration decisions.

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[12] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, amended 2010, Principle 8, pp 36-37

[13] The Corporations and Markets Advisory Committee was set up in 1989 to provide a source of independent advice to the Australian Government on issues that arise in corporations and financial markets law and practice.

CAMAC reported in April 2011.[14] While the CAMAC report contains sensible recommendations, it also refrains from recommending a substantially new approach to remuneration reporting on the basis that the 'two strikes test' legislation will have an impact that needs to be assessed before further change is introduced. However, it recognises that remuneration reports need to be simplified and a non-prescriptive approach applied, so that remuneration reports can provide the information that shareholders require to understand board decision-making.

CSA recommends that disclosure of remuneration policy and the annual remuneration report (a report on how the remuneration policy was implemented in the past year) should be required, but, given the experience in Australia, **CSA strongly recommends** that any disclosure of the remuneration policy and remuneration report not be heavily formulated and prescribed.

CSA also recommends that disclosure of individual remuneration of executives be confined to the KMP.

(10) Should it be mandatory to put the remuneration policy and the remuneration report to a vote by shareholders?

Remuneration policy

CSA notes that, in general, board policies are not put to a vote by shareholders in Australia. Corporations legislation, in Australia and other common law countries, is very clear as to the division of responsibilities in companies. In Australia, the Corporations Act (s 198A) provides that the business of a company is to be managed by or under the direction of a board of directors appointed by and accountable to the shareholders, and the directors exercise all powers of a company except those that are required to be exercised in a general meeting.

Equally, corporations legislation recognises that mechanisms are required for the review of decisions taken by directors. As part-owners, shareholders should be engaged in the corporate governance of companies. They should engage with companies on long-term strategic and governance issues to provide a real test to the thinking and behaviour of boards and management, and to ensure that boards properly oversee management.

In Australian board policies are disclosed, in order to shed sunlight on the values of the company and the decision-making framework of the board. Investors can review board policies and decide if those policies reflect their values. The ultimate power of shareholders is to use their binding vote on the election of directors, or sell their shares.

However, in effect, the advisory vote on the remuneration report in Australia is a vote on the board's policy on remuneration, as the remuneration report is required under the Corporations Act to provide a discussion of the board's policy on the remuneration of KMP.

Remuneration report

The remuneration report of an Australian public listed company must be submitted to a general meeting of shareholders and the adoption of that report is subject to a non-binding vote (ss 250R(2) and (3)).

Director remuneration is subject to shareholder approval (s 202A). ASX Listing Rule 10.17 requires that total remuneration of non-executive directors cannot be increased without shareholder approval. Non-executive director remuneration is submitted to shareholders for approval in aggregate, not on an individual basis. Non-executive directors do not receive bonuses — their remuneration is fixed.

[14] Corporations and Markets Advisory Committee, *Executive Remuneration*, April 2011

The non-binding shareholder vote on the remuneration report provides an opportunity for shareholders to hold boards accountable for their decisions on remuneration. It not only provides the opportunity for shareholder scrutiny of board decision making on remuneration, but also the opportunity to express shareholder views and engage with boards, without blurring the line between managers and owners.

The introduction of the non-binding shareholder vote on a company's remuneration report in Australia has been one of the single biggest catalysts for improved levels of engagement between shareholders and company directors. The remuneration report has provided a basis for companies to explain the rationale of their approach on pay, and the non-binding vote has given shareholders an opportunity to express their views and has generated significant media scrutiny and coverage of the voting results.

CSA recommends that a *non-binding* (advisory) vote on the remuneration report be mandated.

CSA notes that the vote on the remuneration report is advisory. CSA supports this. There are numerous practical difficulties in making the vote on the remuneration report binding, including that:

- the remuneration report deals with events that have already occurred — it is not clear what a binding vote in respect of past events would mean
- if responsibility for setting remuneration policy and outcomes is removed from the board, there may be ambiguity as to who is accountable for the performance of executives — this would be a governance quagmire
- remuneration reports are often complex and cover a number of different aspects of remuneration including the chief executive, other senior executives and non-executive directors. There is no way to determine which particular aspect might have lead to a no vote or what remedial action would be required to address a no vote
- boards may find that they are unable to recruit and retain executives with the necessary skills and talent due to remuneration restraints, that is, they are not in a position to finalise a contract when recruiting or have any certainty from year to year as to what the remuneration will be
- directors have a fiduciary duty to act in the best interests of the company as a whole. Shareholders have no such fiduciary duty.

CSA strongly opposes a binding shareholder vote on the remuneration report, not only because it blurs the line between owners and managers, but also because we note that in Australia, significant representatives of institutional or retail shareholders hold a similar view to that of CSA. For example, shareholders have expressed the view that they do not want to run companies but see this as the role of the CEO overseen by and reporting to their boards, with boards attracting and motivating the CEO and executives through remuneration practice. Shareholders have commented that they do not have the expertise to develop policies that accommodate each individual company's strategy — they can advise the board as to their satisfaction with long-term alignment and hold the board accountable through director elections. However, they do not require a binding vote on remuneration policy.

(11) Do you agree that the board should approve and take responsibility for the company's 'risk appetite' and report it meaningfully to shareholders? Should these disclosure arrangements also include relevant key societal risks?

CSA fully supports boards approving and taking responsibility for the company's risk appetite.

However, disclosure of the risk appetite will inevitably involve disclosure of commercial in-confidence information, and CSA does not believe that such information should be disclosed.

CSA notes that the ASX Corporate Governance Council took a clear decision that it is not in shareholders' interests for the board to disclose the risk appetite of the company, given the confidential and commercially sensitive nature attached to the risk appetite and the fact that the appetite can change rapidly according to changes in the company's circumstances. Accordingly, the Principles and Recommendations do not require disclosure of the risk appetite.

Recommendation 7.1 states that: 'Companies should establish policies for the oversight and management and management of material business risks and disclose a summary of those policies'.[15]

The commentary supporting this Recommendation provides the following guidance:[16]

> Each company will need to determine the 'material business risks' it faces. When establishing and implementing its approach to risk management a company should consider all material business risks. These risks may include but are not limited to: operational, environmental, sustainability, compliance, strategic, ethical conduct, reputation or brand, technological, product or service quality, human capital, financial reporting and market-related risks.....Risk management policies should reflect the company's risk profile and should clearly describe all elements of the risk management and internal control system and any internal audit function.

CSA recommends that a board should approve and take responsibility for the company's risk appetite.

CSA opposes mandatory disclosure of the risk appetite.

(12) Do you agree that the board should ensure that the company's risk management arrangements are effective and commensurate with the company's risk profile?

Importantly, the Principles and Recommendations require boards to report to shareholders that management has:

- implemented the risk management system to manage the company's material business risk, and
- reported to the board on whether those risks are being managed effectively.

CSA is of the view that disclosure of the board's oversight of management responsibility for managing risks is the sound governance approach, rather than disclosure of the company' risk appetite.

CSA recommends that the board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The board should disclose that management has reported to it as to the effectiveness of the company's management of its material business risks.

[15] ASX Corporate Governance Council, Corporate Governance Principles and Recommendations, 2nd edition, amended 2010, p 33
[16] Ibid

Shareholders

(13) Please point to any existing EU legal rules which, in your view, may contribute to inappropriate short-termism among investors and suggest how these rules could be changed to prevent such behaviour.

While CSA is not in a position to point to existing EU rules, we can offer comment on two issues that require consideration when reviewing measures to support or hinder long-term governance approaches.

Remuneration of asset managers
One aspect of remuneration that does need to be considered is how asset managers (known as fund managers in Australia) are rewarded. Their incentives can be misaligned both with the interests of the investors whose interests they are paid to serve as well as with long-term sustainable value-creation in companies. Many funds managers are rated and paid based on quarterly performance. As a result, there is an incentive to maximise quarterly value. Stock will be churned and traded on the basis of short-term speculation. The share is viewed as a commodity, not an investment. It is difficult for boards to redesign the structure of senior executive pay in order to ensure greater long-term shareholder alignment if remuneration in the funds management industry is not also redesigned. While boards are exhibiting behavioural change in response to changed financial conditions, CSA believes that similar behavioural change needs to occur in the funds management industry, but is of the view that this is best achieved through industry-led guidelines rather than through prescriptive approaches.

Regulation in this regard is inappropriate, as investors use asset managers and invest in the market for a range of purposes and this flexibility needs to be encouraged. Quarterly reporting is of itself not necessarily misaligned with the interests of investors, as many, even long-term investors, are seeking short-term gain. The key is to ensure that performance (for remuneration purposes) is measured in a way that includes all of the costs of the investment decisions (including tax paid on short-term gains).

CSA opposes legislating the asset management industry in relation to remuneration.

CSA recommends that industry-led guidelines are the measures most conducive to ensuring good governance outcomes in relation to incentive structures for and performance evaluation of asset managers.

Taxation arrangements
CSA is of the view that the taxing point for equity or rights that qualify for deferral should be at the earliest of where ownership of, and free title to, the shares or rights is transferred to the employee. This in turn encourages long-term remuneration plans to be put in place.

To illustrate this, we look at employee share schemes, as an example of how taxation arrangements can either support long-term remuneration plans or undermine them.

Director share ownership was introduced in Australia in response to shareholder activism, which sought to ensure that the interests of directors and shareholders were aligned. Legislation encouraging employee share schemes was introduced in Australia 1995. This included provision for tax deferral for employees acquiring shares and options under an employee share scheme.

Employee share schemes were introduced to attract, retain and motivate human resources in a company by giving employees a direct link to the fortunes of a company, thus aligning the interests of employees and boards. They provide for employees, as shareholders, to participate in corporate governance debates and shareholder debates at AGMs. Statistics regarding employee ownership in Australia show that 57 per cent of listed companies had a broad-based plan (or plans) in 2009.[17]

Providing for tax to be deferred until the employee gains formal control of the shares supports employee share schemes and the alignment of the interests of directors and shareholders. Legislative measures prohibiting tax deferral for employees acquiring shares and options under an employee share scheme, and providing that employees would be assessed upfront could result in employees paying tax on shares they never receive, which would hinder employee share schemes.

(14) Are there measures to be taken, and if so, which ones, as regards the incentive structures for and performance evaluation of asset managers managing long-term institutional investors' portfolios?

See our comments above on the need for industry-led guidance to be released to assist the funds management industry to redesign remuneration frameworks as appropriate.

(15) Should EU law promote more effective monitoring of asset managers by institutional investors with regard to strategies, costs, trading and the extent to which asset managers engage with the investee companies? If so, how?

CSA has no comment on this.

(16) Should EU rules require a certain independence of the asset managers' governing body, for example from its parent company, or are other (legislative) measures needed to enhance disclosure and management of conflicts of interest?

CSA has no comment on this.

(17) What would be the best way for the EU to facilitate shareholder cooperation?

Companies used to be a community comprising a small number of investors with similar interests, known to the directors and who could have a large impact on outcomes by voting. There were considerably fewer opportunities in the media and analysts' research for shareholders to receive continuous and near real-time information on the performance of the company. However, investors now have many different financial and other interests in companies and are not necessarily long-term investors (they can be 24-hour investors). The concept of the community of shareholders known both to each other and the directors is no longer operative.

Shareholders today are a diverse group, dispersed geographically (including internationally) and, in many large companies, can number in the thousands, if not the millions. With dynamic and global investment strategies, shareholders may include an individual resident in Australia planning for his or her retirement, a large institution with billions of dollars under management, a foreign investor, a global hedge fund, and an investor with no interest in the company beyond a short-term trade. The traditional retail investor in Australian equities may represent a small proportion of the capital of a large ASX-listed company.

[17] I Landau, R Mitchell, A O'Connell, I Ramsay and S Marshall, *Broad-Based Employee Share Ownership in Australian Listed Companies: Survey Report*, Melbourne Law School, The University of Melbourne, April 2009

Such a diverse group and their interests cannot be definitively described as unanimous. It is not feasible to say that all shareholders' interests are aligned. A shareholder who is on the register for 24 hours may not have the same interests as one who seeks to remain on the register over decades. Therefore, it is difficult to devise a 'one-size-fits-all' approach to facilitate shareholder cooperation. CSA notes that many institutional investors already cooperate through their membership of the International Corporate Governance Network (ICGN), which devises policy positions on governance issues agreed by members from multiple jurisdictions.

Notwithstanding this, CSA is of the view that the AGM is increasingly irrelevant as the premium forum in which shareholders could cooperate with each other in terms of engaging with the boards on the performance and prospects of the companies in which they invest.

CSA research over a decade shows that shareholder attendance at AGMs in Australia has been decreasing.[18] Even in circumstances of investor interest in and scrutiny of company performance in 2009, due to the exigencies of the global financial crisis, shareholder attendance at the AGM remained low. In 2009, only 0.3 per cent of shareholders in large Australian companies (> $5b market capitalisation) and 7.3 per cent of shareholders in medium-sized Australian companies in the ASX 200 ($50m—$5bn market capitalisation) attended the AGM. The percentage of shareholders attending the AGMs of Australia's largest companies (many of which have the largest retail shareholder bases) therefore actually decreased from 1.5 per cent in 2007.[19]

Declining shareholder attendance at AGMs needs to be understood in the context of continuous disclosure, as the AGM is no longer the primary source of information for shareholders and prospective investors about a company, while the annual report is historical data. With the advent of continuous disclosure and the technology to facilitate such ongoing disclosure, there is no longer any substantive information in the annual report that is market-sensitive in any respect at the time of the AGM.

Institutional and retail shareholders both wish to engage with the companies in which they invest. Retail shareholders advise that they, in particular, see the AGM as the main forum to review and discuss company results; gain access to the directors to question them on those results as well as plans for the future; elect the directors and, when the office is vacant, the auditor; and be exposed to information concerning any important developments in the previous financial year and in the year to come.[20] Yet they are not attending AGMs. They are, however, attending non-statutory shareholder briefings, where the absence of formal proceedings governed by legislation provides an opportunity for the board to speak to company performance and prospects in a manner that engages shareholders.

It is important to note that declining shareholder attendance at AGMs is not by reason of any legislative barrier, although the formality and often complex voting requirements of certain resolutions often detract from companies' ability to use the meeting to impart valuable information to shareholders. Companies make many efforts to encourage shareholder attendance at AGMs. However, throughout the year, and not just in the lead-up to the AGM, many institutional investors meet with the company and discuss issues relating to performance and prospects. Sophisticated and targeted communication with institutional investors via analyst briefings provides a stream of engagement with institutional investors, who do not rely on the general meeting as the prime forum for engagement with the companies in which they invest.

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[18] Chartered Secretaries Australia, 2010 *Benchmarking Governance in Practice in Australia*, Survey results — May 2010

[19] There is no research on 2010 AGM attendance numbers currently available

[20] Australian Shareholders' Association, ASA Submission on CSA's discussion paper, *Rethinking the AGM*, where it states: 'The AGM is the cornerstone of a listed company's communication with its owners. It is the only opportunity for retail shareholders to directly communicate with those entrusted to manage the company'.

Any information discussed at such meetings that is market-sensitive is required to be released to the market immediately in Australia, as part of our continuous disclosure regime, to ensure that all investors and stakeholders have timely and equal access to information that could affect, either favourably or unfavourably, the price or value of their holdings. These meetings with institutional investors constitute respect for those owners of the company with large holdings, as they provide a forum for the direct questioning of directors and senior management.

The ASX Corporate Governance Council introduced amendments to the Principles and Recommendations in 2010 encouraging companies to 'arrange for advance notification of significant group briefings and to make them widely accessible, including through the use of webcasting or any other mass communication mechanisms as may be practical'.[21] This provides for retail shareholders to readily access analysts' briefings.

Companies are increasingly providing webcasts of their general meetings, and reporting that the numbers of attendees at the webcast are greater than those attending an AGM in person. Moreover, technology allows shareholders to vote without needing to attend the general meeting.

CSA believes it is important to look at the overall interaction a company has with its shareholders when considering shareholder engagement. For example, results announcements, analysts' briefings, investor road shows, 'investor days' (or shareholder briefings), the AGM and other forms of communication all form part of engaging with shareholders. There is a range of options available to companies to communicate with their shareholders and, to a lesser extent, for shareholders to communicate with the companies in which they invest. Social media also opens up new opportunities for companies and shareholders to engage.

CSA does not therefore see a need for the EU to introduce any legislative measures to facilitate shareholder cooperation. Indeed, CSA is of the view that legislative measures are likely to stifle shareholder cooperation, as evidenced by the ongoing failure of the AGM to attract shareholder interest. CSA is of the view that shareholder cooperation is more likely to develop through networking via associations such as ICGN, through technological platforms such as social media and in non-statutory shareholder briefings. CSA strongly supports the EU putting in place a regulatory framework that encourages such practices and their evolution over time, rather than any regulatory framework that seeks to prescribe how such cooperation may take place.

(18) Should EU law require proxy advisors to be more transparent, e.g. about their analytical methods, conflicts of interest and their policy for managing them and/or whether they apply a code of conduct? If so, how can this best be achieved?

Australian institutional investors generally hold positions in hundreds of listed Australian companies. Often they do not have the 'in-house' capability or resources to conduct independent research about each agenda item for each company's ballot at general meetings, including the AGM. Proxy advisory services undertake research and assessment and advise institutional investors on governance arrangements within companies. They evaluate the numerous resolutions proposed by companies, including the resolution on the remuneration report, and make recommendations to institutional investors on how to vote on these resolutions.

Institutional investors take seriously their responsibility to vote their shares on resolutions put to members at general meeting and consider the governance of the entities in which they invest. Superannuation funds and fund managers are required to assess agenda items with care and caution, and exercise their votes in a manner consistent with their fiduciary duties. Even the

[21] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, amended 2010, p 31

best-resourced funds require quality, independent information gathered by proxy advisory services. Accessing quality, independent information in relation to a range of issues assists institutional investors to discharge their voting responsibilities. Such information, which includes recommendations on voting on proposals to be put to shareholders, may have a material effect on voting results.

The conflicts of interest that bedevil proxy advisory firms in other jurisdictions such as the United States do not occur in Australia, as the proxy advisory firms do not currently provide consulting services on corporate governance to Australian investee companies. Nonetheless, CSA is firmly of the view that any such conflicts of interest are not in the interests of good governance, and supports regulation requiring disclosure of them in other jurisdictions.

The main issues that arise in Australia relate to the company often not having a right of reply to a published report that contains factual errors or is based on misinterpretation of the information in the public domain. Australian listed companies would like the opportunity to see the proxy advisory firm's report without charge before it is issued, but understands that the reality is that the proxy advisory firms must release the report to their clients, the institutional investors, before it can release it more widely. Nonetheless, transparency in all phases of the proxy advisory firm's processes is essential, given that they are a key participant in improving the good governance of Australian corporations.

The other issue that arises is that the application of the governance guidelines developed by the proxy advisory firms can be inflexible. The corporate governance framework in Australia is founded on the 'if not, why not' regime which provides the flexibility for a company, if it considers that a Recommendation is inappropriate to its particular circumstances, to not adopt it — a flexibility tempered by the requirement to explain why. CSA sees little value in a checklist approach to corporate governance that does not focus on the particular circumstances of a company with its own unique needs, strengths and weaknesses. The inflexibility of the proxy advisory firms' guidelines is such that in their application they are likely to be used as a checklist.

Some companies have expressed concern that proxy advisory services 'control' the votes of their clients, the institutional investors. However, institutional investors have an obligation to make their own decisions and vote accordingly. Yet proxy advisory services do wield influence and that influence should not be underestimated. The recommendations put forward by proxy advisory services will be attended to by those who commissioned the research. In some instances, investors may not exercise their discretion or may be reluctant to vote against the recommendations of proxy advisory services.

CSA published *Better communication between entities and proxy advisory services (*a copy of which is attached to this submission) containing recommendations for good practice that arose from a Roundtable CSA hosted, attended by institutional investors, proxy advisory services, company secretaries, retail investors, directors and other governance advisers to examine how to improve engagement between investors, proxy advisory services and companies.

In order to assist institutional investors exercise their voting rights, the publication recommends that proxy advisory services should:

- contact issuers in advance of publication of their reports with respect to ambiguity or contentious issues in the issuers' publicly available documents
- provide issuers with an explanation for negative recommendations
- correct factual errors in their reports to institutional clients immediately
- provide a copy of their report upon request to issuers, once it has been released to institutional investors, independently of a corporate subscription
- make their guidelines publicly available on their websites
- enter into a dialogue with issuers independently of a corporate subscription.

While CSA does have concerns about the lack of transparency about the process of how the proxy advisory firms apply their guidelines and arrive at their recommendations for voting, we do not recommend regulatory action in relation to this. CSA is of the view that greater transparency will develop as the engagement between institutional investors and the companies in which they invest also develops, and both parties seek greater accountability from the proxy advisory services in relation to their decision making.

(19) Do you believe that other (legislative) measures are necessary, e.g. restrictions on the ability of proxy advisors to provide consulting services to investee companies?

CSA does not support legislative measures to restrict proxy advisers providing consulting services to investee companies, but does support regulation requiring disclosure of such conflicts of interest.

(20) Do you see a need for a technical and/or legal European mechanism to help issuers identify their shareholders in order to facilitate dialogue on corporate governance issues? If so, do you believe this would also benefit cooperation between investors? Please provide details (e.g. objective(s) pursued, preferred instrument, frequency, level of detail and cost allocation).

In Australia, listed companies are required to maintain a register of substantial shareholders. CSA strongly supports this register, which goes to the heart of understanding control of a company.

However, even with this register being mandated, it can be difficult for companies to identify shareholders on the register. Tracing through layers of nominees and custodians is challenging to identify the beneficial owner — the investor with which the company wishes to engage. In Australia, there are tracing provisions in the Corporations Act, but the process itself is time-consuming and expensive. Many companies commission specialist analyst advisers to trace shareholders on the register. Even with specialist assistance, the information can be out of date by the time the company receives it, given that the composition of the register is constantly changing. Moreover, the costs of the specialist analyst advisers can be beyond the resources of smaller listed companies, although many smaller companies have detailed knowledge of their major shareholders and can easily engage with them, due to the smaller size of the register.

CSA is of the view that it would facilitate dialogue between companies and shareholders on corporate governance issues for companies to be able to more readily identify shareholder on the register, but notes that the deregulation of markets and developments in technology constantly create new ways for shares to be held diversely. Therefore, CSA believes that legal mechanisms are unlikely to assist issuers to identify their shareholders.

(21) Do you think that minority shareholders need additional rights to represent their interests effectively in companies with controlling or dominant shareholders?

The Corporations Act and the ASX Listing Rules in Australia provide a clear set of rights for minority shareholders. CSA strongly supports the high level of legal protection provided to minority shareholders.

There are two important mechanisms under the Corporations Act that protect minority shareholders' rights: Part 2 F.1 deals with the statutory rights of shareholders where the affairs of the company are conducted contrary to the interest of the company and, are as a whole, oppressive, unfairly prejudicial or unfairly discriminatory; and Part 2F.1A allows shareholders to bring proceedings on behalf of a company, or to intervene in proceedings to which the company is a party dealing with statutory action. A statutory derivative action is one commenced by a company's shareholder(s), on behalf of the company itself, when the shareholder(s) believes the company is not adequately protecting its legal rights and interests. Statutory derivative actions are generally brought against the directors or officers of a company for wrongdoings such as negligence, fraud, breach of fiduciary duties or an abuse of power.

Other remedies for different forms of oppressive conduct against the minority are the winding up of the company and a buy-out of the minority's shares, the purchase being made either by majority shareholders or by the company itself.

CSA notes that in some European countries, minority shareholders remain vulnerable to the actions of controlling shareholders. CSA does not believe that this is good governance. CSA refers the EU to the rights of minority shareholders in Australia for comparative purposes.

(22) Do you think that minority shareholders need more protection against related party transactions? If so, what measures could be taken?

CSA has no comment on this.

(23) Are there measures to be taken, and is so, which ones, to promote at EU level employee share ownership?

As noted above, legislation encouraging employee share schemes was introduced in Australia 1995. Currently, it is not a policy priority for the Australian Government. CSA recommends that taxation arrangements be considered to promote employee share ownership.

Monitoring and implementation of Corporate Governance Codes

(24) Do you agree that companies departing from the recommendations of corporate governance codes should be required to provide detailed explanations for such departures and describe the alternative solutions adopted?

CSA is strongly of the view that the 'if not', why not' regime can only operate successfully if companies provide an explanation to shareholders as to why they have implemented a governance practice that is different from the one recommended in the Principles and Recommendations.

Under ASX Listing Rule 4.10.3, companies are required to provide a statement in their annual report disclosing the extent to which they have followed the Recommendations in the reporting period. Where companies have not followed all the Recommendations, they must identify the Recommendations that have not been followed and give reasons for not following them.

As noted in the Implementation Review Group's report on the application of the Principles and Recommendations:

> Adequate disclosure will address the following three elements:
> 1. How the company's approach is different from the relevant Recommendation;
> 2. The reasons why the company's approach has been adopted and how its approach accords with the intent or 'spirit' of the relevant Principle, and
> 3. That the company understands the relevant issues and has considered the impact of its alternative practices.

(25) Do you agree that monitoring bodies should be authorised to check the informative quality of the explanations in the corporate governance statements and require companies to complete the explanations where necessary? If yes, what exactly should be their role?

A listing authority has a licence from the government to operate a market. This brings supervision responsibilities.

CSA therefore firmly believes that it is incumbent on listing authorities to set the consequences for non-reporting. This forms part of their supervision responsibilities and also promotes confidence in the market. CSA also notes that it is a means of a listing authority adding value to the market when competing exchanges are operating.

However, CSA is equally strongly of the view that it is not for the listing authority to judge the quality of any corporate governance statements made by companies. It is for investors to judge the quality of the corporate governance statements, which are intended to provide a window onto board decision-making, so that shareholders can assess and test the thinking and behaviour of boards.