



Environmental
Defenders Office

Submission on the proposed 5th Edition of the ASX Corporate Governance Principles and Recommendations

6 May 2024

About EDO

EDO is a community legal centre specialising in public interest environmental law. We help people who want to protect the environment through law. Our reputation is built on:

Successful environmental outcomes using the law. With over 30 years' experience in environmental law, EDO has a proven track record in achieving positive environmental outcomes for the community.

Broad environmental expertise. EDO is the acknowledged expert when it comes to the law and how it applies to the environment. We help the community to solve environmental issues by providing legal and scientific advice, community legal education and proposals for better laws.

Independent and accessible services. As a non-government and not-for-profit legal centre, our services are provided without fear or favour. Anyone can contact us to get free initial legal advice about an environmental problem, with many of our services targeted at rural and regional communities.

Environmental Defenders Office is a legal centre dedicated to protecting the environment.

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EXECUTIVE SUMMARY

The Environmental Defenders Office (**EDO**) welcomes the opportunity to comment on the proposed 5th Edition of the *ASX Corporate Governance Principles and Recommendations* dated 27 February 2024 (**Consultation Draft**).

We set out below a summary of our key recommendations and detailed responses to the Consultation Draft.

SUMMARY OF RECOMMENDATIONS

Recommendation 1 – The EDO recommends that the term “sustainable value” is defined.

Recommendation 2 – The EDO welcomes the new Recommendation 3.3 that listed entities should have regard to the interests of the entity’s key stakeholders including First Nations stakeholders.

Recommendation 3 – The EDO recommends that the Commentary to Recommendation 4.2 clarifies that references to sustainability reports can include voluntary sustainability or ESG reports disclosed to the market.

Recommendation 4 – The EDO recommends that the Commentary to Recommendation 7.4 be strengthened by providing further guidance on the meaning of “material risk” and including biodiversity loss as a specific example of material risk.

DETAILED RESPONSES TO CONSULTATION DRAFT

1. Define the term “sustainable value”

The Consultation Draft gives prominence to the concept of creating sustainable value, which is essential to the interests of the entity and its security-holders. The EDO supports this approach for the 5th Edition. However, the EDO considers that a definition of sustainable value is required to ensure that the term is used consistently across all entities.

Significance of the term in the Consultation Draft

The term “sustainable value” is used in numerous key parts of the Consultation Draft, beginning with the section “What is “corporate governance”:

“Good corporate governance can contribute to the long-term sustainable value of listed entities.”¹

¹ Consultation Draft, page 5.

The Consultation Draft expressly links the creation of sustainable value with the principle of responsible business conduct and the values and culture of a listed entity. This is achieved through the following provisions:

The Commentary to Recommendation 1.1:

“Generally, the board of a listed entity should be responsible under its charter for:

[...]

- approving the entity’s statement of values and code of conduct, to underpin a desired culture within the entity that supports the creation of long-term sustainable value;”²

The Commentary to Recommendation 1.1. further states that:

“The board should oversee implementation of these strategic objectives to build sustainable value for security holders of the entity.”³

In Principle 3:

“Principle 3: Instil a culture of acting lawfully, ethically and responsibly.

A listed entity should instil and continually reinforce a culture of acting lawfully, ethically and responsibly within the organisation and in its dealings with external stakeholders, to create long-term sustainable value.”⁴

The Commentary to Recommendation 3.1:

“In formulating its values, a listed entity should consider the behaviours needed to create long-term sustainable value for its security holders.”⁵

The Commentary to Recommendation 3.2:

“Indicators of a healthy organisational culture include:

[...]

- a culture which recognises and has regard to the interests of internal and external stakeholders, to create long-term sustainable value;”⁶

The commentary to Recommendation 3.3:

² Ibid, page 10.

³ Consultation Draft, page 11.

⁴ Ibid, page 24.

⁵ Ibid, page 25.

⁶ Ibid, page 26.

“It is in the best interests of an entity to have regard to its impact and interaction with its key stakeholders, as appropriate, to support creation of long-term sustainable value for security-holders.”⁷

The EDO supports the approach taken by the ASX Corporate Governance Council (**the Council**) to give prominence to the creation of sustainable value in the Consultation Draft. Given the significance of this term, the EDO considers that including a definition is important to enable entities to interpret and apply the Principles and Recommendations consistently and to issue accurate corporate governance disclosures.

Meaning of sustainable value

The terms “sustainable” and “sustainability” are widely used in the corporate governance context, but not always clearly defined. One example is the Australian Institute of Company Directors, *Directors’ “best interests” duty in practice* (July 2022), which uses these terms at numerous points in describing the need for directors to take a long-term view of an entity’s interests.

The EDO notes that the Consultation Draft includes a description of sustainability, and that this description aligns with the Consultation Draft’s use of the term sustainable value and the connections between sustainability/sustainable value with responsible business conduct.

In this regard, the EDO supports the inclusion in the Consultation Draft of a description of sustainability by reference to how that term is construed in the draft Australian Accounting Standards Board’s ASRS1 General Requirements for Disclosure of Climate-related Financial Information and the ISSB’s IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information:

“The sustainability of an organisation considers the interactions between the entity, the resources it uses to generate value, and its relationships. For example, this includes capital management, human capital management, considering the impact of technology on business models, the entity’s impacts and dependencies on natural resources, and the interests of various stakeholders throughout the entity’s upstream and downstream value chain.”⁸

This description of sustainability is consistent with the widely accepted definition of sustainable development. Originally articulated in the Brundtland Report, sustainable development is development that “meets the needs of the present without compromising the ability of future generations to meet their own needs.”⁹

The Brundtland Report explains that “sustainable development is not a fixed state of harmony, but rather a process of change in which the exploitation of resources, the direction of investments, the orientation of technological development, and institutional change are made consistent with future as well as present needs.”¹⁰

⁷ Ibid, page 27.

⁸ Consultation Draft, page 46.

⁹ Report of the World Commission on Environment and Development (Brundtland Report): Our Common Future, 1987, paragraph 27. See <https://sustainabledevelopment.un.org/content/documents/5987our-common-future.pdf>

¹⁰ Ibid, paragraph 30.

This definition of sustainable development is used in the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, which make the specific recommendation that enterprises should contribute to economic, environmental and social progress with a view to achieving sustainable development.¹¹

Accordingly, contributing to sustainable development, i.e. the creation of value in a way that is consistent with future as well as present needs, is core to responsible business conduct. As responsible business conduct is enshrined in Principle 3 of the Consultation Draft and underpins many other aspects of the Principles and Recommendations, the various references to sustainable value demonstrate an internal consistency and logic to the approach taken in the Consultation Draft.

We encourage the Council to take the additional step of adding a clear articulation of the meaning of sustainable value to create clarity and encourage accurate and relevant corporate governance disclosures. The definition should cross-refer to the Consultation Draft's description of sustainability and refer to the widely accepted definition of sustainable development. It could be included in the Glossary to the 5th Edition.

2. Stakeholder interests

The EDO welcomes the new Recommendation 3.3 that listed entities should have regard to the interests of the entity's key stakeholders. The EDO considers that effective early and continued engagement with stakeholders and assessment of the entity's impacts upon them are essential factors in good corporate governance and risk management. It is entirely appropriate that Recommendation 3.3 requires any material issues in this regard to be reported to the Board.

The EDO notes that failure to have regard to the interests of the entity's key stakeholders can give rise to significant risks for entities, including insufficient consultation with First Nations stakeholders.¹² As such, the EDO considers that the new Recommendation strikes an appropriate balance between the interests of security holders, stakeholders and the listed entity.

3. Periodic corporate reports and assurance

The EDO supports the revisions to Recommendation 4.2 to disclose the processes for the verification of any periodic corporate report released to the market, including the extent to which a report has been the subject of audit or assurance by an external assurance practitioner. Integrity enhancing mechanisms including external assurance can provide greater confidence to investors that the information provided in periodic reports is reliable. The EDO notes that the revisions to Recommendation 4.2 are consistent with the findings and recommendations made in the Deakin Integrated Reporting Centre's White Paper on the effectiveness of communication and efficacy of integrity enhancement processes.¹³

¹¹ OECD Guidelines, 2023, page 15.

¹² See, for example, *Santos Pty Ltd v Tipakalippa* [2022] FCAFC 193 where the Full Court found that consultation with First Nations stakeholders can be a significant obligation.

¹³ Deakin Integrated Reporting Centre, Review of ASX 300 Corporate Governance Recommendation 4.3 Disclosures: Effectiveness of communication and efficacy of integrity enhancement processes, Deakin University, 2022. See https://www.deakin.edu.au/__data/assets/pdf_file/0006/2488542/8-August-2022-IRC-White-Paper_v6.pdf

The EDO recommends that the Commentary to Recommendation 4.2 clarifies that references to sustainability reports can include voluntary sustainability or ESG reports disclosed to the market as well as sustainability reports issued under the requirements for financial-related financial disclosures under Chapter 2M.3 of the Corporations Act.

4. Management of risk

The EDO supports the Council's intention to recast Recommendation 7.4 in order to improve the quality of reporting by listed entities and to enhance their risk management approach. The EDO agrees with the Council that the amended Recommendation and Commentary may assist in avoiding generic ESG disclosures and support listed entities to focus on risks that may affect the entity's prospects in the short, medium and long term.

The EDO considers that the Commentary to Recommendation 7.4 is strengthened by:

- a. providing further guidance on the meaning of material risk; and
- b. including biodiversity loss as an additional example of risk.

Meaning of material risk

The EDO supports the approach taken in Recommendation 7.4 to encourage listed entities to consider the extent of financial and non-financial risks that may be material in the short, medium and long term. In this regard, the EDO considers it helpful that the Consultation Draft directs entities to consider sustainability concepts and includes a description of sustainability.

The EDO considers that additional guidance on the meaning of material risks would further strengthen the effect of Recommendation 7.4 by ensuring the term is used consistently and encouraging better quality disclosures.

The EDO considers that the description of "material risk" in the Commentary to Recommendation 7.4 should also refer to, and be consistent with, the approach taken by the sustainability disclosure standards issued by the International Sustainability Standards Board (**ISSB**) and the Australian Accounting Standards Board (**AASB**).¹⁴ These Standards require the disclosure of information about the sustainability or climate-related risks and opportunities that could reasonably be expected to affect the entity's prospects over the short, medium and long term.¹⁵

Accordingly, the EDO recommends that the following clarifications be added to the Commentary to Recommendation 7.4:

- a. the description of "material risk"¹⁶ confirm that a material risk is that which could reasonably be expected to affect a listed entity's prospects over the short, medium and long term; and

¹⁴ ISSB IFRS S1, General Requirements for Disclosure of Sustainability-related Financial Information, and AASB ASRS 1, General Requirements for Disclosure of Climate-related Financial Information [in draft].

¹⁵ ISSB IFRS S1 paragraph 3; AASB ASRS S1 paragraph Aus3.1(a).

¹⁶ Consultation Draft, page 45.

- b. the statement “Entities that believe their prospects may not be impacted by any material environmental, social or governance risks”¹⁷ should be amended to refer to a belief that there are no risks that could reasonably be expected to affect their prospects.

Biodiversity loss as an example of risk

The EDO considers that biodiversity loss should be explicitly recognised as an example of risk for listed entities. Australia is experiencing significant biodiversity loss, and this creates material economic risks.¹⁸ While disclosure of nature-related risks under the framework of the Taskforce on Nature-related Financial Disclosures remains voluntary, directors may have a duty to disclose material nature-related risks.¹⁹

For these reasons, the EDO considers that biodiversity risk should be included as an example of contemporary and emerging risks in the Commentary to Recommendation 7.2.²⁰ Biodiversity risk should also be included as an example of risk in the Commentary to Recommendation 7.4.²¹

¹⁷ Ibid, page 46.

¹⁸ Australian Government, Taskforce on Nature-related Financial Disclosures, Pilots – Australian Case Study Report (2022), Department of Climate Change, Energy, the Environment and Water. See <https://www.dcceew.gov.au/sites/default/files/documents/tnfd-pilots-australian-case-study.pdf>

¹⁹ Legal Opinion, Nature-related risks and directors’ duties (2023), S Hartford-Davis and Z Bush. See <https://commonwealthclimatelaw.org/wp-content/uploads/2023/11/Joint-Memorandum-of-Opinion-Nature-related-risks-and-directors-duties.pdf>

²⁰ Consultation Draft, page 44.

²¹ Ibid, page 47.