

Proposed Amendments to the
ASX Corporate Governance Council
Corporate Governance Principles
and
Recommendations

ASX Corporate Governance Council
Exposure Draft
22 April 2010

ABOUT THE ASX CORPORATE GOVERNANCE COUNCIL

The ASX Corporate Governance Council (Council) was formed in August 2002 and has been chaired by the Australian Securities Exchange Limited (ASX) since its inception. The Council is a diverse body, bringing together 21 business, investment and shareholder groups. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be a practical guide for listed companies, their investors and the wider Australian community. The Council's diverse membership is one of its key strengths and its modus operandi of seeking a consensus facilitates a balanced approach to regulatory and reporting affairs under the *Corporate Governance Principles and Recommendations*.

The *Corporate Governance Principles and Recommendations* provide a non-prescriptive and principles-based framework for corporate governance for listed companies. Where a listed company considers that a particular Recommendation(s) is not appropriate for its circumstances, it has the flexibility under the "if not, why not?" approach not to adopt the Recommendation(s), provided an explanation is disclosed. Consistent with ASX's disclosure-based approach, listed companies are required in the ASX Listing Rules to publish a statement in their annual reports outlining the extent to which they have adopted each Recommendation.

Council representatives include:

- Association of Superannuation Funds of Australia Ltd
- Australian Council of Superannuation Investors
- Australian Financial Markets Association
- Australian Institute of Company Directors
- Australian Institute of Superannuation Trustees
- Australian Securities Exchange
- Australian Shareholders' Association
- Australasian Investor Relations Association
- Business Council of Australia
- Chartered Secretaries Australia
- CPA Australia
- Financial Services Institute of Australasia
- Group of 100
- Institute of Actuaries of Australia
- Institute of Internal Auditors Australia
- Investment and Financial Services Association
- Law Council of Australia
- National Institute of Accountants
- Property Council of Australia
- Stockbrokers Association of Australia
- The Institute of Chartered Accountants in Australia

1. Introduction: What this Exposure Draft is About

- 1.1 In its first release of the *Corporate Governance Principles and Recommendations* in March 2003, the Council acknowledged the evolving nature of the corporate governance debate. Accordingly, the Council committed to reviewing emerging corporate governance issues to ensure the Principles remain relevant and appropriate to the Australian business community.
- 1.2 In August 2007, following an extensive review, the Council released its second edition of the *Corporate Governance Principles and Recommendations*.
- 1.3 Over the past 12 months, three significant independent reviews have been undertaken at the request of the Australian Government. The reviews focused on issues which included corporate governance practices of Australian listed entities and resulted in the following reports with recommendations relevant to the *Corporate Governance Principles and Recommendations*:
- i. The Corporations and Markets Advisory Committee (CAMAC) Report "*Diversity on Boards of Directors*" dated August 2009
 - ii. The CAMAC Report "*Aspects of Market Integrity*" dated June 2009
 - iii. The Productivity Commission Inquiry Report "*Executive Remuneration in Australia*" dated January 2010.
- 1.4 The Council has followed the policy debate on the issues under review and has examined the merit of amending the *Corporate Governance Principles and Recommendations* to implement relevant recommendations. This paper sets out the Council's proposals to amend the *Corporate Governance Principles and Recommendations* to address the particular corporate governance issues that have been identified over the past 12 months.
- 1.5 This is a revision to the second edition of the *Corporate Governance Principles and Recommendations*. This Exposure Draft is not intended to operate as a review of the second edition of the *Corporate Governance Principles and Recommendations* or a draft of a new edition. It is anticipated that the next full review of each of the *Corporate Governance Principles and Recommendations* will commence in 2012 and will result in consultation and release of the third edition of the *Corporate Governance Principles and Recommendations* by mid 2013, after four full years of operation of the second edition of the *Corporate Governance Principles and Recommendations*.

2. The Contents of the Exposure Draft

- 2.1 The first part of this paper provides an outline of the key corporate governance issues discussed and the recommendations for reform in the recent reviews, together with an overview of the key proposed amendments to the *Corporate Governance Principles and Recommendations*.
- 2.2 The second part of this paper provides the proposed amendments to the second edition of the *Corporate Governance Principles and Recommendations*, with the proposed changes marked-up.

3. The Date of Implementation

- 3.1 It is intended that the change in the reporting requirement will apply to an entity's first financial year commencing on or after 1 January 2011. Accordingly, for example, where an entity's financial year begins on 1 January, disclosure will be required in relation to the financial year ending 31 December 2011 and will be made in the annual report published by end April 2012. Similarly, where a company's financial year begins on 1 July, disclosure will be required in relation to the financial year ending 30 June 2012 and will be made in the annual report published by the end of October 2012.

- 3.2 While the formal commencement date of operation of the proposed amendments to the *Corporate Governance Principles and Recommendations* is 1 January 2011, Council considers that, especially in the case of the recommendations on diversity, listed entities with a balance date of 30 June 2010 should be able to establish a diversity policy and report against the new Recommendations in respect of the year commencing 1 July 2010. Accordingly, Council encourages listed entities to make an early transition to the proposed changes to the *Corporate Governance Principles and Recommendations*.

Time table for implementation

Date	Event
22 April 2010	Release by Council of Exposure Draft in relation to proposed amendments to the <i>Corporate Governance Principles and Recommendations</i> on dealing policies, diversity and remuneration.
22 April 2010	Release by ASX of draft listing rule amendments in relation to trading policies and remuneration committees which are either related to, or require consequential amendments to, the <i>Corporate Governance Principles and Recommendations</i> .
31 May 2010	Due date for comments in relation to Council Exposure Draft and ASX draft listing rule amendments in relation to remuneration committees.
30 June 2010	Approval and release by Council of amendments to <i>Corporate Governance Principles and Recommendations</i> on dealing policies, diversity and remuneration.
1 January 2011	Date of commencement of operation of the amendments to the <i>Corporate Governance Principles and Recommendations</i> on dealing policies, diversity and remuneration for listed entities with an annual reporting period beginning on or after 1 January 2011*. The proposed amendments to the ASX Listing Rules relating to trading policies and remuneration committees will also be effective from 1 January 2011.

* As noted above, the Council encourages companies to adopt the amendments to the *Corporate Governance Principles and Recommendations*, especially those related to diversity, at the earliest opportunity.

4. Why you should consider this Exposure Draft

- 4.1 Input from listed entities, investors and other stakeholders on the proposed changes to the *Corporate Governance Principles and Recommendations* will assist Council in ensuring that the revised Principles and Recommendations adequately reflect market sentiment, are appropriately designed and are expected to be effective in delivering the stated objectives.

INVITATION TO COMMENT

The ASX Corporate Governance Council is seeking comments on the proposed changes to the *Corporate Governance Principles and Recommendations* put forward in this paper by:

- close of business Friday, 31 May 2010.

Submissions can be forwarded to:

- regulatorypolicy@asx.com.au

or

ASX Regulatory & Public Policy Unit
Level 7, 20 Bridge Street
SYDNEY NSW 2000

The Council prefers to receive comments in electronic form.

For enquiries, please call Carl Gray on +61 2 9227 0622.

Comments on the draft listing rule amendments relating to remuneration committees released by ASX on 22 April 2010 should also be sent to regulatorypolicy@asx.com.au by 31 May 2010. For enquiries in relation to the proposed amendments to the Listing Rules, please call Diane Lewis on +61 2 9227 0154.

Confidentiality

It will be assumed that submissions are not confidential and may be made publicly available. If you would like your submission, or any part of it, to be treated as 'confidential' please indicate this clearly.

The *Corporate Governance Principles and Recommendations* will be referred to as the Principles and Recommendations throughout the remainder of this Exposure Draft.

PROPOSED CHANGES TO THE PRINCIPLES AND RECOMMENDATIONS

Recent Developments

1. CAMAC Report on “Aspects of Market Integrity”

- 1.1 On 30 July 2009, CAMAC publicly released its report on “Aspects of Market Integrity”. The report addresses the effect of a number of market practices on the integrity of the Australian financial market, including directors entering into margin loans, trading by company directors in “blackout” periods, spreading false or misleading information, and corporate briefings to analysts in response to advice sought from the then Minister for Superannuation and Corporate Law.
- 1.2 Following the release of the report, Council considered the aspects of the report relevant to the matters covered by the second edition of the Principles and Recommendations and, in particular, focused on CAMAC’s analysis and recommendations on trading by company directors in blackout periods. The Council also considered the issues surrounding corporate briefings of analysts, where the briefings may create the perception that material information is being disclosed selectively and is not available to other analysts, shareholders and the public.
- 1.3 The Council formed a sub-committee to consider the issues raised in the CAMAC report on “Aspects of Market Integrity”.
- 1.4 In relation to blackout trading, the Australian Securities Exchange (ASX) also has examined the case for introducing minimum requirements for the adoption and disclosure of trading policies that provide for restrictions on trading by directors and other key management personnel during sensitive periods. ASX has concluded that the introduction of such requirements under the ASX Listing Rules would be beneficial in addressing both the perception of, and the potential for, insider trading. ASX’s proposal to introduce trading policy requirements under the ASX Listing Rules was set out in the ASX Public Consultation Paper “Listing Rule Amendments – Company Policies on Trading Windows and Blackout Periods” dated 4 December 2009.

Details of the revision to the proposed amendments to take account of submissions are to be released on 22 April 2010.

http://www.asx.com.au/about/pdf/20091203_asx_consultation_paper_listing_rule_amendments.pdf

2. CAMAC Report on “Diversity on Boards of Directors”

- 2.1 On 13 August 2009, CAMAC released its report on “Diversity on Boards of Directors”. The report examined the issue of diversity on boards, with a particular focus on the participation of women. It discussed the role and structure of boards, the current state of diversity, ways of promoting greater board diversity and ways to assist in developing a broader pool of skilled and experienced candidates. In the report, CAMAC concluded 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”.
- 2.2 One of the main objectives of the CAMAC review was to provide advice on options for addressing the current lack of gender diversity on corporate boards. The report notes that the proportion of women on the boards of the ASX top 200 listed entities is 8.3%, which is down from 8.7% in 2006. CAMAC also noted that the proportion of women represented in the ASX top 200 listed entities has remained in the 8% band since 2002.
- 2.3 The CAMAC report put forward three proposals for further developing the commentary in the Principles and Recommendations:
 - (i) *consideration of board diversity matters* – CAMAC suggested that an explicit reference to board diversity be included in the commentary on the board nomination committee;
 - (ii) *a more structured approach to candidate selection* – CAMAC suggested that the commentary on the board nomination committee also include discussion of the benefits of the board nomination committee

undertaking a more structured approach to identifying the pool of candidates for board positions, including the possible use of consulting firms; and

- (iii) *information to shareholders* – CAMAC suggested that the guidance on the information to be provided to shareholders in voting for board candidates could be expanded to cover, among other things, a statement by the board of the skills it is looking for in any new appointment to the board and the steps taken to ensure that a range of candidates was considered.
- 2.4 The Council formed a sub-committee to consider the CAMAC proposals and representations made by a number of other stakeholders on the issue of diversity, and to report back to the Council with options for amending the Principles and Recommendations.
 - 2.5 The Council reviewed a recent report released by Goldman Sachs JB Were titled “Australia’s Hidden Resource: The Economic Case for Increasing Female Participation” dated 26 November 2009, which focused on the economic impact of improving gender diversity within Australia’s workforce. It was estimated that closing the gap between male and female employment rates “would boost the level of Australian GDP by 11%”. The report recommended a minimum quota of two female positions per board in Australia’s top 200 listed entities, and believed “mentoring and visibility of females would encourage a lift in female participation”.
 - 2.6 Council has taken note also of initiatives to promote gender diversity on company boards in other developed economies. Norway introduced a quota system, which required public companies to have boards comprised of up to 40% of female directors by 1 January 2008. In December 2009, France introduced legislation in parliament, which required women to comprise 50% of the board of directors of publicly listed companies by 2015. Spain has also introduced a regulatory requirement that private companies awarded public contracts must have at least 40% of their board of directors comprised of women by 2015. The Spanish Government also established a Special Working Group to provide advice to the National Securities Market Commission on gender diversity issues. The Special Working Group issued a Unified Code of Corporate Governance for publicly listed companies, which takes a similar approach to that proposed in this exposure draft. On 16 December 2009, the US Securities and Exchange Commission released rule amendments that require disclosure of whether and, if so, how a nomination committee considers diversity in identifying nominees for director.
 - 2.7 Following consideration by the sub-committee, the Council has concluded that the Principles and Recommendations should be amended to include a recommendation that companies establish and disclose a policy concerning diversity, which includes measurable objectives for gender diversity. The Council is of the view that there is a strong case for including a recommendation in the Principles and Recommendations calling for companies to include in their annual reports details of the proportion of women on the board, in senior executive positions and employed in the whole organisation. The Council considers that an ‘if not, why not’ requirement for the establishment of measurable objectives, together with recommendations promoting greater transparency of such policies and companies’ achievements against their objectives, will help facilitate shareholders, and the market more generally, to play a role in promoting greater gender diversity on boards and within senior management.
 - 2.8 The Council also proposes that commentary and guidance in the Principles and Recommendations be expanded to include consideration of diversity in candidate selection processes for board appointments.
- 3. **Productivity Commission Report on “Executive Remuneration in Australia”**
 - 3.1 On 4 January 2010, the Productivity Commission released its final report on “Executive Remuneration in Australia”. The report examined the trends in and existing regulatory framework for director and executive remuneration in Australia, and recommended a suite of corporate governance reforms aimed at reducing conflicts of interests, improving board accountability, enhancing disclosure and enhancing shareholder engagement.

- 3.2 The Council formed a sub-committee to consider the Productivity Commission Discussion Draft. Council made a submission to the Productivity Commission in response to the Discussion Draft focusing on Recommendations 2, 3, 10 and 11. Council raised concerns regarding Recommendation 10 that expert advisers be disclosed and highlighted the potential for the complexities related to such disclosure leading to an unintended consequence of discouraging expert advice being sought by companies.
- 3.3 While the Productivity Commission's recommendations underpinned the central role of boards in setting executive remuneration and in ensuring an efficient labour market for executives, the Commission did recommend measures aimed at strengthening the integrity of remuneration setting by boards and enhancing the effectiveness of boards' engagement with their shareholders to help maintain investor and broader public confidence in the corporate sector. Two of these recommendations called for amendments to the Principles and Recommendations:
- Recommendation 2* of the report suggests the introduction of an 'if not, why not' recommendation specifying the composition of the remuneration committee; and
- Recommendation 10* of the report suggests the introduction of an 'if not, why not' recommendation for companies to disclose information regarding the use of expert advisers in the remuneration of directors and key management personnel.
- 3.4 On 16 April 2010, the Australian Government responded to the Productivity Commission's Inquiry Report on "Executive Remuneration in Australia". In relation to Recommendation 2 above, the Government provided in principle support, but noted that this is a matter for the ASX Corporate Governance Council. In relation to Recommendation 10 above, the Government indicated its intention to amend the *Corporations Act 2001* to introduce the requirements included in the Recommendation and introduce additional disclosure obligations in relation to the fees paid to remuneration consultants. In light of the Government's decision, this Exposure Draft only addresses Recommendation 2 above.

Overview of Key Changes by Principle

4. Principle 2 – Structure the board to add value

- 4.1 The proposed changes to Principle 2 are focused on promoting board diversity, with a particular focus on gender diversity. Council proposes to extend the commentary and guidance associated with Recommendation 2.4 in defining the responsibilities of any nomination committee to include making recommendations to the board about strategies to address board diversity. It is proposed also that the commentary on the charter for any nomination committee be revised to recommend that the charter provide for regular review of the proportion of women employed at all levels of the company. It is proposed further that the commentary on board renewal is amended to include diversity as an issue that a nomination committee should consider in its succession planning. Council considers that supporting and developing the feeder pool of female senior executives within organisations and developing succession plans which include diversity objectives are important elements in promoting board diversity.
- 4.2 In relation to the commentary on the information that should be provided to shareholders for the purpose of electing directors, Council proposes to include an item in the list suggesting that companies provide a statement by the board as to whether it supports the nomination of the proposed candidate(s).
- 4.3 It is proposed that the commentary and guidance associated with Recommendation 2.5 be amended to include diversity objectives at all levels in the company as a measure against which the performance of the board should be reviewed regularly. Council considers that increasing board accountability for diversity objectives is an important element in delivering improvements in diversity on boards and at all levels of companies. In the commentary on 'induction and education', it is proposed that director induction programs should include topics on 'the culture and values of the company', and 'meeting arrangements and director interaction'.

4.4 It is proposed that the “Guide to reporting on Principle 2” be amended to require that companies disclose the mix of skills and diversity for which the board is looking for in its membership. The objective of this proposed amendment is to encourage more transparent board appointment processes that would facilitate consideration of candidates from a more diverse pool of candidates.

5. Principle 3 – Promote ethical and responsible decision making

Trading Policies

5.1 Council proposes to delete Recommendation 3.2, the associated commentary and Box 3.2 “Suggestions for the content of a trading policy” upon the introduction of ASX’s proposed ASX Listing Rules for the adoption and disclosure of company trading policies in order to avoid any overlap and duplication between the amended Listing Rules and the Principles and Recommendations. As indicated in the ASX Public Consultation Paper “Listing Rule Amendments – Company Policies on Trading Windows and Blackout Periods”, dated 4 December 2009, ASX will be covering the content of Recommendation 3.2 and much of the associated commentary of the Principles and Recommendations in a listing rule and an associated guidance note. ASX also will be providing guidance in the proposed guidance note on how companies should address in their trading policies trading in derivative products consistent with the approach taken to these issues in item 7 from Box 3.2 of the Principles and Recommendations. ASX also will review the proposed legislation foreshadowed by the Government on 16 April 2010 in relation to hedging over unvested entitlements by directors and executives as to whether it leaves any need for ASX to include the substance of what currently appears as item 8 from Box 3.2 in its proposed guidance note. The Council is supportive of ASX’s proposal to address the issues related to items seven and eight from Box 3.2 in this way. Overall, the Council is supportive of ASX addressing the issues raised in the CAMAC report on “Aspects of Market Integrity” relating to “blackout” trading by way of principles-based and disclosure-based listing rule requirements.

Diversity

5.2 The Council proposes the introduction of a new Recommendation 3.2, which requires companies to establish a diversity policy that includes measurable objectives in relation to gender diversity. The Council considers that an ‘if not, why not’ recommendation for the establishment of a diversity policy with measurable objectives for gender diversity provides a balanced approach by allowing boards to develop policies and objectives appropriate for their circumstances, and provides a mechanism for increased transparency and accountability, which will be integral in driving improvements.

5.3 The Council proposes a new Recommendation 3.3, which requires companies to report their achievements against their measurable objectives on gender diversity in their annual report. Council also proposes a new Recommendation 3.4, which requires companies to disclose the proportion of women employees in the organisation, in senior executive positions and on the board. This disclosure should be meaningful and Council encourages companies to make disclosure which is relevant to the organisation, for example, disclosing the proportion of women employees on a full-time employee basis and by job category or seniority. Council is of the view that increased transparency is a key component in driving the success of the initiatives because it enables shareholders to monitor company performance with regard to gender diversity.

6. Principle 6 – Respect the rights of shareholders

6.1 It is proposed that Box 6.1 on ‘Using electronic communications effectively’ be amended to include a new sub-point suggesting that companies consider arranging for advance notification of group briefings and make them widely accessible, including through the use of web casting through the internet and / or conference calls. The Council considers that this amendment addresses the concerns raised by CAMAC in its report on “Aspects of Market Integrity” in relation to shareholders not being properly informed of corporate briefings provided to analysts and any resulting inequity in disclosure. The Council considers that these issues are best addressed by companies in their shareholder communication policies.

6.2 Council also proposes to amend Box 6.1 to include a new sub-point suggesting that companies keep a record of the topics discussed at briefings with investors and analysts, including a record of those present, and the time and place of the meeting. The Council takes a similar position to CAMAC on the issue and is of the view that record keeping of this nature would be useful in assisting Companies to comply with the insider trading and continuous disclosure provisions of the Corporation Act.

7. Principle 8 – Remunerate fairly and responsibly

7.1 Council proposes to elevate the existing commentary and guidance in Principle 8 on the composition of the remuneration committee to a new Recommendation 8.2. It is proposed that new commentary be included highlighting the potential for conflict of interest in having executive directors serve on the remuneration committee. Council discussed the Recommendation put forward by the Productivity Commission for the compositional requirement that remuneration committees should be comprised solely of non-executive directors, but came to the view that a majority of smaller listed entities would face difficulty complying with this without hiring additional directors to serve on their boards. Council sees this as effectively prescribing for listed entities to appoint a minimum number of three non-executive directors in order to be in a position to adopt the Council's Principles and Recommendations. Such prescription would contribute to increased regulatory costs and may pose an inappropriate burden on smaller listed entities. Council also is of the view that such a prescriptive approach is not necessary to achieve the underlying policy objective articulated by the Productivity Commission of ensuring that independent directors have a significant influence on remuneration decisions. Council also decided that it would be more appropriate to include the Productivity Commission's recommendation relating to the charter of the remuneration committee setting out procedures for non-committee members attending meetings, as part of Council's commentary and guidance rather than include it as a new recommendation with a reporting requirement.

7.2 Council notes that ASX has decided to make it mandatory for ASX top 300 companies to have a remuneration committee comprised solely of non-executive directors, consistent with the Productivity Commission's Recommendation 3. These companies currently represent about 90% of the aggregate market capitalisation of companies listed for quotation on ASX.

7.3 Council acknowledges that there is an expectation on listed entities to introduce more rigorous corporate governance practices as they grow and develop, and encourages companies outside of the ASX top 300 to put in place a procedure for adopting practices, such as considering the appointment of non executive directors sufficient to enable them to comply with the proposed ASX listing rule, relating to remuneration committees.

7.4 Council has invited ASX to take the opportunity to consult on whether it should be mandatory under the ASX Listing Rules for ASX top 500 companies to have a remuneration committee as a step in the growth and development of corporate governance practices appropriate to the stage of development of those companies and their place in the capital market. ASX has adopted the suggestion and will invite comments on this issue in its release scheduled for 22 April 2010.

Request for Comments

To enable Council to refine its views, Council invites comments on any of the proposed amendments raised in this Exposure Draft.

MARKED-UP AMENDED PRINCIPLES AND RECOMMENDATIONS

Principle 2: Structure the board to add value

Companies should have a board of an effective composition, size and commitment to adequately discharge their responsibilities and duties.

An effective board is one that facilitates the effective discharge of the duties imposed by law on the directors and adds value in a way that is appropriate to the particular company's circumstances. The board should be structured in such a way that it:

- has a proper understanding of, and competence to deal with, the current and emerging issues of the business
- exercises independent judgement
- encourages enhanced performance of the company
- can effectively review and challenge the performance of management.

Ultimately the directors are elected by the shareholders. However the board and its delegates play an important role in the selection of candidates for shareholder vote.

Recommendation 2.1:

A majority of the board should be independent directors¹.

Commentary

Independent decision-making

All directors – whether independent or not - should bring an independent judgement to bear on board decisions.

To facilitate this, there should be a procedure agreed by the board for directors to have access in appropriate circumstances to independent professional advice at the company's expense.

Non-executive directors should consider the benefits of conferring regularly without management present, including at scheduled sessions.² Their discussions can be facilitated by the chair or lead independent director, if any.

Independent directors

An independent director is a non-executive director who is not a member of management, and who is free of any business or other relationship that could materially interfere with - or could reasonably be perceived to materially interfere with - the independent exercise of their judgement.

Relationships which may affect independent status are set out in Box 2.1.

Directors considered by the board to be independent should be identified as such in the corporate governance statement in the annual report. The board should state its reasons if it considers a director to be independent notwithstanding the existence of relationships listed in Box 2.1 and the corporate governance statement should disclose the existence of any such relationships. In this context, it is important for the board to consider materiality thresholds from the perspective of both the company and its directors, and to disclose these.³

¹ A series of relationships affecting independent status are set out in Box 2.1.

² At times it may be appropriate for the independent directors to meet without other directors present.

³ For example, a board may decide that affiliation with a business which accounts for, say, less than X% of the company's revenue is, as a category, immaterial for the purpose of determining independence. If the company discloses the standard it follows and makes a general statement that the relevant director meets that standard, investors are better informed about the board's reasoning.

Box 2.1: Relationships affecting independent status⁴

When determining the independent status of a director the board should consider whether the director:

1. is a substantial shareholder of the company or an officer of, or otherwise associated directly with, a substantial shareholder of the company⁵
2. is employed, or has previously been employed in an executive capacity by the company or another group member, and there has not been a period of at least three years between ceasing such employment and serving on the board
3. has within the last three years been a principal of a material professional adviser or a material consultant to the company or another group member, or an employee materially associated with the service provided
4. is a material supplier or customer of the company or other group member, or an officer of or otherwise associated directly or indirectly with a material supplier or customer
5. has a material contractual relationship with the company or another group member other than as a director of the company.

Family ties and cross-directorships may be relevant in considering interests and relationships which may compromise independence, and should be disclosed by directors to the board.

Regular assessments

The board should regularly assess whether each non-executive director is independent. Each non-executive director should provide to the board all information that may be relevant to this assessment.

If a director's independent status changes, this should be disclosed and explained to the market in a timely fashion.

Recommendation 2.2:

The chair should be an independent director.

Commentary

Role of Chair

The chair is responsible for leadership of the board and for the efficient organisation and conduct of the board's functioning.

The chair should facilitate the effective contribution of all directors and promote constructive and respectful relations between directors and between board and management.

Where the chair is not an independent director, it may be beneficial to consider the appointment of a lead independent director.

The role of chair is demanding, requiring a significant time commitment. The chair's other positions should not be such that they are likely to hinder effective performance in the role.

Recommendation 2.3:

The roles of chair and chief executive officer should not be exercised by the same individual.

⁴ The relationships affecting independent status in Box 2.1 are adapted from the definition of independence given by Corporate Governance, A Guide for Fund Managers and Corporations – Blue Book, Investment and Financial Services Association, 2004 at www.ifsa.com.au.

⁵ For this purpose a "substantial shareholder" is a person with a substantial holding as defined in section 9 of the Corporations Act.

Commentary

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 such employment and serving on the board.

Recommendation 2.4:

The board should establish a nomination committee.

Commentary

Purpose of the nomination committee

A board nomination committee is an efficient mechanism for examination of the selection and appointment practices of the company.

Ultimate responsibility for these practices, however, rests with the full board, whether or not a separate nomination committee exists.

For smaller boards, the same efficiencies may not be derived from a formal committee structure. Companies without a nomination committee should have board processes in place which raise the issues that would otherwise be considered by the nomination committee.

Charter

The nomination committee should have a charter that clearly sets out its roles and responsibilities, composition, structure, membership requirements and the procedures for inviting non-committee members to attend meetings.

The terms of reference of the nomination committee should allow it to have access to adequate internal and external resources, including access to advice from external consultants or specialists.

[The charter should provide for regular review of and reporting to the board about the proportion of women at all levels of the company.](#)

Composition of nomination committee

The nomination committee should be structured so that it:

- consists of a majority of independent directors
- is chaired by an independent director
- has at least three members.

Responsibilities

Responsibilities of the committee should include recommendations to the board 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
- the appointment and re-election of directors
- [strategies to address board diversity.](#)

Selection and appointment process and re-election of directors

A formal and transparent procedure for the selection, appointment and re-appointment of directors to the board helps promote investor understanding and confidence in that process.

Important issues to be considered as part of the process include:

- Director competencies

In order to be able to discharge its mandate effectively the board should comprise directors possessing an appropriate range of skills and expertise. The nomination committee should consider implementing a plan for identifying, assessing and enhancing director competencies.

An evaluation of the range of skills, experience and expertise on the board is important when considering new candidates for nomination or appointment. Such an evaluation enables identification of the particular skills that will best increase board effectiveness.

- Board renewal

Board renewal is critical to performance, and directors should be conscious of the duration of each director's tenure in succession planning.

The nomination committee should consider whether succession plans are in place to maintain an appropriate **balance mix** of skills, experience, ~~and~~ expertise and diversity on the board.

- Composition and commitment of the board

The board should be of a size and composition that is conducive to making appropriate decisions. The board should be large enough to incorporate a variety of perspectives and skills, and to represent the best interests of the company as a whole rather than of individual shareholders or interest groups. It should not, however, be so large that effective decision-making is hindered.

Individual board members should devote the necessary time to the tasks entrusted to them. All directors should consider the number and nature of their directorships and calls on their time from other commitments.

In support of their candidature for directorship or re-election, non-executive directors should provide the nomination committee with details of other commitments and an indication of time involved. Prior to appointment or being submitted for re-election non-executive directors should specifically acknowledge to the company that they will have sufficient time to meet what is expected of them.

The nomination committee should regularly review the time required from a non-executive director, and whether directors are meeting that requirement. Non-executive directors should inform the chair and the chair of the nomination committee before accepting any new appointments as directors.

- *Election of directors* - The names of candidates submitted for election as directors should be accompanied by the following information to enable shareholders to make an informed decision on their election:
 - biographical details, including competencies and qualifications and information sufficient to enable an assessment of the independence of the candidate
 - a statement by the board as to whether it supports the nomination of the proposed candidate(s)
 - details of relationships between:
 - the candidate and the company, and
 - the candidate and directors of the company
 - directorships held ⁶
 - particulars of other positions which involve significant time commitments

⁶ These are directorships required to be disclosed by law, and any other directorships relevant to an assessment of independence.

- the term of office currently served by any directors subject to re-election
- any other particulars required by law.⁷

Non-executive directors should be appointed for specific terms subject to re-election and to the ASX Listing Rules and Corporations Act provisions concerning removal of a director.

Re-appointment of directors should not be automatic.

Recommendation 2.5:

Companies should disclose the process for evaluating the performance of the board, its committees and individual directors.

Commentary

The performance of the board should be reviewed regularly against appropriate measures. [These measures should include gender diversity objectives at all levels in the company.](#)

Induction and education

Induction procedures should be in place to allow new directors to participate fully and actively in board decision-making at the earliest opportunity.

To be effective, new directors need to have a good deal of knowledge about the company and the industry within which it operates. An induction program should be available to enable new directors to gain an understanding of:

- the company's financial, strategic, operational and risk management position
- [the culture and values of the company](#)
- the rights, duties and responsibilities of the directors
- the roles and responsibilities of senior executives
- the role of board committees
- [meeting arrangements and director interaction.](#)

Directors should have access to continuing education to update and enhance their skills and knowledge. [This should include education concerning key developments in the company and in the industry and environment within which it operates.](#)

Access to information

The board should be provided with the information it needs to discharge its responsibilities effectively.

Senior executives should supply the board with information in a form and timeframe, and [the information should be](#) of a quality that enables the board to discharge its duties effectively. Directors are entitled to request additional information where they consider such information necessary to make informed decisions.

⁷ The *Guidelines for notices of meeting* at www.asx.com.au are designed to assist communication with shareholders and contain guidance on framing resolutions for the election of directors.

The board and the company secretary

The company secretary plays an important role in supporting the effectiveness of the board by monitoring that board policy and procedures are followed, and coordinating the timely completion and despatch of board agenda and briefing material.

It is important that all directors have access to the company secretary.

The appointment and removal of the company secretary should be a matter for decision by the board as a whole.

The company secretary should be accountable to the board, through the chair, on all governance matters.

Recommendation 2.6:

Companies should provide the information indicated in the Guide to reporting on Principle 2.

Guide to reporting on Principle 2

The following material should be included in the corporate governance statement in the annual report:

- the skills, experience and expertise relevant to the position of director held by each director in office at the date of the annual report
- the names of the directors considered by the board to constitute independent directors and the company's materiality thresholds
- the existence of any of the relationships listed in Box 2.1 and an explanation of why the board considers a director to be independent, notwithstanding the existence of these relationships
- [a statement as to the mix of skills and diversity for which the board of directors is looking to achieve in membership of the board](#)
- a statement as to whether there is a procedure agreed by the board for directors to take independent professional advice at the expense of the company
- the period of office held by each director in office at the date of the annual report
- the names of members of the nomination committee and their attendance at meetings of the committee, or where a company does not have a nomination committee, how the functions of a nomination committee are carried out
- whether a performance evaluation for the board, its committees and directors has taken place in the reporting period and whether it was in accordance with the process disclosed
- an explanation of any departures from Recommendations 2.1, 2.2, 2.3, 2.4, 2.5 or 2.6.

The following material should be made publicly available, ideally by posting it to the company's website in a clearly marked corporate governance section:

- a description of the procedure for the selection and appointment of new directors and the re-election of incumbent directors
- the charter of the nomination committee or a summary of the role, rights, responsibilities and membership requirements for that committee
- the board's policy for the nomination and appointment of directors

Application of Principle 2 in relation to trusts and externally managed entities

References to "board" and "directors" should be applied as references to the board and directors of the responsible entity of the trust and to equivalent roles in respect of other externally managed entities.

There may be technical conflict in implementing the Recommendations that a director be independent and that the chair be an independent director or a lead independent director, where the manager or responsible entity is a wholly-owned subsidiary of a parent company such as a fund manager and all the directors are employees of the parent. This should be discussed and clarified in any explanation of departure from the Recommendations included in the corporate governance statement in the annual report.

Principle 3: Promote ethical and responsible decision-making

Companies should actively promote ethical and responsible decision-making.

To make ethical and responsible decisions companies should not only comply with their legal obligations, but should also consider the reasonable expectations of their stakeholders including; shareholders, employees, customers, suppliers, creditors, consumers and the broader community in which they operate. It is a matter for the board to consider and assess what is appropriate in each company's circumstances. It is important for companies to demonstrate their commitment to appropriate corporate practices and decision making.

Companies should:

- clarify the standards of ethical behaviour required of the board, senior executives and all employees and encourage the observance of those standards
- comply with their legal obligations and have regard to the reasonable expectations of their stakeholders
- publish the policy concerning the issue of board and employee trading in company securities and in associated products, including products which operate to limit the economic risk of those securities.

Recommendation 3.1:

Companies should establish a code of conduct and disclose the code or a summary of the code as to:

- the practices necessary to maintain confidence in the company's integrity
- the practices necessary to take into account their legal obligations and the reasonable expectations of their stakeholders
- the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

Commentary

Purpose of a code of conduct

Good corporate governance ultimately requires people of integrity. Personal integrity cannot be regulated. However, investor confidence can be enhanced if the company clearly articulates acceptable practices for directors, senior executives and employees.

The board has a responsibility to set the ethical tone and standards of the company. Senior executives have a responsibility to implement practices consistent with those standards. Company codes of conduct which state the values and policies of the company can assist the board and senior executives in this task and complement the company's risk management practices.

Application of a code of conduct

Companies should formulate policies on the appropriate behaviour of directors, senior executives and employees. Companies should also encourage the integration of these policies into company-wide management practices. A code of conduct, supported by appropriate training and monitoring of compliance with the code are effective ways to guide the behaviour of directors, senior executives and employees and demonstrate the commitment of the company to ethical practices. Companies should ensure that training on the code of conduct is updated on a regular basis.

Companies should consider making advisers, consultants and contractors aware of the company's expectations as set out in the code of conduct.

It is not necessary for companies to establish a separate code for directors and senior executives. Depending on the nature and size of the company's operations, the code of conduct for directors and senior executives may stand alone or be part of the corporate code of conduct.

Suggestions for the content of a code of conduct are set out in Box 3.1.

Box 3.1: Suggestions for the content of a code of conduct

Companies may find it useful to consider the following matters when formulating a code of conduct:

1. Give a clear commitment by the board and senior executives to the code of conduct. This is often linked to statements about the aspirations or objectives of the company, its core values, and its views about the expectations of shareholders, employees, customers, suppliers, creditors, consumers and the broader community.
2. Detail the company's responsibilities to shareholders and the financial community generally. This might include reference to the company's commitment to delivering shareholder value and how it will do this, and the company's approach to accounting policies and practices, and disclosure.
3. Specify the company's responsibilities to shareholders, employees, customers, suppliers, creditors, consumers and the broader community. This might include reference to standards of product quality or service, commitments to fair value, fair dealing and fair trading and the safety of goods produced.
4. Describe the company's approach to the community. This might include environmental protection policies, support for community activities, and donation or sponsorship policies
5. Articulate the company's responsibilities to the individual. This might include the company's privacy policy, and its policy on the use of privileged or confidential information.
6. Outline the company's employment practices. This might include reference to occupational health and safety, employment opportunity practices, special entitlements above the statutory minimum, employee security trading policies, training and further education support policy, practices on drug and alcohol usage and policies on outside employment.
7. Describe the company's approach to business courtesies, bribes, facilitation payments, inducements and commissions. This might include how the company regulates the giving and accepting of business courtesies and facilitation payments and prevents the offering and acceptance of bribes, inducements and commissions and the misuse of company assets and resources.
8. State the measures the company follows to promote active compliance with legislation affecting its operations wherever it operates. This might include stating whether the company's policy is to comply with Australian or local legal requirements regarding employment practices, responsibilities to the community and responsibilities to the individual, particularly if the host country follows materially different standards than those prescribed by Australian law or international protocols.
9. Specify how the company handles actual or potential conflicts of interest. This might include reference to how the company manages situations where the interest of a private individual interferes or appears to interfere with the interests of the company as a whole and how the company prevents directors, senior executives and employees from taking improper advantage of property, information or position, or opportunities arising from these, for personal gain or to compete with the company.
10. Identify measures the company follows to encourage the reporting of unlawful or unethical behaviour and to actively promote ethical behaviour. This might include reference to how the company protects those, such as whistleblowers who report violations in good faith, and its processes for dealing with such reports.⁸
11. Describe the means by which the company monitors and ensures compliance with its code.

~~Recommendation 3.2: Companies should establish a policy concerning trading in company securities by directors, senior executives and employees and disclose the policy or a summary of that policy.~~

~~Commentary and guidance~~

~~Public confidence in the company can be eroded if there is insufficient understanding about the company's policies governing trading by "potential insiders". The law prohibits insider trading, and the Corporations Act and the ASX Listing Rules require disclosure of any trading undertaken by directors or their related entities in the company's~~

⁸ For guidance on the provision of a whistleblowing service, see Australian Standards on *Whistleblowing Programs for Entities* (AS 8004).

securities.⁹

For the purpose of this policy a “potential insider” is a person likely to possess inside information and includes the directors, the chief executive officer, or equivalent, the chief financial officer, or equivalent, staff members who are involved in material transactions concerning the company, and any other member of staff who is likely to be in the possession of inside information.

“Inside information” means information concerning a company’s financial position, strategy or operations and any other information which a reasonable person might consider, if it were made public, would be likely to have a material impact on a decision to buy or sell a company’s securities.¹⁰

Where companies establish a code of conduct and trading policy, they should also introduce appropriate compliance standards and procedures to ensure that the policy is properly implemented. There should also be an internal review mechanism to assess compliance and effectiveness. This review may involve an internal audit function.

Suggestions for the content of a trading policy are set out in Box 3.2.

Box 3.2: Suggestions for the content of a trading policy

Companies may find it useful to consider the following matters when formulating a trading policy:

1. Clearly identify the directors, officers, employees or group of employees who are restricted from trading (“designated officers”).¹¹
2. Identify and raise awareness about the prohibitions under the law and the requirements of the policy. This should include an awareness that it is inappropriate for the designated officer to procure others to trade when the designated officer is precluded from trading, and an awareness of the need to enforce confidentiality against external advisers.
3. Require designated officers to provide notification to an appropriate senior member of the company, for example, in the case of directors, to the chair, of intended trading, including entering into transactions or arrangements which operate to limit the economic risk of their security holdings in the company. No prior notification is needed for dividend reinvestment plans and other corporate actions open to all shareholders.¹²
4. Require subsequent confirmation of the trading that has occurred.
5. Identify whether trading windows or black outs are used and if so, details of their application.
6. Specify whether there is any discretion to permit trading by designated officers in specific circumstances, for example, financial hardship, details of such circumstances, and the basis upon which discretion is applied.
7. Specify whether the company prohibits designated officers from trading in financial products issued or created over the company’s securities by third parties, or trading in associated products.
8. Specify that the company prohibits designated officers from entering into transactions in associated products which operate to limit the economic risk of security holdings in the company over unvested entitlements.
9. Specify whether the policy applies to the securities of other companies of which the designated officer has inside knowledge because of their position with the company.

Where a company makes any representations about the alignment of a director’s or senior executive’s interests, the company should take into account the extent to which that director or senior executive has an economic interest in the

Recommendation 3.2:

Companies should establish a policy concerning diversity and disclose the policy or a summary of that policy. The policy should include measurable objectives for achieving gender diversity.

⁹ ASX Listing Rule 3.19A regarding disclosure by the company of directors’ notifiable interests within five business days. Companies should note that as at July 2007 the Government proposes amending Section 205G of the Corporations Act regarding disclosure by directors of their notifiable interests. The proposed amendment would reduce the timeframe for disclosure from 14 days to two days. There is also a proposal to remove the Listing Rule.

¹⁰ Companies should be aware of the relevant provisions of the Corporations Act.

¹¹ Anyone coming into possession of inside information has obligations under to comply with the law relating to insider trading.

¹² The recommended disclosure is of the designated officer’s effective exposure under their security holdings as a result of these transactions or arrangements.

Commentary

For the purpose of this policy “diversity” includes gender, age, ethnicity and cultural background.

The measurable objectives should identify ways in which the achievement of gender diversity is measured, for example, the proportion of women employed by (or consultants to) the company, in senior executive positions and on the board.

Where companies establish a diversity policy they should also introduce appropriate procedures to ensure that the policy is properly implemented, which may include additional measurable objectives in relation to other aspects of diversity as identified in the policy. There should also be an internal review mechanism to assess the effectiveness of the policy.

Suggestions for the content of a diversity policy are set out in Box 3.2

Box 3.2 Suggestions for the content of a diversity policy

Companies may find it useful to consider the following matters when formulating a diversity policy:

1. Commitment to diversity and articulation of the corporate benefits arising from employee and board diversity and the importance of benefiting from all available talent. This should promote an environment conducive to the appointment of well qualified employee, senior management and board candidates so that there is appropriate diversity to maximise the achievement of corporate goals. For example, the needs of a company may point to the need for directors with particular skills and experience.
2. Commitment to and identification of ways to promote a corporate culture which embraces diversity when determining the composition of employees, senior management and the board, including recruitment of employees and directors from a diverse pool of qualified candidates.
3. Identification of factors that should be taken into account in the selection processes and whether professional intermediaries should be used to identify or assess candidates.
4. Identification of programs that assist in the development of a broader pool of skilled and experienced board candidates including initiatives focused on skills development such as executive mentoring programs or more targeted practices relating to career advancement such as those that develop skills and experience that prepare employees for senior management and board positions.
5. Articulation of a corporate culture which not only supports workplace diversity but also recognises that employees at all levels of the company may have domestic responsibilities.
6. Transparency of board processes, review and appointments.

Recommendation 3.3:

Companies should disclose in each annual report the measurable objectives for achieving gender diversity set by the board in accordance with the diversity policy.

Commentary

The ASX Corporate Governance Council encourages companies in Australia to foster a governance culture that embraces diversity in the composition of corporate boards, with a focus on the participation of women. The shareholder role is enhanced if shareholders are fully informed of the policy and its measurable objectives which facilitate tracking and monitoring of the company’s performance against those objectives.

Recommendation 3.4: Companies should disclose in each annual report the proportion of women employees in the whole organisation, women in senior executive positions and women on the board. Companies should report on a full-time employee basis by category or seniority where relevant to the organisation.

Commentary

Diversity is an economic driver of competitiveness for companies. Research has shown that increased gender diversity on boards is associated with better financial performance, and improved workforce participation at all levels which positively impacts on the economy. The promotion of gender diversity broadens the pool for recruitment of high quality employees, enhances employee retention, encourages greater innovation and an improved corporate image and reputation. Reporting on the diversity profile of the company facilitates greater transparency and accountability in relation to the policy that has been put in place, together with the objectives to be achieved by the company.

Companies should consider, in the context of the economic group controlled by the company, how best the reporting might be achieved to reflect accurately the participation of women in the workplace and the roles in which they are employed: for instance, whether a full-time equivalent measure is appropriate in all or some circumstances as opposed to clear categorisation of full-time, part-time and contracted services and whether the participation is in management leadership or supporting roles.

Recommendation 3.53: Companies should provide the information indicated in the Guide to reporting on Principle 3.

Guide to reporting on Principle 3

An explanation of any departure from Recommendations 3.1, 3.2, 3.3, 3.4 or 3.5 should be included in the corporate governance statement in the annual report.

The following material should be made publicly available, ideally by posting it to the company's website in a clearly marked corporate governance section:

- any applicable code of conduct or summary
- any diversity policy or a summary.

~~the trading policy or a summary of its main provisions.~~

Application of Principle 3 in relation to trusts and externally managed entities

References to "directors" and "employees" of a company should be applied as references to directors and employees of the responsible entity, and the relevant trading is in securities of the trust and to equivalent roles in respect of other externally managed entities. The trading policy should refer to the securities or units of the listed entity.

Principle 6: Respect the rights of shareholders

Companies should respect the rights of shareholders and facilitate the effective exercise of those rights.

Companies should empower their shareholders by:

- communicating effectively with them
- giving them ready access to balanced and understandable information about the company and corporate proposals
- making it easy for them to participate in general meetings.

Recommendation 6.1:

Companies should design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose their policy or a summary of that policy.

Commentary

Publishing the company's policy on shareholder communication will help investors understand how to obtain access to relevant information about the company and its corporate proposals.

Electronic communication

Companies should consider how best to take advantage wherever practicable of new technologies that provide:

- opportunities for more effective communications with shareholders
- improved access for shareholders unable to be physically present at meetings.

See Box 6.1 for suggestions on how to improve shareholder participation and enhance market awareness through electronic means.

Meetings

Companies should consider how to use general meetings effectively to communicate with shareholders and allow reasonable opportunity for informed shareholder participation.

The ASX Corporate Governance Council has developed guidelines for improving shareholder participation through the design and content of notices and through the conduct of the meeting itself.¹³

Communication with beneficial owners

Companies may wish to consider allowing beneficial owners to choose to receive shareholder materials directly; for example, by electronic means.

Website

All companies should have a website and are encouraged to communicate with shareholders via electronic methods. If a company does not have a website it must make relevant information available to shareholders by other means; for example, a company may provide the information on request by email, facsimile or post.

Box 6.1

Using electronic communications effectively

Companies should use their websites to complement the official release of material information to the market. This will enable broader access to company information by investors and stakeholders. Measures companies may consider include:

- placing all relevant announcements made to the market, and related information (for example, information provided to analysts or media during briefings), on the company website after they have been released to ASX
- webcasting or teleconferencing analyst or media briefings and general meetings, or posting a transcript or summary to the website
- placing the full text of notices of meeting and explanatory material on the website - see Guideline 12 in the *Guidelines for notices of meeting* at www.asx.com.au
- providing information about the last three years' press releases or announcements plus at least three years of financial data on the website
- providing information updates to investors by email

[Analyst briefings](#)

- [where possible, particularly in the case of results announcements, arrange for advance notification of group briefings and make them widely accessible, including through the use of web casting through the internet and / or conference calls](#)
- [keeping a summary record of the topics discussed at briefings with investors and analysts, including a record of those present, and the time and place of the meeting.](#)

¹³ Guidelines for improving shareholder participation through the design and content of notices and the conduct of the meeting itself are at www.asx.com.au. They are guidelines only and not reporting requirements.

Recommendation 6.2:

Companies should provide the information indicated in the Guide to reporting on Principle 6.

Guide to reporting on Principle 6

An explanation of any departure from Recommendations 6.1 or 6.2 should be included in the corporate governance statement in the annual report.

The company should describe how it will communicate with its shareholders publicly, ideally by posting the information on the company's website in a clearly marked corporate governance section.

Application of Principle 6 in relation to trusts and externally managed entities

The annual general meeting is the central forum by which companies can effectively communicate with shareholders, provide them with access to information about the company and corporate proposals, and enable their participation in decision-making. The Corporations Act does not, however, require trusts to hold annual general meetings, although they may do so. Trusts should consider the range of means by which they may achieve the same ends, including the possibility of convening general meetings.

Listed entities that are not required to comply with section 250RA of the Corporations Act should consider the range of means by which they may achieve the same ends.¹⁴ This applies not only to trusts and externally managed entities but also to entities such as foreign incorporated entities. Any such entity should include in its annual report a statement disclosing the extent to which it has achieved the aims of the provisions of section 250RA during the reporting period and give reasons for not doing so.

Principle 8: Remunerate fairly and responsibly

Companies should ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to performance is clear.

The awarding of remuneration is a key area of focus for investors. When setting the level and structure of remuneration, a company needs to balance its desire to attract and retain senior executives and directors against its interest in not paying excessive remuneration. It is important that there be a clear relationship between performance and remuneration, and that the policy underlying executive remuneration be understood by investors.¹⁵

Recommendation 8.1:

The board should establish a remuneration committee.

Commentary

Purpose of the remuneration committee

A board remuneration committee is an efficient mechanism for focusing the company on appropriate remuneration policies.

Ultimate responsibility for a company's remuneration policy rests with the full board, whether or not a separate remuneration committee exists.

¹⁴ Section 250RA [Auditor required to attend listed company' AGM] of the Corporations Act makes it an offence for the lead auditor not to attend a listed company's AGM, or arrange to be represented by a suitably qualified member of the audit team who is in a position to answer questions about the audit.

¹⁵ Note the requirements relating to disclosure of remuneration policy and details in Section 300A of the Corporations Act.

For smaller boards, the same efficiencies may not be derived from a formal committee structure. Companies without a remuneration committee should have board processes in place which raise the issues that would otherwise be considered by the remuneration committee.

Charter

The remuneration committee should have a charter that clearly sets out its role and responsibilities, composition, structure and membership requirements and the procedures for [inviting](#) non-committee members to attend meetings.

The terms of reference of the remuneration committee should allow it to have access to adequate internal and external resources, including access to advice from external consultants or specialists.

Composition of remuneration committee

~~The remuneration committee should be structured so that it:~~

- ~~• consists of a majority of independent directors~~
- ~~•~~
- ~~• is chaired by an independent director~~
- ~~•~~
- ~~• has at least three members.~~

Responsibilities of the remuneration committee

The responsibilities of the remuneration committee should include a review of and recommendation to the board on:

- the company's remuneration, recruitment, retention and termination policies and procedures for senior executives
- senior executives' remuneration and incentives
- superannuation arrangements
- the remuneration framework for directors¹⁶.

Remuneration policy

The company should design its remuneration policy in such a way that it:

- motivates senior executives to pursue the long-term growth and success of the company
- demonstrates a clear relationship between senior executives' performance and remuneration.

The remuneration committee may seek input from individuals on remuneration policies, but no individual should be directly involved in deciding their own remuneration.

The remuneration committee should ensure that the board is provided with sufficient information to ensure informed decision-making.

¹⁶ The remuneration framework for directors is often addressed by the nomination committee rather than the remuneration committee.

Recommendation 8.2:

The remuneration committee should be structured so that it:

- consists of a majority of independent directors
- is chaired by an independent director
- has at least three members

Commentary

The remuneration committee should be of sufficient size and independence to discharge its mandate effectively¹⁷.

Companies should, where possible, limit the use of executive directors serving on a remuneration committee in order to address the potential for or perception of conflict of interest of executive management's involvement in board decisions on the remuneration packages of directors.

In addressing remuneration, individuals should have no involvement in decisions directly pertaining to their own remuneration.

Recommendation 8.32:

Companies should clearly distinguish the structure of non-executive directors' remuneration from that of executive directors and senior executives.

Commentary

Executive directors' and senior executives' remuneration packages should involve a balance between fixed and incentive pay, reflecting short and long-term performance objectives appropriate to the company's circumstances and goals.

The Corporations Act requires companies to make detailed disclosure of executive remuneration policies in their remuneration reports which are subject to an advisory vote by shareholders. Under the Listing Rules and the Corporations Act companies are not generally required to obtain shareholder approval for equity-based incentive plans for senior executives who are not directors.

However, companies may find it useful to submit to shareholders proposed equity-based incentive plans which will involve the issue of new shares to senior executives prior to implementing them. This communication is directed at providing the board with a timely assurance that a plan is reasonable.¹⁸ Companies may also consider reporting to shareholders on whether equity-based remuneration payments involving the issue of new shares to senior executives are made pursuant to plans approved by shareholders.

Guidelines on an appropriate framework for determining executive directors' and senior executives' remuneration packages are contained in Box 8.1.

¹⁷ [See also the new composition requirements under the proposed new listing rule for ASX top 300 companies.](#)

¹⁸ Under Section 211 of the Corporations Act benefits that are "reasonable remuneration" are an exception to the requirement for member approval for financial benefits to related parties under Section 208 of the Act.

Box 8.1: Guidelines for executive remuneration packages

Most executive remuneration packages will involve a balance between fixed and incentive pay.¹⁹ Companies may find it useful to consider the following components in formulating packages:

1. Fixed remuneration

This should be reasonable and fair, taking into account the company's legal and industrial obligations and labour market conditions, and should be relative to the scale of business. It should reflect core performance requirements and expectations.

2. Performance-based remuneration

Performance-based remuneration linked to clearly specified performance targets can be an effective tool in promoting the interests of the company and shareholders.

Incentive schemes should be designed around appropriate performance benchmarks that measure relative performance and provide rewards for materially improved company performance.

3. Equity-based remuneration

Appropriately designed equity-based remuneration, including stock options, can be an effective form of remuneration when linked to performance objectives or hurdles.

Equity-based remuneration has limitations and can contribute to 'short-termism' on the part of senior executives. Accordingly, it is important to design appropriate schemes. The terms of such schemes should clearly prohibit entering into transactions or arrangements which limit the economic risk of participating in unvested entitlements under these schemes.²⁰ The exercise of any entitlements under these schemes should be timed to coincide with any trading windows under any trading policy established by the company.

4. Termination payments

Termination payments, if any, for chief executive officers should be agreed in advance, including detailed provisions in case of early termination. There should be no payment for removal for misconduct.

Agreements should clearly articulate performance expectations. Companies should consider the consequences of an appointment not working out, and the costs and other impacts of early termination.

Box 8.2 contains guidelines for appropriate practice in non-executive director remuneration.

Box 8.2: Guidelines for non-executive director remuneration

Companies may find it useful to consider the following when considering non-executive director remuneration:

1. Non-executive directors should normally be remunerated by way of fees, in the form of cash, non-cash benefits, superannuation contributions or equity; they should not normally participate in schemes designed for the remuneration of executives.
2. Non-executive directors should not receive options or bonus payments.
3. Non-executive directors should not be provided with retirement benefits other than superannuation.

¹⁹ Companies should note that entering into employment agreements with senior executives, or obligations under those agreements falling due may trigger a continuous disclosure obligation under Listing Rule 3.1. See Companies Update 1 May 2003 *Continuous Disclosure and Chief Executive Officer Remuneration* at www.asx.com.au.

²⁰ Where a company makes any representations about the alignment of a senior executive's interests, the company should take into account the extent of that senior executive's alignment of interest based on any disclosure under the company trading policy.

Recommendation 8.3~~4~~: Companies should provide the information indicated in the Guide to reporting on Principle 8.

Guide to reporting on Principle 8

The following material or a clear cross-reference to the location of the material should be included in the corporate governance statement in the annual report:

- the names of the members of the remuneration committee and their attendance at meetings of the committee, or where a company does not have a remuneration committee, how the functions of a remuneration committee are carried out
- the existence and terms of any schemes for retirement benefits, other than superannuation, for non-executive directors
- an explanation of any departures from Recommendations 8.1, 8.2, ~~or~~ 8.3 ~~or~~ 8.4.

The following material should be made publicly available, ideally by posting it to the company's website in a clearly marked corporate governance section:

- the charter of the remuneration committee or a summary of the role, rights, responsibilities and membership requirements for that committee
- a summary of the company's policy on prohibiting entering into transactions in associated products which limit the economic risk of participating in unvested entitlements under any equity-based remuneration schemes.

Application of Principle 8 in relation to trusts and externally managed entities

Under the Corporations Act, remuneration and indemnity for costs and expenses of the responsible entity is required to be disclosed in a trust's constitution. This may overlap to an extent with the Recommendations and should be taken into account by trusts.

Externally managed entities should disclose a summary of any management agreement terms relating to management fees or the equivalent, including performance fees, including a clear cross reference to the location of this material.

Listed entities that are not required to comply with section 300A of the Corporations Act or AASB 124 *Related Party Disclosures* should consider the range of means by which they may achieve the same ends and should provide a clear cross-reference to the location of this material.²¹

²¹ Section 300A [Annual Directors' Report – Specific information to be provided by listed companies – particularly Disclosure of remuneration policy and details] and AASB 124 *Related Party Disclosures*.