

# ASX Corporate Governance Council

## Transitioning to the third edition of the Principles and Recommendations



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# Outline

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- Summary of key changes
- When you have to start reporting against the third edition
- Things you should be doing now to get ready
- Early adoption
- Concluding remarks
- Questions

# Key changes

- ✓ Greater flexibility to put your governance disclosures on your website rather than in your annual report
- △ Enhanced risk recommendations (including new recommendations on internal audit and sustainability risks)
- △ Seven other new recommendations to report against
- △ Changes to director independence criteria
- ✓ Board committee recommendations less prescriptive – can have audit, nom, risk and rem committees **OR** disclose alternative governance practices and still report you comply
- △ Modified recommendation on board skills matrix
- △ CEO/CFO declarations required for quarter/half year, as well as full year, financial statements

## Key changes (cont.)

- △ Modified recommendations on respecting the rights of security holders
- △ Enhanced commentary on diversity recommendations
- ✓ Simpler and clearer directions for externally managed entities
- △ “If not, why not” corporate governance statement (“CGS”) must be dated and approved by your board
- △ New Appendix 4G (key to corporate governance disclosures) to be lodged with your annual report

Note: detailed summary of changes in ASX roadshow tomorrow. Slides for the roadshow presentation and this presentation available on ASX website:

ASX | Regulation | ASX Compliance | Presentations and webinars

<http://www.asx.com.au/regulation/compliance/presentations-and-webinars.htm>

# Effective date of changes

- Third edition and related Listing Rule changes take effect for your first full financial year commencing on or after 1 July 2014, ie:
  - 30 June balance date → report for FY ending 30 June 2015
  - 31 Dec balance date → report for FY ending 31 Dec 2015
  - 31 March balance date → report for FY ending 31 March 2016
- Requirements to:
  - report against third edition
  - date and have your board approve your CGS, and
  - lodge Appendix 4Gtherefore don't apply until 2015/2016, depending on your balance date
- **BUT NOTE**: there are a number of steps you will need to implement beforehand if you want to report in 2015/2016 that you are in compliance with the third edition

# Enhanced risk recommendations

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## Rec 7.1 – risk committees (changed)

- If you have, or intend to have, a committee or committees to oversee risk, check their composition and you have disclosed their charters (Rec 7.1(a))
- If you don't, articulate the processes the board employs to oversee your risk management framework to satisfy itself that it is sound (Rec 7.1(b))
- Consider how your disclosures on these matters might read and whether you should upgrade your processes

# Enhanced risk recommendations (cont.)

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## Rec 7.2 – annual review of risk management framework (changed)

- If you haven't done so already, articulate your risk management framework and review process
- Consider how your disclosures about these matters might read and consider whether they need to be upgraded
- If you don't have such a process currently, institute a process for the board or a committee of the board to review your risk management framework at least annually to satisfy itself that it continues to be sound
- Remember to disclose in your annual report or on your website that the review took place during the relevant reporting period

# Enhanced risk recommendations (cont.)

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## Rec 7.3 – internal audit (new)

- If you have an internal audit function, articulate how the function is structured and what role it performs
- If you don't have an internal audit function, articulate the processes you employ for evaluating and continually improving the effectiveness of your risk management and internal control processes
- Consider how your disclosures on these matters might read and whether you should upgrade your internal audit function/processes



# Enhanced risk recommendations (cont.)

## Rec 7.4 - economic, environmental and social sustainability risks (new)

- Note definitions of ‘economic sustainability’, ‘environmental sustainability’ and ‘social sustainability’ in glossary to, and definition of ‘material exposure’ in footnote 38 of, the third edition
- Note focus is on investment risks, not environmental or social outcomes
- If you consider you do not have a material exposure to sustainability risks, all you need do is to state that fact
- If you consider you do have a material exposure to sustainability risks, you should disclose what those risks are and how you manage, or intend to manage, them
- This does not require you to publish a sustainability report – but, if you do, you can meet Rec 7.4 simply by cross-referring to that report
- You can also meet Rec 7.4 by cross-referring to relevant sections in your operating and financial review

# Other new recommendations

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## **Rec 1.2 – background checks for new directors etc**

- Check processes are in place to undertake appropriate checks before appointing a person, or putting forward to security holders a candidate for election, as a director

## **Rec 1.3 – written contracts of appointment**

- Check you have a written agreement with each director and senior executive setting out the terms of their appointment

## **Rec 1.4 – company secretary**

- Review reporting lines and confirm that the secretary is accountable directly to the board, through the chair, on all matters to do with the proper functioning of the board

## Other new recommendations (cont.)

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### **Rec 2.6 - director induction and professional development**

- Review your program for inducting new directors and satisfy yourself it is sound
- Have the board or nom committee periodically review whether there are any gaps in the skills or knowledge of directors and consider professional development opportunities to fill those gaps

### **Rec 4.3 - auditor to be present at the AGM**

- Will mainly impact entities established outside Australia not subject to ss250PA, 250RA and 250T of the Corporations Act
- Consider how security holders may direct questions to the auditor if they are not able to attend the meeting (see Rec 6.3)

## Other new recommendations (cont.)

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### Rec 6.1 - information on website

- If you don't have a website, get one!
- Review and refresh the materials on your company and its governance on your website, using the commentary to Rec 6.1 for guidance

### Rec 6.4 - option for electronic communications

- If you don't have an email address for security holder communications, get one and publicise it!
- If it is a generic email address, make sure someone is monitoring it at least daily
- Confirm with your registry that it gives the option for your security holders to communicate with it electronically

# Director independence

- Board or board committee should review the independence of each director against the changes made to Box 2.3:
  - expansion of references to material suppliers and customers to cover other material business relationships, going back 3 years
  - inclusion of 'close family ties' to someone not considered independent
  - inclusion of 'been in role for such a period that independence may have been compromised'

in each case, assessing the materiality of any interest, position, association or relationship to determine whether it might interfere, *or might reasonably be seen to interfere*, with independent judgment

- If a director's status as an independent director has changed:
  - disclose and explain that change to the market in a timely manner
  - assess the impact of that change on the composition of board committees (do they still have the required number of independents?)

# Nom, audit and rem committees

- If you have such committees, check their composition and you have disclosed their charters (Rec 2.1(a), 4.1(a) and 8.1(a))
- If you don't have such committees, articulate the processes you employ:
  - to address board succession issues and to ensure the board has an appropriate balance of skills, knowledge, experience, independence and diversity (Rec 2.1(b))
  - to independently verify and safeguard the integrity of your corporate reporting, including the processes for the appointment and removal of external auditor and rotation of audit engagement partner (Rec 4.1(b))
  - for setting the level and composition of remuneration for directors and senior executives and ensuring it is appropriate and not excessive (Rec 8.1(b))
- Consider how your disclosures on these matters might read and whether you should upgrade your processes

# Board skills matrix

- Note change in Rec 2.2 of third edition compared to Rec 2.6 (5<sup>th</sup> bullet point) of second edition – ‘board skills matrix’ instead of ‘statement as to mix of skills and diversity’
- ‘Matrix’ implies specificity around disclosure of skills, not motherhood statements
- Doesn’t have to be in tabular format – choose a format that you feel best conveys the information
- Can reflect the board’s current mix of skills and diversity or the mix of skills and diversity that the board is looking to achieve
- Disclosure only has to be made collectively across the board as a whole – you don’t need to identify the presence or absence of particular skills by a particular director
- Commercially sensitive information can be excluded

# CEO/CFO declarations for interim financials

- Note change in Rec 4.2 in third edition compared to Rec 7.3 in second edition
- Before approving financial statements for any financial period, your board should receive from the CEO and CFO a declaration that, in their opinion:
  - the financial records of the entity have been properly maintained
  - the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity, and
  - the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively
- Institute processes to get CEO/CFO declarations in time to table them at board meetings approving any quarterly or half yearly financial statements



# Respecting the rights of security holders

## Rec 6.2 - investor relations program

- Articulate your investor relations program and how it facilitates effective two-way communication with investors
- Consider how your disclosures on your program might read and whether you should upgrade it

## Rec 6.3 - facilitate participation at meetings of security holders

- If you haven't already done so, document the policies and processes you have in place to facilitate and encourage participation at meetings of security holders
- Consider how your disclosures on your policies and processes might read and whether you should upgrade them
- Disclose those policies and processes on your website

# Diversity policy and disclosures

- If you are a ‘relevant employer’ under the Workplace Gender Equality Act, you can choose to report;
  - your ‘Gender Equality Indicators’, or
  - the respective proportions of men and women on boards, in senior management and across the organisation
- If you are thinking about the former, note footnote 16 on page 11 of the third edition
- If you choose the latter, you must disclose how you have defined ‘senior executive’
- Note the enhanced commentary on how to define ‘senior executive’ and reassess how you have defined the term
- Note also the enhanced commentary on the meaning of ‘measurable objectives’ and test whether your diversity policy really sets meaningful and measurable objectives

## Diversity policy and disclosures (cont.)

- If you want guidance on setting measurable objectives, see:
  - Workplace Gender Equality Agency, *About Setting Gender Targets*: <https://www.wgea.gov.au/learn/about-setting-gender-targets>
  - Women on Boards, *Guidelines for Gender Balance Performance and Reporting*: <http://www.womenonboards.org.au/pubs/guidelines/>
- If you want to lead rather than lag, see:
  - *Male Champions of Change, Accelerating the advancement of women in leadership: Listening, Learning, Leading*: [https://www.humanrights.gov.au/sites/default/files/document/publication/2013\\_AHRC\\_MCC\\_accelerating\\_advancement\\_women.pdf](https://www.humanrights.gov.au/sites/default/files/document/publication/2013_AHRC_MCC_accelerating_advancement_women.pdf)
  - *Male Champions of Change Raise the Bar on Gender Reporting*: <https://www.humanrights.gov.au/male-champions-change-raise-bar-gender-reporting>

# Externally managed listed trusts

- Familiarise yourself with the section in the third edition: ‘The application of the recommendations to externally managed listed entities’
- Note the additional two recommendations that apply to you (an alternative to Rec 1.1 and an alternative to Rec 8.1, 8.2 and 8.3)
- Look at the table at the back of Guidance Note 9, which conveniently summarises how the recommendations apply to you
- Review your governance disclosures against that table

# Plan your governance disclosures

- Work out which recommendations in the third edition you intend to follow and what disclosures that will entail (Appendix 4G will help!)
- Work out where you intend to make those disclosures - on your website or in your annual report
- If you are going to put them on your website, map out the user experience:
  - Menu location ('About us', 'Investor centre', 'Information for shareholders')
  - 'Corporate governance' landing page
  - Links to pages with more information (eg director bios, info about board committees etc)
  - Links to relevant documents (eg board committee charters)

## Plan your governance disclosures (cont.)

- Remember that you still have to produce a stand-alone CGS disclosing:
  - the extent to which you have followed the Council's recommendations over the reporting period, and
  - separately for each recommendation you haven't followed:
    - the reasons why
    - the period for which it was not followed, and
    - what (if any) alternative governance practices you adopted during that period (LR 4.10.3)
- CGS may incorporate material by reference (eg on your website or in another part of your annual report)
- CGS can be published on your website or in your annual report
- CGS must specify the date at which it is current and state that it has been approved by your board (LR 4.10.3)

## If your CGS is on your website ...

- Can be a separate PDF document or just a HTML web page
- Make sure it specifies the date at which it is current and that date is your balance date or a later date (LR 4.10.3)
- Make sure it includes a statement that it has been approved by the Board (LR 4.10.3)
- Remember to include the URL of the web page where it is located in your annual report (LR 4.10.3)
- Remember to lodge a copy of the CGS, current as at its effective date, with your annual report (LR 4.7.4)
- On page 1 of your Appendix 4G, remember to:
  - check the second box to indicate that your CGS is on your website and fill out the URL of the web page where it is located, and
  - include the effective date of your CGS in the following paragraph

## If your CGS is in your annual report ...

- Make sure it specifies the date at which it is current and that date is your balance date or a later date (LR 4.10.3)
- Make sure it includes a statement that it has been approved by the Board (LR 4.10.3)
- On page 1 of your Appendix 4G, remember to:
  - check the first box to indicate that your CGS is in your annual report and fill out the page numbers of your annual report where it is located, and
  - include the effective date of your CGS in the following paragraph



# Getting board approval for your CGS

- Think about the effective date of your CGS:
  - your balance date?
  - the date the board makes its declaration under s295(4) of the Corporations Act?
  - some other convenient date after your balance date?
- Plan when you will get the board's approval and include this in your board calendar
- Discuss with the board ahead of time the process for obtaining approval:
  - pre-vetting by audit committee?
  - certification by company secretary?
  - sign-off by external counsel?

# The new Appendix 4G

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- Not a replacement for your CGS
- A verification tool you and ASX can use to confirm you are meeting your corporate governance disclosure requirements
- A key investors and other stakeholders can use to find your governance disclosures
- Also a useful guide to help you map out your governance disclosures
- It looks more daunting than it really is!

# Early adoption of website disclosure?

- Only possible if you early-adopt the whole package, that is:
  - report against the third edition of the Principles and Recommendations, and follow ...
  - amended Listing Rule 4.10.3 (ie date your corporate governance statement and have it approved by the board)
  - new Listing Rule 4.7.4 (ie give ASX a copy of your corporate governance statement at the same time as your annual report)
  - new Listing Rule 4.7.3 (ie give ASX a completed Appendix 4G at the same time as your annual report)
- If you don't do **ALL** of these things, you will need to include your corporate governance statement in your annual report, as per the existing rules

## Early-adoption of the third edition alone?

- Encouraged and can be done without adopting new LR 4.7.3 or 4.10.3 (ie no need to date your CGS, have it approved by the board or to lodge Appendix 4G)
- Your CGS must be included in your annual report and, technically, report the extent to which you complied with the second edition over the whole of the reporting period
- Simply report in your CGS:
  - the switchover date
  - the extent to which you complied with the second edition in the period up to the switchover date
  - the extent to which you complied with the third edition in the period after the switchover date
- Note that new and amended recommendations in the third edition will likely mean that few will be able to early-report full compliance with the third edition

# Early adoption of a specific recommendation only?

- Encouraged and can be done without adopting new LR 4.7.3 or 4.10.3 (ie no need to date your CGS, have it approved by the board or to lodge Appendix 4G)
- Your CGS must be included in your annual report and, technically, report the extent to which you complied with the second edition over the whole of the reporting period
- If you early-adopt a new recommendation (ie no counterpart in second edition), technically, there's no need to mention it in your CGS at all – although you can, if you want, and you probably should
- If you early-adopt an amended recommendation (eg diversity), simply report in your CGS:
  - the switchover date;
  - the extent to which you complied with the recommendation in the second edition in the period up to the switchover date
  - the extent to which you complied with the recommendation in the third edition in the period after the switchover date

# Concluding remarks

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- No right or wrong answers – just tell your governance story as it is
- Remember the purpose of the recommendations – to ensure that the market receives an appropriate level of disclosure about the corporate governance practices an entity has adopted so that:
  - security holders and other stakeholders can have a meaningful dialogue with the board and management on corporate governance matters
  - security holders can factor that information into their decision on how to vote on particular resolutions
  - investors can factor that information into their decision on whether or not to invest in the entity's securities
- Remember you can always choose not to follow a recommendation and give an “if not, why not” explanation
- Note new version of Guidance Note 9, to be issued 1 July 2014

# Thank you

