

2005 Analysis of corporate governance practice disclosure

22 May 2006



EXECUTIVE SUMMARY

Key findings

The 2005 ASX review of compliance with its Listing Rules and the ASX Corporate Governance Council's (Council) ten "Principles of Good Corporate Governance" (Principles) and the twenty-eight "Best Practice Recommendations" (Recommendations) that support the Principles (Guidelines) demonstrates that listed companies are continuing to improve their corporate governance reporting. Overall reporting levels (being the aggregate of the levels of adoption of the Recommendations and the levels of 'if, not, why not' exception reporting against the Recommendations) in 2005 are higher than in 2004, with particularly strong improvements in key areas.

- **Excellent results with overall reporting improved in 2005**

The ASX review of disclosures in 2005 annual reports showed:

Overall reporting levels

- The overall reporting level for all Recommendations has increased to 88% from 84% in 2004.
- 14 out of 28 Recommendations had reporting levels over 90%
- An additional 9 out of 28 Recommendations had reporting levels over 80%
- This compares with the 2004 review where 8 out of 28 Recommendations had reporting levels over 90% and an additional 9 out of 28 Recommendations had reporting levels over 80%
- The overall reporting level increased at a faster rate among companies outside the Top 500¹.

Adoption reporting levels

- The adoption reporting level for all Recommendations increased to 74% from 68%

'If not, why not' exception reporting levels

Companies' continue to make strong use of 'if not, why not' exception reporting, that is, providing an explanation for non-adoption or describing an alternative practice. 'If not, why not' exception reporting demands that companies provide explanations that suit their circumstances and demonstrates to investors that they have considered the issues raised by the Guidelines. In particular there continues to be a strong 'if not, why not' exception reporting level in relation to:

- Recommendation 2.1 - A majority of the board should be independent directors, an 'if not, why not' exception reporting level of 47%
- Recommendation 2.4 - The board should establish a nomination committee, an 'if not, why not' exception reporting level of 57%

¹ Top 500 companies is a reference made in Listing Rule 12.7 to all companies in the S&P All Ordinaries Index at the beginning of the company's financial year.

- Recommendation 9.2 - The board should establish a remuneration committee, an ‘if not, why not’ exception reporting level of 38%.

ASX believes that this is a consequence of companies’ increased familiarity with and understanding of the Principles and a lesser focus on a “tick the box” approach.

- **Significant improvements in specific reporting levels**

Companies have improved reporting on their practices in a number of areas:

- Recommendation 3.1: Establish a code of conduct – the reporting level increased to 90% in 2005 from 78% in 2004, an increase of 12%
- Recommendation 5.1 - Establish policies and procedures to ensure compliance with the Listing Rules – the reporting level increased to 92% in 2005 from 79% in 2004, an increase of 13%
- Recommendation 6.1- Design and disclose a strategy for communicating with shareholders and encouraging participation at meetings – the reporting level increased to 91% in 2005 from 82% in 2004, an increase of 9%
- Recommendation 8.1 - Disclose the process for board and executive performance evaluation – the reporting level increased to 85% in 2005 from 73% in 2004, an increase of 12%.

ASX believes the following factors have contributed to the improved levels of reporting:

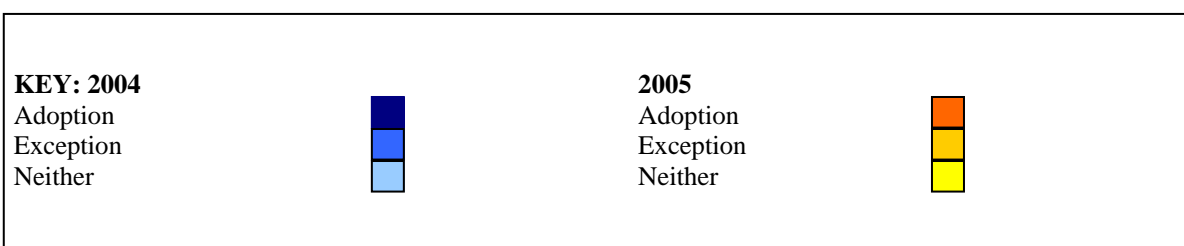
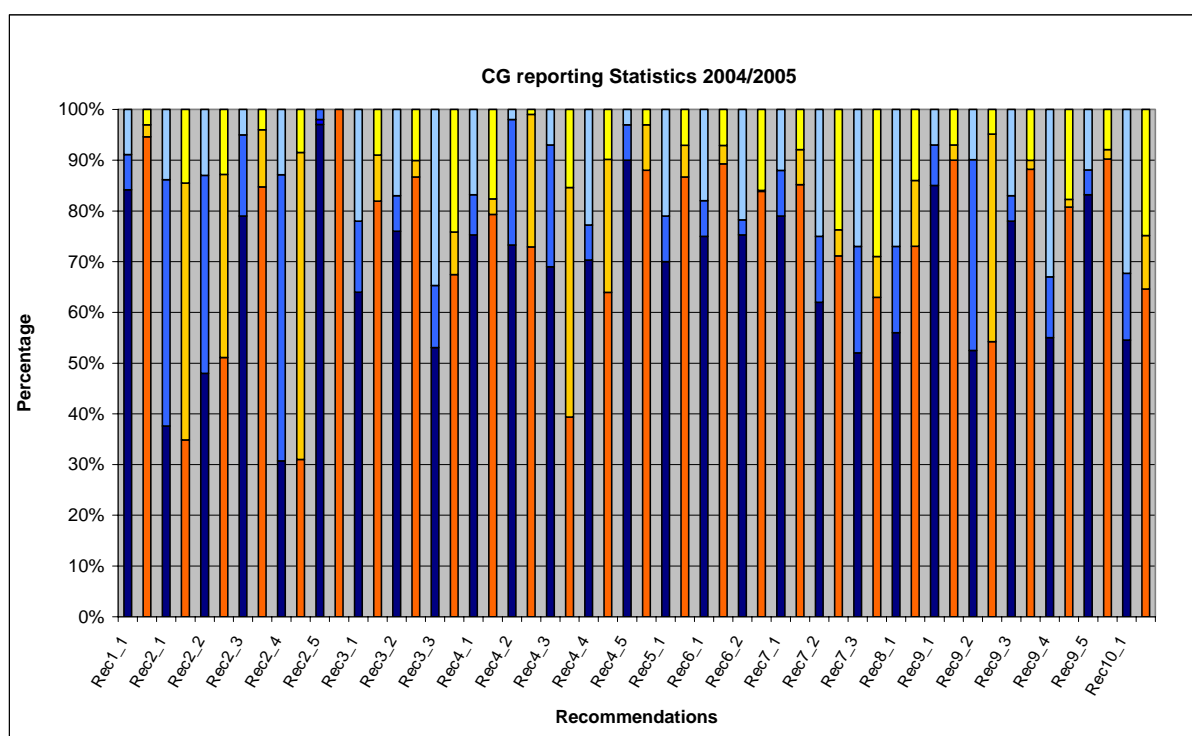
- Companies are more familiar with and better understand the Guidelines in their second year of operation
- ASX contacted over 390 entities during the 2004 review to discuss their corporate governance reporting
- ASX’s program of ongoing monitoring of corporate governance disclosures following the 2004 review
- The ongoing work of the Council in promoting disclosure of corporate governance practices.

What this report is about

This report presents an analysis of corporate governance disclosure and compliance by listed companies with ASX Listing Rules for the 2005 reporting period. It also provides commentary on the trends in disclosure and adoption reporting levels of various Recommendations between the 2004 and 2005 reporting periods as identified in the recent review of 2005 annual reports.

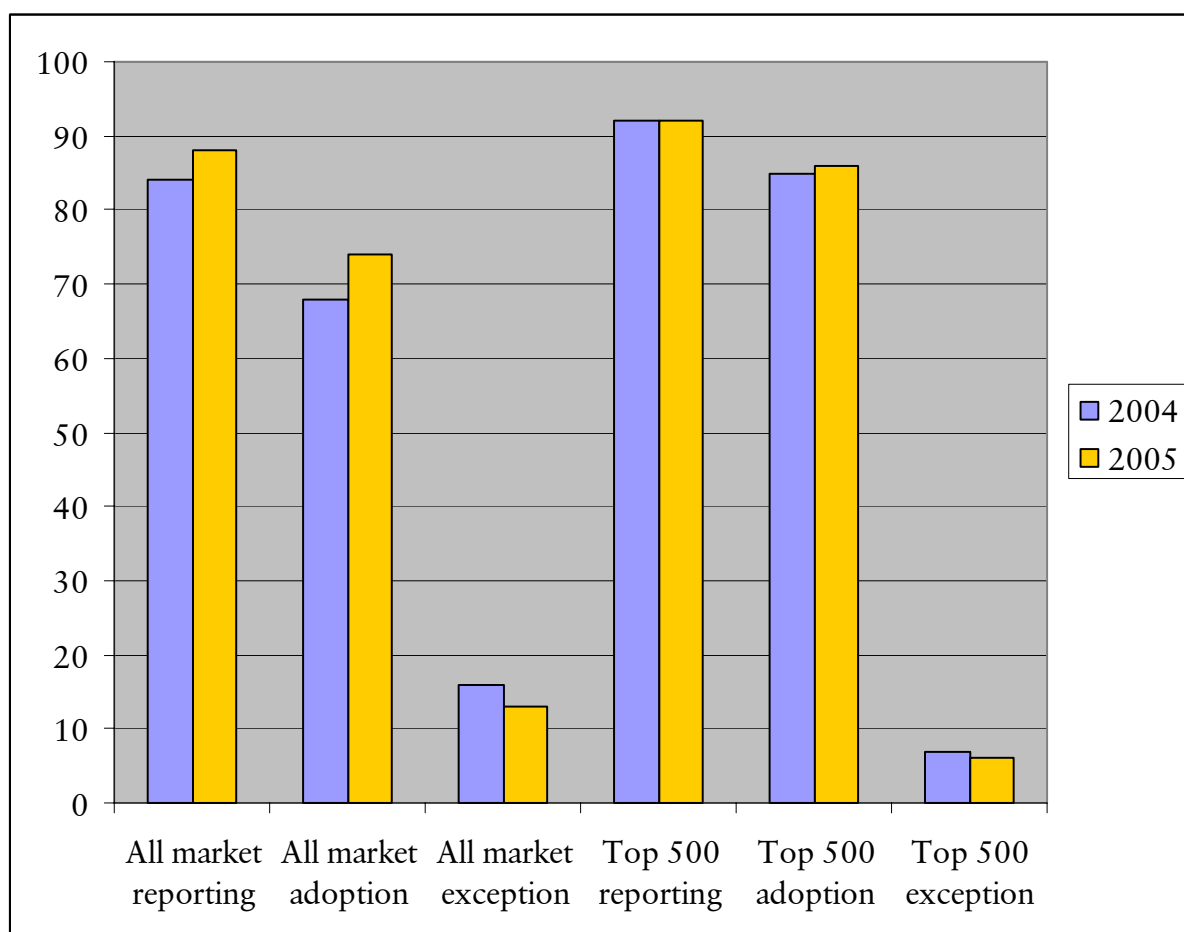
1. Overview and general observations

- 1.1. Figure 1 provides an overview of the disclosures in 2005 by all companies reviewed and compares these disclosures with the results of the 2004 review. It also distinguishes between levels of adoption of the Recommendations and levels of adoption of alternative practices (that is, providing reasons for not following a Recommendation – known as ‘if not, why not’ exception reporting).
- 1.2. The bottom colour section (navy blue in 2004 and orange in 2005) shows companies whose disclosure indicated adoption of the Recommendation. The middle colour section (mid blue in 2004 and yellow in 2005) shows ‘if not, why not’ exception reporting. The top colour section (light blue in 2004 and bright yellow in 2005) refers to companies that did not address the particular Recommendation.²



² There was a change in the methodology used for the review of Recommendation 4.3 between 2004 and 2005, in that the 2005 review applied the composition requirements under Recommendation 4.3 to companies that were not required to have an audit committee for the purposes of Listing Rule 12.7. For this reason it is not possible to make a direct comparison between the adoption reporting level for Recommendation 4.3 between 2004 and 2005.

- 1.3. A substantial majority of listed entities have fulfilled their disclosure obligations under Listing Rule 4.10.3, either by confirming adoption of the various Recommendations or by providing 'if not, why not' exception reporting.³
- 1.4. The 2005 ASX review reveals that on the basis of the annual reports reviewed, there was an overall reporting level of 88% of compliance with this Listing Rule. The reporting level of compliance with Listing Rule 4.10.3 is higher in 2005 than in 2004 - 88% compared with 84%.
- 1.5. The 2005 ASX review reveals that the adoption reporting level for all Recommendations has increased to 74% from 68% in 2004. There has been little change in the adoption reporting level by the Top 500 Companies between 2004 and 2005 - almost 85% in 2004 to 86% in 2005. This demonstrates improved adoption reporting level rates for companies outside the Top 500.



- 1.6. ASX believes the continuing strong level of 'if not, why not' exception reporting is evidence that companies are turning their minds to the Principles. In particular ASX notes continuing strong exception reporting levels in relation to:

³ Listing Rule 4.10.3 requires a company to include in its annual report a statement of the extent to which the company has followed the Council's Principles and Recommendations during the reporting period. If the company has not followed all of the recommendations, the company must identify which recommendations were not followed and give reasons. If a recommendation is only followed for part of the period the company must state the period during which it had been followed.

- Recommendation 2.1: A majority of the board should be independent directors, 47% ‘if not, why not’ exception reporting level
- Recommendation 2.4: The board should establish a nomination committee, 57% ‘if not, why not’ exception reporting level
- Recommendation 9.2: The board should establish a remuneration committee, 38% ‘if not, why not’ exception reporting level.

1.7. ASX congratulates listed entities on the overall level of reporting. ASX also notes by way of observation, the following suggestions to enhance reporting further:

- The 2005 review process indicates that companies should be encouraged to improve their compliance with Listing Rule 4.10.3 by simplifying their corporate governance statements. This could be achieved by dealing with the Recommendations consecutively on a Recommendation by Recommendation basis. Some of the better reports provided information in this format either in narrative or tabular form
- Clear cross references to the location of information not included in the corporate governance statement but located elsewhere in the annual report were also useful
- The need for greater clarity when providing corporate governance information was one of the key findings of the User Survey of professional and private investors conducted by the Council in late 2005 and released in March 2006.⁴ Other suggestions in the User Survey for improving corporate governance information included:
 - Existing information could be clearer and more concise
 - Existing information could be more accessible
 - More details about boards - board experience, independence and affiliations, commitments, share trading, committees including composition, policies and review processes
 - Clarity of information concerning remuneration of directors and key personnel
 - A summary statement of whether companies are adopting/exception reporting against the Council’s Principles and Recommendations
- Web sites are a valuable tool for disclosing many of the supporting documents referred to in the Recommendations such as board and committee charters, codes of conduct and relevant policies.

1.8. During the 2004 review, ASX identified and addressed over 1750 individual disclosure issues. Following the 2004 review, ASX has been consistent in reinforcing the requirement for corporate governance disclosure and has encouraged new and existing companies to upgrade their practices and increase their disclosure of these practices.

1.9. In managing governance disclosure issues ASX has a number of options available to it. These include:

⁴ See the Survey at www.asx.com.au/supervision/pdf/asx_corporate_governance_summary_march06

- Contacting the company to discuss the issue, emphasising education and guidance to achieve an informed market
- Encouraging the company to voluntarily make additional disclosure, where ASX identified the need for further disclosure
- Writing to the company and releasing this correspondence and the company's response to the market
- Writing to the board of the company asking for an explanation
- Exercising its power to suspend or de-list companies where there is a breach of the listing rules.

ASX has relied on each of these options to manage corporate governance disclosure issues during 2005 and 2006.

1.10. ASX and the Council have also been involved in activities that have assisted with improving compliance with the Principles and Recommendations:

- Following the 2004 review, ASX has been involved in a program of ongoing monitoring of corporate governance disclosures
- The Council has been involved in ongoing work in promoting corporate governance disclosure.

2. Commentary – Key Recommendations

A more detailed analysis of reporting on Recommendations which have generated particular interest from companies, investors and other stakeholders is set out below.

Board issues

Recommendation 2.1- A majority of the board should be independent directors

- 2.1 Principle 2 is about structuring boards to add value. Recommendation 2.1 is about boards having a majority of independent directors.
- 2.2 In 2005 the reporting level was 960 companies or 83% of entities reviewed reporting compliance with the Listing Rule either by adopting this Recommendation or by 'if not, why not' exception reporting.
- 2.3 The adoption reporting level for this Recommendation has remained reasonably static: 36% in 2005 and 38% in 2004. There continues to be a high 'if not, why not' exception reporting level of 47% in 2005.
- 2.4 The continuing high level of 'if not, why not' exception reporting demonstrates that companies are comfortable with the nature of 'if not, why not' exception reporting and the flexibility that this approach allows.
- 2.5 As in 2004, the main reason given by companies in 2005 for not adopting this Recommendation was the size of the company or the board. Other reasons given were

that in the company's circumstances non independent directors offer specialist knowledge of the business.

Committees

Recommendation 2.4 – The board should establish a nomination committee

Recommendation 9.2 – The board should establish a remuneration committee

- 2.6 The Guidelines recommend that companies establish three committees: audit, remuneration and nomination.⁵ Recommendation 2.4 is about establishing a nomination committee. This committee is responsible for matters relating to the composition of the board, the evaluation of the board and the appointment and removal of directors. Recommendation 9.2 is about establishing a remuneration committee to oversee the development and implementation of remuneration policies.
- 2.7 The 2005 review revealed a high rate of compliance with the Listing Rules in relation to Recommendations 2.4 and 9.2 with a reporting level of over 92% of companies reviewed addressing these Recommendations in some way. This is an improved reporting level on the same Recommendations in 2004. When looking at the adoption reporting levels for these Recommendations, more companies have a remuneration committee (56%) than a nomination committee (33%).
- 2.8 The results of the review indicate a majority of companies reviewed have addressed the issue of nomination and remuneration committees either by adopting the Recommendations or by 'if not, why not' exception reporting. The results again demonstrate companies' level of comfort with 'if not, why not' exception reporting.

Audit Committees

Recommendation 4.2 – The board should establish an audit committee

Recommendation 4.3 – Structure the audit committee so that it consists of: only non-executive directors, a majority of independent directors, an independent chairperson who is not chairperson of the board and at least three members

- 2.9 A key focus of the 2005 review was compliance with Listing Rule 12.7 which supports Recommendations 4.2 and 4.3.⁶
- 2.10 Recommendation 4.2 recommends that companies establish an audit committee and Recommendation 4.3 that the audit committee consists of: only non-executive directors, a majority of independent directors, a chairperson who is not chairperson of the board

⁵ See the separate discussion below on Recommendations 4.2 and 4.3 on audit committees.

⁶ Listing Rule 12.7 requires a company in the S&P All Ordinaries Index at the beginning of its financial year to have an audit committee during that year. If the company was in the Top 300 of that index at the beginning of its financial year it **must** also comply with Recommendation 4.3 in relation to composition of the audit committee. Top 300 companies is a reference made in Listing Rule 12.7 to the Top 300 companies listed in the S&P/ASX 300 at the beginning of the company's financial year. To assist companies in understanding whether they fall within this category at the commencement of the financial year the ASX provides a list of companies in this Top 300 category in the corporate governance section of the ASX web site www.asx.com.au. This list is updated for the beginning of each financial reporting period.

and at least three members. Listing Rule 12.7 requires Top 300 companies to comply with Recommendations 4.2 and 4.3. and companies in the Top 500 to comply with Recommendation 4.2. Companies outside the Top 500 are not required to have an audit committee under Listing Rule 12.7 but are required to report on their practices in relation to Recommendations 4.2 and 4.3 under Listing Rule 4.10.3.

- 2.11 Compliance with Listing Rule 4.10.3 was extremely high in relation to Recommendation 4.2 with a reporting level of approximately 98% or 1140 companies of companies reviewed addressing the issue of audit committees in some way.
- 2.12 Outside the Top 500 this reporting was in the main 'if not, why not' exception reporting with many companies disclosing that they do not have an audit committee because the board is too small or because the company has insufficient independent directors. In other examples, the Recommendation was adopted by the company but a statement made to the effect that the board as a whole performed the function of an audit committee. In recognition of this, there is an adoption reporting of level of 65% for Recommendation 4.4 - audit committee charter.
- 2.13 During the 2005 review of compliance with Listing Rule 12.7 by the Top 500 companies, ASX identified 'possible breaches' of the Listing Rule. All breaches were or are continuing to be followed up by ASX Issuers advisers and enforcement action has been taken where applicable.
- 2.14 Most of the breaches related to the composition of the audit committee in the Top 300 companies. Examples of the types of breaches followed up were:
- Insufficient number of committee members
 - The chair of the committee being the chair of the board
 - An insufficient number of independent directors on the committee
 - Insufficient disclosure of information on board composition
 - Executive directors sitting on the committee.
- 2.15 Companies followed up by ASX in relation to possible breaches have appointed additional independent directors, re-arranged their committee composition to ensure the chair is independent and have provided disclosure to the market regarding their audit committee compliance.
- 2.16 ASX notes that most breaches did not reflect a lack of diligence in relation to the Listing Rule by the relevant companies. In many cases, the breach occurred as a result of transitional arrangements in place or the time it took to appoint independent directors where there was an unexpected change in board composition.

Communications and Performance Evaluation

Recommendation 6.1 – Design and disclose a communications strategy to promote effective communication with shareholders and encourage effective participation at general meetings

Recommendation 8.1 – Disclose the process for performance evaluation of the board, its committees, individual directors, and key executives

- 2.17 Principles 6 and 8 are about communication with shareholders. Principle 6 is about companies providing shareholders with ready access to balanced and understandable information about them and their proposals. Principle 8 is about companies encouraging enhanced board and management performance and disclosing their performance evaluation process.
- 2.18 As is the case with the results of reporting on codes of conduct, the reporting and adoption levels in relation to Recommendations 6.1 and 8.1 improved significantly in 2005.
- 2.19 The reporting level for Recommendation 6.1 increased by 9% to 91%, with over 1000 of the companies reviewed disclosing their strategy for communicating with shareholders in some form.
- 2.20 The reporting level for Recommendation 8.1 increased by 12%, with over 85% of companies reviewed disclosing the process for performance evaluation in some form.
- 2.21 This improvement indicates companies' increasing recognition of the need to keep shareholders informed about their activities and policies and to have strategies in place to support the process of communication.
- 2.22 ASX encourages companies to use web sites to communicate with their shareholders about their activities and policies. Web sites also provide an efficient and cost effective way of giving shareholders as much or as little information as they require. This was reinforced in the results of the Council's User Survey.⁷

Codes of conduct

Recommendation 3.1- Establish a code of conduct to guide the directors, the chief executive officer, the chief financial officer and any other key executives as to the practices necessary to maintain confidence in the company's integrity [and] the responsibility and accountability of individuals for reporting and investigating reports of unethical practices

Recommendation 10.1 – Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders

- 2.23 Recommendations 3.1 and 10.1 both recommend that companies establish codes of conduct. Principle 3 addresses promoting ethical and responsible decision making and Principle 10 addresses the recognition of legal and other obligations to all legitimate stakeholders.
- 2.24 The reporting levels for both of these Recommendations have increased substantially since 2004. The reporting level for Recommendation 3.1 has increased by 12% to 90%. The reporting level for Recommendation 10.1 has increased by 7% to 74%.
- 2.25 The adoption reporting level for these Recommendations has also increased since 2004. The adoption reporting level for Recommendation 3.1 has increased to 82% in 2005 from 64% in 2004. The adoption reporting level for Recommendation 10.1 has also increased to 65% in 2005 from 54% in 2004.

⁷ See the Survey at www.asx.com.au/supervision/pdf/asx_corporate_governance_summary_march06

- 2.26 While there were improved reporting and adoption reporting levels for these Recommendations there was less reporting and disclosure of the content of the actual codes referred to in the annual reports.
- 2.27 ASX notes that while the reporting level for Recommendation 3.1 was 90%, the reporting level for Recommendation 3.3 was only 67% even fewer companies actually disclosed the code of conduct. There is still room for improvement in the rate of disclosure of these codes either in the annual report or on company web sites.
- 2.28 It emerged during the course of the review that companies were reporting against these two Recommendations in a way that suggests Council could provide greater clarity as to the scope of these Recommendations.

Sign – offs and risk management

Recommendation 4.1 – Require the chief executive officer and the chief financial officer to state in writing to the board that the company’s financial reports present a true and fair view, in all material respects, of the company’s financial condition and operational results and are in accordance with relevant accounting standards

Recommendation 7.2 – The chief executive officer and the chief financial officer should state to the board in writing that the statement given in accordance with ... recommendation 4.1 ... is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the board [and] the company’s risk management is operating efficiently and effectively in all material respects

- 2.29 The sign-off required under Recommendation 4.1 is complemented by the sign-off under Recommendation 7.2. Following the CLERP 9 amendments to the Corporations Act the sign-off under Recommendation 4.1 is largely mandated by law.⁸ In its current review of the Principles, Council proposes to remove or revise Recommendation 4.1. The new Section 295A of the Corporations Act effectively codifies the Recommendation 4.1 sign-off but also contains additional specific references, most notably that the financial records have been properly maintained.
- 2.30 Reporting against Recommendation 4.1 in 2005 showed an adoption reporting level of 81% of entities reviewed, with an additional 3% ‘if not, why not’ exception reporting level.
- 2.31 Reporting against Recommendation 7.2 in 2005 showed an adoption reporting level of 72% of companies, with an additional 5% ‘if not, why not’ exception reporting level. In summary, there was a reporting level of 77% of entities reporting against this Recommendation, compared with a reporting level of 75% in 2004.
- 2.32 ASX believes that there is room for further improvement in the reporting level for Recommendation 7.2. This Recommendation shows the highest rate of non-compliance

⁸ CLERP 9 introduced a new section 295A (Declaration in relation to listed entity’s financial statements by chief executive officer and chief financial officer) into *Part 3M – Financial Reporting* of the Corporations Act. The directors’ declaration under s295(4) can now only be made once the directors have received a declaration from the CEO and CFO, or equivalents that: (a) the financial records have been properly maintained, (b) the financial statements comply with accounting standards and (c) the financial records give a true and fair view.

with the Listing Rule, with over 240 or 23% of companies failing to address this Recommendation.⁹

- 2.33 One difficulty encountered in the 2005 review which was also noted as a difficulty in the 2004 review was that while the wording of Recommendations 4.1 and 7.2 requires the sign-offs to be given, it does not explicitly require companies to report on the fact of the sign-off. The Council proposes to address this issue in its current review of the Principles.¹⁰
- 2.34 As part of the current review of the Principles, Council proposes to revise Recommendation 7.2 and possibly issue further guidance. One issue Council proposes to consider is that CLERP 9 sign-off does not require disclosure or sign-off in relation to underlying risk management and internal compliance and controls and is not a substitute for Recommendation 7.2. Council proposes to consider how the Recommendation 7.2 sign-off sits in relation to Section 295A of the Corporations Act to ensure that the reporting in relation to underlying risk management and internal compliance and controls is not lost or diminished.

Recommendation 7.1 – The board or appropriate board committee should establish policies on risk oversight and management

Recommendation 7.3 – Provide an explanation of any departures from Recommendations 7.1 and 7.2 and a description of the company’s risk management policy and internal control system

- 2.35 Recommendation 7.1 recommends establishing policies on risk oversight and management and Recommendation 7.3 recommends providing an explanation of departures from Recommendations 7.1 and 7.2 and the disclosure of a description of the company’s risk management policy and internal compliance and control system.
- 2.36 As was the case in the 2004 review, the 2005 review showed that while many companies referred to responsibility for risk management (for example, a specific committee, often a combined risk and audit committee or the board as a whole being responsible), fewer companies actually reported on the policies in place or disclosed a description of these policies. The review showed a reporting level of 92% of companies reporting on risk management issues but only 63% of companies disclosed these policies. In 2004, there was a reporting level of 88% of companies reporting on risk management but only 52% disclosed these policies. This improvement from 2004 to 2005 is encouraging, but ASX feels there is scope for further work in this area.
- 2.37 Council proposes issuing further guidance or clarifying the existing guidance to take into account the difficulties companies have experienced in reporting under this Principle and a number of international and domestic developments in reporting on risk.

⁹ The 2004 review of annual reports also indicated a need for improvement in the level of reporting. The 2004 review showed that while a core group of companies made reasonably comprehensive disclosure under Recommendation 7.2, most companies provided limited, generic information. In 2004 only 18 per cent of companies disclosed their risk profile and only 32 per cent disclosed a detailed description of the system of risk management and internal control. The 2004 review found that over 20% of companies did not make an explicit statement of their risk management practices in their annual report.

¹⁰ See the discussion below on Recommendations 7.1 and 7.3.

Remuneration

Recommendation 9.1 – Provide disclosure in relation to the company’s remuneration policies to enable investors to understand the costs and benefits of those policies and the link between remuneration paid to directors and key executives and corporate performance

- 2.38 The 2005 review revealed consistently high compliance with Listing Rule 4.10.3 and the reporting levels for each of the Recommendations dealing with remuneration. This reporting was not necessarily in the corporate governance section of the annual report but was often in the remuneration report section of the directors’ report.
- 2.39 The current review by the Council of the Principles is reviewing the content of Principle 9 to consider eliminating areas of overlap between the Recommendations and the Corporations Act following the enactment of the CLERP 9 amendments and changes to the accounting standards.

Sustainability/corporate responsibility reporting

- 2.40 ASX’s review also looked at the levels of sustainability/corporate responsibility (CR) reporting. This is the first time ASX has reviewed companies’ disclosures in this area. ASX looked at whether companies are disclosing sustainability/CR information in their annual reports, and if so, whether the disclosures are in the context of the Principles. The results of the review indicate some companies are currently reporting on sustainability/CR issues in their annual reports.
- 2.41 The ASX review looked at the range of terms companies are using in their annual reports to report on these issues and at how they are reporting. A number of the Top 300 companies report on sustainability/CR issues but not necessarily in the context of a specific principle. Where companies did refer to a Principle they referred to Principles 1, 3, 4, 7 and 10 or a combination of these Principles.
- 2.42 Of the companies reviewed, 108 companies included reporting which falls in the categories: corporate responsibility, corporate social responsibility, sustainability/environmental, community or people reporting. While some of these companies refer to this type of reporting in the context of a specific principle, most did not. The sample included 151 companies of the Top 300 companies, and of those reporting in the categories: corporate social responsibility, sustainability/environmental, community or people, 47 companies (43%) of the 151 companies reporting in these categories were Top 300 companies.
- 2.43 ASX notes that its review of 2005 reporting is limited to a review of reporting in annual reports and that many companies report on sustainability/CR issues in other ways such as a separate report or on their web-site.

3 Background information

- 3.1 In May 2005, ASX produced an analysis of corporate governance practices reported in 2004 Annual Reports. The analysis was based on information gathered from 2004 Annual Reports as part of ASX’s review of compliance with its Listing Rules and the Council’s Principles and Recommendations. ASX has recently undertaken a review of 2005 Annual Reports to examine compliance with its Listing Rules and the Recommendations in relation to these reports.

- 3.2 The ASX Listing Rules contain three rules which specifically support the Principles and the Recommendations; Listing Rule 4.10.3, Listing Rule 12.7 and Listing Rule 1.1 Condition 13.
- 3.3 Listing Rule 4.10.3 requires companies to disclose in the corporate governance section of the annual report the extent to which the company has followed the Recommendations for the period covered by the report and, if a Recommendation is not followed, the reasons for not following the Recommendation. Disclosure is to be on an 'if not, why not' exception basis.
- 3.4 Listing Rule 12.7 requires that all Top 500 companies comply with Recommendation 4.2 and have an audit committee in place from the commencement of the financial year. In addition, Listing Rule 12.7 requires that the composition of the audit committee for all Top 300 companies must comply with Recommendation 4.3 and comprise only non-executive directors, a majority of independent directors, an independent chairperson who is not the chair of the board and at least three members. Listing Rule 1.1 Condition 10 is a reflection of Listing Rule 12.7 and requires newly listed companies included in either the Top 300 or Top 500 to meet similar audit committee requirements on listing.
- 3.5 Listing Rule 4.10.3 only came into effect for financial years beginning after 1 January 2003. For most companies the 2004 annual reports were the first reports to contain this information. The 2005 annual reports are, for most companies, the second year in which this information is provided.
- 3.6 Transitional provisions in place until 1 July 2005 in relation to Listing Rule 12.7 also means that the 2005 Financial Year is the first year relevant companies are required to be fully compliant with this Listing Rule.

4. Methodology

- 4.1 The results contained in this report are based on a review of annual reports with financial statements having a 30 June 2005 balance date. This involved reviewing 1162 annual reports for this period. This number represents approximately 66% of all listed entities at 30 June 2004, the total number being 1638.¹¹
- 4.2 The approach adopted by ASX in the review involved not only a review of each company's annual report but also any applicable corporate governance section of the company's web site.
- 4.3 In the first instance, the review considered compliance with the Listing Rules, in particular Listing Rule 4.10.3 was considered. A company was found to have complied with this Listing Rule in relation to a Recommendation where the company reported on its approach to the Recommendation in some form and whether it followed the Recommendation or not and, if not, provided some explanation for why not. The explanation could be in the form of reasons for non adoption of the Recommendation, for example, the company was too small to justify appointment of independent directors or in the form of a description of an alternate practice, for example, and that the whole board performs the duty of a particular committee.
- 4.4 A company is not required to adopt the Recommendation to comply with the Listing Rules. Compliance with the Listing Rule simply requires disclosure or reporting of the

¹¹ See the ASX Annual Report 2005 at page 44.

company's approach in relation to the Recommendation and if the Recommendation is not followed the reasons why the Recommendation was not followed. Compliance was measured on the basis that if a company referred to a Recommendation and indicated adoption then it was recognized as having adopted the Recommendation. If the company referred to a Recommendation and gave reasons for not adopting it or indicated an alternative way of dealing with the particular Recommendation this was regarded as 'if not, why not' exception reporting. Reporting on the adoption of a Recommendation and 'if not, why not' exception reporting are both regarded as compliant reporting for the purpose of the Listing Rules.

- 4.5 The review also looked at the adoption reporting levels for each of the Recommendations in addition to the rate of compliance with the Listing Rules.
- 4.6 Listed trusts were not included in the review and will be the subject of a separate review which will also include stapled entities and listed managed investment schemes. Companies not having a balance date of 30 June or that had been suspended or deregistered post this balance date were also excluded from the review. Each report was reviewed for disclosure in relation to each of the 28 Recommendations. This equates to almost 33,000 individual actions.

Appendix 1 - ASX Corporate Governance Council Recommendations

1.	Lay solid foundations for management and oversight
	1.1 Formalise and disclose the functions reserved to the board and those delegated to management.
2.	Structure the board to add value
	2.1 A majority of the board should be independent directors. 2.2 The chairperson should be an independent director 2.3 The roles of chairperson and chief executive officer should not be exercised by the same individual. 2.4 The board should establish a nomination committee. 2.5 Provide the information indicated in Guide to reporting on Principle 2.
3.	Promote ethical and responsible decision making
	Establish a code of conduct to guide the directors, the chief executive officer (or equivalent), the chief financial officer (or equivalent) and any other key executives as to: 3.1.1 the practices necessary to maintain confidence in the company's integrity 3.1.2 the responsibility and accountability of individuals for reporting and investigating reports of unethical practices. 3.2 Disclose the policy concerning trading in company securities by directors, officers and employees. 3.3 Provide the information indicated in Guide to reporting on Principle 3.
4.	Safeguard integrity in financial reporting
	4.1 Require the chief executive officer (or equivalent) and the chief financial officer (or equivalent) to state in writing to the board that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards. 4.2 The board should establish an audit committee. 4.3 Structure the audit committee so that it consists of: only non-executive directors, a majority of independent directors, an independent chairperson, who is not chairperson of the board, at least three members. 4.4 The audit committee should have a formal charter 4.5 Provide the information indicated in Guide to reporting on Principle 4.
5.	Make timely and balanced disclosure
	5.1 Establish written policies and procedures designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior management level for that compliance. 5.2 Provide the information indicated in Guide to reporting on Principle 5.

6.	Respect the rights of shareholders
	<p>6.1 Design and disclose a communications strategy to promote effective communication with shareholders and encourage effective participation at general meetings.</p> <p>6.2 Request the external auditor to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report.</p>
7.	Recognise and manage risk
	<p>7.1 The board or appropriate board committee should establish policies on risk oversight and management.</p> <p>7.2 The chief executive officer (or equivalent) and the chief financial officer (or equivalent) should state to the board in writing that:</p> <p>7.2.1 the statement given in accordance with best practice recommendation 4.1 (the integrity of financial statements) is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the board</p> <p>7.2.2 the company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.</p> <p>7.3 Provide the information indicated in Guide to reporting on Principle 7.</p>
8.	Encourage enhanced performance
	8.1 Disclose the process for performance evaluation of the board, its committees and individual directors, and key executives.
9.	Remunerate fairly and responsibly
	<p>9.1 Provide disclosure in relation to the company's remuneration policies to enable investors to understand (i) the costs and benefits of those policies and (ii) the link between remuneration paid to directors and key executives and corporate performance.</p> <p>9.2 The board should establish a remuneration committee.</p> <p>9.3 Clearly distinguish the structure of non-executive directors' remuneration from that of executives.</p> <p>9.4 Ensure that payment of equity-based executive remuneration is made in accordance with thresholds set in plans approved by shareholders.</p> <p>9.5 Provide the information indicated in Guide to reporting on Principle 9.</p>
10.	Recognise the legitimate interests of stakeholders.
	10.1 Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.