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To the ASX Corporate Governance Council

**Review of the *Corporate Governance Principles and Recommendations*:
Draft 3rd edition**

Governance Institute of Australia (previously Chartered Secretaries Australia) is the only independent professional association with a sole focus on the practice of governance. We provide the best education and support for practising chartered secretaries, governance advisers and risk managers to drive responsible performance in their organisations.

Our Members hold primary responsibility within listed entities for developing governance policies, ensuring compliance with the Australian Securities Exchange (ASX) listing rules and supporting the board on all governance matters. Their familiarity with the practical aspects of how to implement best practice governance frameworks and ensure sound reporting to shareholders has informed the comments in this submission.

Governance Institute of Australia welcomes the opportunity to comment on the proposed amendments to the *Corporate Governance Principles and Recommendations* (Principles and Recommendations). The Principles and Recommendations have played a vital role in improving corporate governance in Australian listed companies since the release of the first edition in 2003. Their history is one of practical statements on governance which have brought meaningful change to governance practice.

The Principles and Recommendations, and practitioners such as chartered secretaries who have primary carriage in implementing the Principles and Recommendations, have served Australia well in lifting and maintaining its standing as a country with a high-performing corporate governance environment.

General comments

We are pleased to see that the draft 3rd edition retains the eight underlying principles in previous versions of the Principles and Recommendations. We also agree with and commend the Council on the decision to:

- move the reporting triggers that were previously included in the section called 'Guide to Reporting' at the close of each Principle to the body of each Principle
- streamline a significant amount of the commentary accompanying the Recommendations
- elevate a number of practices or disclosures previously contained in the commentary to reporting triggers

- enable listed entities to disclose corporate governance practices on the entities' websites, rather than requiring them to be included in the annual report
- clarify for smaller listed entities and boards how they can demonstrate that they meet the spirit of the recommendations — this addresses past criticism that the recommendations have been geared to large listed entities and large boards
- make reference, as appropriate, to governance codes in other jurisdictions — while there is an increasing global convergence of governance practice and it is therefore appropriate to review other codes, any reference to other codes always needs to be considered in relation to its applicability to Australia. It should not be assumed that other codes are automatically applicable.

However, Governance Institute of Australia is of the view that the Council has not taken the opportunity to reaffirm the key principle underpinning the guidelines, which is the 'if not, why not' model comprising 'suggestions for sound practice designed to optimise corporate performance and accountability in the interests of shareholders and the broader economy'¹. This model provides for other approaches, subject to explanation. While this approach is mentioned on page 3 of the draft 3rd edition, it is not sufficiently highlighted, despite it being the fundamental thesis of the Principles and Recommendations.

Highlighting this model is particularly important, given the preponderance of other governance guidelines issued by multiple parties, including intermediaries acting collectively on behalf of asset owners as well as individual asset owners, fund managers, proxy advisers and shareholder groups, and while there can be commonality in some areas between these multiple guidelines, they can also conflict at times. The approach can also at times be prescriptive.

The last decade has shown that the approach taken by Council in the Principles and Recommendations — that governance cannot be a 'one-size-fits-all' approach and that 'if an entity considers a Recommendation is inappropriate to its particular circumstances, it has the flexibility not to adopt it — a flexibility tempered by the requirement to explain why'² — is key to the success of the guidelines in being adopted by listed entities as the primary governance document in Australia.

Highlighting the 'if not, why not' approach also assists the market to counteract the tendency to assume that entities must 'comply' with the Recommendations or be 'marked down' on governance practice.

Recommendations on matters of general concern

Governance Institute of Australia recommends that the 3rd edition:

- provide greater emphasis to the key principle underpinning the guidelines — the 'if not, why not' approach. This could be done by including the words in the subheading 'The purpose of the Principles and Recommendations' on page 3 as well as in any media release accompanying the issue of the new edition and also by moving the section 'Disclosing the reasons for not following a recommendation' currently found on page 7 to sit next to the section setting out how the 'if not, why not' approach works. It may also be useful for the ASX Corporate Governance Council to engage in an exercise similar to that undertaken by the UK's Financial Reporting Council as part of its 2012 update of the UK Corporate Governance Code. This was the inclusion of additional guidance on

¹ ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, 2nd edition, with 2010 amendments, p 5

² *ibid*

the 'comply-or-explain' regime as a way of clarifying its methodology and improving its effectiveness for companies and investors alike

- clarify that the Principles and Recommendations are the primary governance guidelines adopted by listed entities.

Comments on specific issues

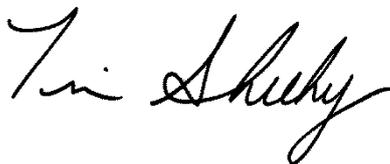
As a founding member of the ASX Corporate Governance Council, Governance Institute of Australia has been involved in the development of each edition, including the draft 3rd edition.

However, we accept that each draft issued for public consultation represents the consensus view of all members of the Council, and is not necessarily reflective of the views of any individual Council member.

Our comments and recommendations on the draft 3rd edition are the views of our Members, who have primary responsibility to draft policies and implement the governance frameworks in listed entities. Governance Institute of Australia's great strength in the review of the draft 3rd edition is our Members' ability to bring to light the practical and applied governance challenges that arise from changes to the framework.

Our comments on specific aspects of the draft 3rd edition follow. Where we have suggested drafting amendments, our recommended changes are shown in red.

Kind regards

A handwritten signature in black ink, appearing to read 'Tim Sheehy', written in a cursive style.

Tim Sheehy
Chief Executive

Principle 1: Lay solid foundations for management and oversight

Recommendation 1.1

- a) Recommendation 1.1 requires that the board charter set out the role of the chair. However, the board charters of many listed entities do not currently set out the role of the chair in the board charter, as this is dealt with elsewhere, such as in a board governance document, or on a corporate governance page on the website or in the corporate governance statement in the annual report. This requirement will force the majority of listed entities to amend their board charters to set out the role of the chair, with no commensurate benefit to shareholders from a governance perspective.

The existing commentary on page 8, which notes that the role of the chair is set out in commentary to Recommendation 2.3, could be amended to state that: 'The usual role of the chair is mentioned in commentary to Recommendation 2.3 below. The role of the chair may be addressed in the board charter, **or other board governance document, a position description or similar, or a corporate governance page on the website or in the annual report.**'

The existing commentary on page 8 also notes that the role of deputy chair or 'senior independent director' should also be included in the board charter. The commentary could be amended to state that: 'If the board of a listed entity has a deputy chair or a 'senior independent director' (see Recommendation 2.3 below), the board charter **or other board governing document, a position description or similar, or corporate governance page on the website or annual report** should also include a description of their roles and responsibilities'.

Governance Institute of Australia recommends that the requirement that the role of the chair be set out in the board charter be removed from Recommendation 1.1. This matter can be dealt with in the commentary on page 8 as suggested above.

- b) The existing commentary on page 8 sets out a list of board responsibilities. Many listed entities have formed board committees to which they delegate certain of these responsibilities, with the board retaining ultimate oversight and decision on the matters delegated to the relevant committees.

Governance Institute of Australia recommends that an additional sentence be included in the commentary on page 8 noting that some of the responsibilities listed may be delegated to a relevant board committee with the board retaining ultimate oversight and decision on these matters.

- c) The existing commentary on page 8 states that: 'The board charter should set out the entity's policy on when directors may seek independent professional advice at the expense of the entity ...'. The commentary needs to expand to include reference to the board charter clarifying how the directors can seek such advice.

Governance Institute of Australia recommends that the commentary on page 8 be amended to state: "The board charter should set out the entity's policy on when **and how** directors may seek independent professional advice at the expense of the entity ...'

Recommendation 1.2

- a) Recommendation 1.2 deals with the checks a listed entity is recommended to undertake before nominating or appointing a director. However, it may not be possible for a listed entity to undertake such checks when an external candidate nominates for the board. Moreover, the experience of our Members in listed entities that are also APRA-regulated entities (which are required to undertake checks to ensure that any potential

director is 'fit and proper') is that there are times when the entity does not have all the checks back in time when the appointment is made (particularly for overseas directors) or may not be able to access the information required (again, particularly for overseas directors, as some jurisdictions will not release this information) and therefore the appointments are made 'subject to the satisfactory completion of the fitness and proprietary checks'. Governance Institute of Australia Members are of the view that similar provision should be made in the Principles and Recommendations.

Governance Institute of Australia recommends that Recommendation 1.2 be amended to:

- provide for the fact that a listed entity may not be able to undertake such checks when external candidates nominate for board appointment
 - include wording to the effect that a listed entity should ensure that the board appointment is made subject to the satisfactory outcomes of such checks.
- b) The existing commentary on page 9 notes the checking of criminal records and bankruptcy as the first priorities for a listed entity when considering appointing a director to a board. Our Members are strongly of the view that this is an inappropriate emphasis, given that capability, knowledge, experience and suitability for the challenges of the role should be considered as the key priorities when considering appointing a director to the board.

Governance Institute of Australia recommends that the commentary on page 9 be revised to state that: 'A listed entity should ensure that appropriate checks (such as **capability, knowledge, experience, suitability for the challenges of the role**, character reference checks, education, bankruptcy and criminal records) are undertaken before it appoints a person, or puts forward to security holders a new candidate for election, as a director'.

- c) We note that the consultation paper states on page 7 in relation to Recommendation 1.2 that: 'Council believes that most listed entities would be using specialised search firms to locate potential appointees to their boards and that those firms would normally undertake appropriate checks as a matter of course'. While we recognise that any commentary in the consultation paper is not repeated in the Principles and Recommendations, Members note that many smaller listed entities do not use specialised search firms.

Recommendation 1.4

Governance Institute of Australia is pleased that the draft 3rd edition looks to enhance the effectiveness of corporate governance in Australia, particularly with the recommendation that the company secretary, given their prime governance function, should report directly to the board.

Recommendation 1.4 deals with the direct reporting line of the company secretary to the chair. While the commentary notes that a company secretary may also have a management reporting line, it needs amending to further clarify that the company secretary has a non-exclusive reporting line to the board. A company secretary in many companies may have a dual role, for example, they may also be the CFO, and they will always have a dual reporting line, regardless of whether they are in a dedicated company secretary role or not, as they are also part of the management team. In larger companies, there may also be multiple people who have been appointed as a company secretary of the company for administrative reasons.

The challenges of a dual-reporting line should be recognised in the commentary to Recommendation 1.4, that is, the commentary should include additional material promoting the

role of the board in the performance review of the company secretary. The board effectively is only required to appoint two people: the CEO and the company secretary. The board therefore has an important role to fill in reviewing whether the company secretary is providing them with the requisite standard of corporate governance advice. It also strengthens the company secretary role as a key governance role.

Governance Institute of Australia recommends that the commentary on page 10 be amended to clarify that:

- the direct reporting line to the chair is in relation to the governance-related aspects of the role and that the company secretary may have a dual reporting line
- the board has a responsibility for monitoring the performance of the company secretary in the provision to it of the governance-related aspects of the role.

Recommendation 1.5

- a) We agree with Council's decision to move the recommendations on diversity from Principle 3 to Principle 1 and amalgamate the separate recommendations in the 2nd edition in one.

Our support for the move to Principle 1 is that diversity is not primarily a social justice issue, but one of seeking to improve the long-term performance of an entity and utilise the full range of human capital available to it. It is very much a matter of management and oversight governance to have diversity at all levels of seniority to reflect the community in which the entity operates and bring together different experiences to achieve better outcomes.

Currently, Recommendation 1.5 requires the board to set the measurable objectives for achieving gender diversity and assess annually both the objectives and the entity's progress in achieving them (and that this should be set out in the diversity policy). Our Members note that many listed entities have delegated these responsibilities to a relevant board committee.

Governance Institute of Australia recommends that Recommendation 1.5 be redrafted to state that:

A listed entity should:

- a) have a diversity policy which includes requirements for the board **or its relevant committee**:
- (1) to set measurable objectives for achieving gender diversity; and
 - (2) to assess annually both the objectives and the entity's progress in achieving them;

Recommendation 1.6

The existing commentary on page 13 states that: 'The non-executive directors, led by the deputy chair or senior independent director (if any), should be responsible for the performance evaluation of the chair We note that there may not be a deputy chair or senior independent director.

Governance Institute of Australia recommends that the commentary on page 13 be amended to state that: 'The non-executive directors, led by the deputy chair or senior independent director (if any) **or an appropriate non-executive director**, should be responsible for the performance evaluation of the chair ...'.

Final comment on Principle 1

Our Members note that the Principles and Recommendations do not cover management governance, apart from Recommendation 1.5 which addresses gender diversity throughout the entire organisation. Principle 1 is silent on disclosure of governance below the board, that is, the

manner in which the entity governs its decision-making internally. Governance Institute Members do not suggest that any new reporting trigger be included, but suggest that Council consider including a sentence or two encouraging listed entities to disclose management committees and any other information that provides transparency on how the entity ensures responsible decision-making.

Principle 2: Structure the board to add value

Box 2.1: the defining characteristics of an independent director

- a) Governance Institute of Australia is a strong supporter of assessing independence as a lens for judging director capability but we note that it is not the only indicator of director suitability or capacity. We also note that independence of judgment may be affected by the indicators set out in Box 2.1, but that it cannot be assumed that independence of judgment is lost if some of those indicators are met.

Furthermore, we note that the Australian Prudential Regulatory Authority (APRA) has previously taken the criteria for independence in the 2nd edition of the Principles and Recommendations and applied them as prescriptive criteria in the prudential standards applicable to financial institutions. There has been considerable disquiet in relation to this, given that in the Principles and Recommendations the indicators are examples of interests, positions, associations and relationships that may raise doubts about independence and require consideration, but they do not prescribe a loss of independence. It is likely that any amendments to the indicators of independence in the 3rd edition of the Principles and Recommendations will be set, in turn, as prescriptive criteria in the APRA prudential standards. It is therefore important to consider the implications of such prescription when assessing the need for amendment of Box 2.1.

Our Members therefore have concerns with a number of the modifications to the indicators of independence as set out in Box 2.1.

The first concern is the change from the word 'relationships' to characteristic'. This modification changes the emphasis from matters that may indicate independence or a loss of independence, as judged by the board, to set criteria of independence or a loss of independence. This is a serious shift in emphasis with which our Members do not agree.

Governance Institute of Australia recommends that the heading be changed to Box 2.1: relationships affecting independent status.

- b) The criteria for a director to be considered independent as set out in Box 2.1 have been modified to include close family ties. While it is important to consider close family ties when assessing independence, Governance Institute Members are of the view that including family members or partners in the criteria for assessing independence does not accommodate the contemporary reality of family members and partners operating independently of one another. While it is recognised that the inclusion of close family ties is based on whether they fall into any of the other categories of indicators set out in Box 2.1, thus introducing a need to assess the materiality of the interest, position, association or relationship, the inclusion of close family ties would potentially include independent adult children, parents and siblings who have separate and independent financial lives to other board members. It assumes that control is inevitable. Moreover, it would be difficult to apply in practice. For example, if an adult son of a director works as a partner in a law firm that provides advice to the listed entity, how is the board to assess the materiality of the relationship? Furthermore, the current drafting suggests that the three-year look-back will be extended to close family members. Our Members

consider that this approach again does not reflect the reality of contemporary family life and creates an unhelpful expectation.

Governance Institute of Australia recommends that the idea of ‘control’ is central to any reference to close family ties and that this should be reflected in the drafting.

- c) The draft 3rd edition of Box 2.1 has modified the indicator of independence in the 2nd edition referring to material professional advisers and consultants. The word ‘material’ has been deleted, yet this word is retained in references to suppliers, customers and contractual relationships. It is insufficient to have the final paragraph refer to the need to assess the materiality of the relationship or interest of a professional adviser — the word needs to be retained as it is with other indicators.

Governance Institute of Australia recommends that the word ‘material’ be inserted before the words ‘professional adviser’ and ‘consultant’ in this indicator.

- d) Box 2.1 contains a new indicator on tenure, suggesting that after nine years a director may no longer be considered independent. As noted above, open-mindedness to new ideas is a central tenet of independence of judgment, rather than any indicator, including tenure, applied in isolation.

The addition of tenure in Box 2.1 assumes that the longer a director is on the board, the less independence they have in undertaking their role. However, this assumption fails to account for the fact that board members are also required to undertake ongoing education and training to ensure that their skills remain up-to-date — their skills and knowledge of the company improve the longer they are on the board. From an organisational point of view, therefore, tenure limits may serve as a detriment, as in some industries there may be a short supply of technically knowledgeable and qualified non-executive directors available to sit on the board.

Importantly, board composition policy should require companies to have a mix of directors on the board with different skills and a robust board renewal plan should be in place, which will better serve independence on the board than a limit on tenure.

We note that there was a reference in the commentary in the 1st edition of the Principles and Recommendations to the Higgs Review proposal that 10 years should be considered as the tenure beyond which independence is called into question. However, the public consultation on the 2nd edition clarified that tenure cannot be assumed to be a factor affecting independence and the decision was taken by Council to remove this commentary from the 2nd edition. While we acknowledge that some other jurisdictions currently include tenure as a criterion for independence, and that it can be useful to test our thinking on governance in Australia against the codes in other jurisdictions, we are of the view that the inclusion of tenure in the governance codes of other jurisdictions is insufficient reason to include it in the 3rd edition, particularly in light of the public debate on its applicability in 2007. We also note that there has been considerable reflection on the focus on and causes of short-termism in the United Kingdom, and that there has been discussion of how best to provide for long-term decision-making on boards, including providing for corporate memory and deep industry experience.

Should some reference to tenure be considered appropriate, Governance Institute of Australia is of the view that it would be preferable to include this in the commentary and to take a similar approach to the one set out in the current governance guidelines of the Australian Council of Superannuation Investors (ACSI). ACSI’s approach to tenure states that, ‘There is no firm threshold for when the length of a directorship affects independence. It is assessed on a case-by-case basis.’

We also note that a quick review of the ASX50 reveals that there is indeed no firm consensus for when or if the length of a directorship affects independence. One-third of these companies do not include any reference to tenure in the board charter, while one-third make reference to three terms, that is, nine years, and the final third make reference to four terms, that is, 12 years. Many note that tenure would be extended if appropriate.

Governance Institute of Australia recommends that the indicator of tenure be deleted and replaced with commentary to the effect that there is no firm threshold for when the length of a directorship affects independence and this should be assessed on an individual basis.

- e) Recommendation 2.6 requires a listed entity to disclose a summary of the main features of the induction program the entity has in place for new directors. It appears that it may also require a listed entity to disclose the professional development opportunities undertaken by continuing directors to develop and maintain their skills and knowledge. The drafting of the Recommendation is ambiguous — it requires disclosure of the program, which clearly refers to the induction program, whereas when referring to continuing education for directors the word used is ‘opportunities’, and so it is unclear if these opportunities are considered to be part of a program requiring disclosure.

Governance Institute of Australia has two concerns with Recommendation 2.6.

- i) Our Members note that the elements of induction programs for directors are very similar in most companies and query whether any benefits to shareholders and the market will arise from disclosures that will be remarkably similar. Attached is a *Good Governance Guide: Director induction packs — contents*, that Governance Institute has made available on our website, where it can be downloaded free of charge. We would expect these elements to appear in the induction packs of most companies. We would certainly expect that the induction program would include an introduction to senior management (briefings) and site visits, as noted in the attached Guide. It is most likely that the majority of disclosures in response to the draft Recommendation 2.6 will contain almost identical information. We cannot see the benefit to shareholders and the market in the majorities of entities disclosing that their induction program includes meetings with senior management and site visits.
- ii) As noted above, the current drafting of Recommendation 2.6 is ambiguous as it appears that it could contemplate the possibility that the ‘program’ requiring disclosure encompasses the two aspects of induction and providing appropriate professional development opportunities for directors to maintain their skills and knowledge needed to perform their role. Governance Institute of Australia Members note that continuing professional development on legal and accounting matters should be the responsibility of individual directors — it should not be the responsibility of the entity. The entity will ensure that the directors receive briefings and updates on entity-specific or industry-specific matters, and may also provide briefings on governance matters and some legal issues. For example, a number of listed entities provided briefings to directors on Revised Guidance Note 8 on continuous disclosure.

However, while our Members strongly encourage directors to avail themselves of opportunities to undertake continuing education on legal and accounting matters, as offered by a number of bodies such as professional associations and law firms, we are strongly of the view that the entity itself is not best placed to provide such education. The entity could provide advice on where directors could seek such education, but the onus should be on the director to avail themselves of those educational opportunities.

Furthermore, should the disclosure requirement in relation to director education be intended, the entity would be required to obtain a record from each director annually, setting out any professional development each has undertaken in the previous 12 months. This would be an onerous compliance obligation imposed on the entity. For directors of multiple companies, the same information would appear in multiple reports.

Our Members note that if all that is required is inclusion of a statement that the entity provides directors with guidance on where to source professional development opportunities, the disclosure requirement is feasible. However, a detailed listing would be a great burden on entities — as noted above — and for directors of multiple companies, the same information would appear in multiple reports.

Governance Institute of Australia recommends that:

- Recommendation 2.6 be redrafted to clarify that disclosure of continuing professional development is limited to entity-specific matters, and
- the second part of Recommendation 2.6 requiring disclosure of a summary of the induction program be deleted.

Principle 3: Promote ethical and responsible decision making

- a) The existing commentary on page 18 notes that: ‘Where a listed entity makes contributions or provides other support to charitable or philanthropic causes, it should disclose any actual or potential conflict of interest a director or senior executive may have in relation to that matter ...’.

While this is not a reporting trigger, it will create an expectation of disclosure. The practical implications are that the listed entity will be required to maintain a database of involvement by senior management in charities and philanthropic causes and cross-check this against all donations made by the entity. Yet such donations could be no more than \$1,000 to a local sporting club, as listed entities (particularly large ones) make numerous donations for multiple reasons. Currently the commentary contains no reference to a materiality threshold. The administrative work involved in this is significant, yet our Members query whether any benefits to shareholders and the market will arise from such disclosures where materiality is not an issue.

Moreover, this disclosure expectation is in addition to that contained in Box 3.1: suggestions for a code of conduct, which states that the code of conduct should ‘describe the organisation’s processes for handling actual or potential conflicts of interest’. Our Members are of the view that this disclosure is essential, as shareholders and other stakeholders should have transparency as to how a listed entity manages actual or potential conflicts of interest. However, our Members do not agree that disclosure of individual donations is necessary.

Governance Institute of Australia recommends that the commentary on page 18 stating that: “Where a listed entity makes contributions or provides other support to charitable or philanthropic causes, it should disclose any actual or potential material conflict of interest a director or senior executive may have in relation to that matter ...”.

- b) The existing commentary on page 18 also states that acting ethically and responsibly may include ‘employing people with disability or from other disadvantaged groups in society’. Our Members query whether employing people with a disability or from other disadvantaged groups in society should be considered a matter of ethical decision-making when it is a matter of diversity.

Governance Institute of Australia Members are of the view that employing people with disability is a diversity issue, and that this commentary would sit more appropriately under Recommendation 1.5.

Governance Institute of Australia recommends that reference to employing people with disability or from other disadvantaged groups in society is appropriately captured in the commentary under Recommendation 1.5 and should be deleted from Principle 3.

Principle 4: Safeguard integrity in financial reporting

The commentary under Recommendation 4.2 notes that it mirrors s 295A of the Corporations Act, which requires a declaration in relation to the listed entity’s financial statements by the chief executive officer and chief financial officer. However, while the commentary includes the words ‘in their opinion’, as occur in the Corporations Act, these words are missing in the recommendation itself.

Governance Institute of Australia recommends that Recommendation 4.2 be redrafted to include the words ‘in their opinion’.

Principle 5: Make timely and balanced disclosure

- a) This principle closes with a paragraph that states: ‘In designing its disclosure policy, a listed entity should also have regard to ASX Guidance Note 8 *Continuous Disclosure: Listing Rules 3.1—3.1B* and to the 10 principles set out in ASIC Regulatory Guide 62 *Better disclosure for investors*’.

Governance Institute of Australia Members note that ASX Guidance Note 8 in particular is central to the design of any disclosure policy and are of the view that this paragraph should not be located at the close of the commentary on this Principle, but at the start of it. All listed entities should refer to ASX Guidance Note before developing their disclosure policy.

Governance Institute of Australia recommends that this paragraph be moved from the end of the commentary on Principle 5 and inserted after the second paragraph in the commentary. Some minor redrafting will be required.

- b) We recognise that the Council has decided not to include references to various publications issued by the members of Council that assist in applying the principles. Notwithstanding this, we recommend that a new footnote be included referencing the joint publication issued by Chartered Secretaries Australia and the Australasian Investor Relations Association (AIRA), *Handling confidential information: Principles of good practice*. The document is attached and it can be located at <http://www.governanceinstitute.com.au/knowledge-resources/good-governance-guides/?categoryid=8031>. Our reasons for suggesting its inclusion are that it was

developed at the request of ASIC. ASIC had issued a draft Regulatory Guide on this issue in 2010, but agreed with Chartered Secretaries Australia and AIRA that industry-led guidance on this issue was more appropriate, given that processes for handling confidential information need to be tailored to various factors, such as the size of the company, the size of the transaction and the commercial imperatives and timing of a transaction, which can differ markedly from company to company.

Principle 6: Respect the rights of security holders

The existing commentary on page 24 includes a bullet point that a listed entity should include in an appropriate area of its website 'contact details (preferably for a named individual) for enquiries from security holders, analysts or the media.

Some of this information may be included on ASX announcements and in media releases, but is usually not included on websites, as staff can change and website updates may take time to effect. Moreover, in large entities, there will be multiple staff members listed on media releases. The inclusion of email addresses also attracts spam and, at times, abuse, and many entities therefore have a policy of not including the contact details (beyond the main switchboard number) of any individual staff named on the website.

Governance Institute of Australia recommends that this bullet point be amended to delete the reference to named individuals.

Principle 7: Recognise and manage risk

- a) The board is responsible for the informed oversight of risk management within the entity and should regularly review and approve the risk management policies and framework. Management is responsible for developing and implementing a sound system of risk management and internal control. This separation of oversight responsibility and implementation responsibility is recognised in the existing drafting of the commentary introducing Principle 7.

However, Governance Institute of Australia Members are of the view that the existing commentary that introduces this principle would benefit from additional commentary noting that a proactive and clear understanding of how the management of risk maps to the strategy of the entity is essential, and assists all staff to understand that risk management is part of the success of the business. Encouraging a meaningful discussion of risk management internally assists staff to understand that 'organisations of all kinds face internal and external factors and influences that make it uncertain whether, when, and the extent to which, they will achieve or exceed their objectives'³ and is also more likely to lead to meaningful reporting on how an entity manages its risk. That is, our Members are of the view that the inclusion of some additional commentary could help to limit the possibility of boilerplate disclosure.

Governance Institute of Australia recommends that additional commentary of the kind noted above be included in the introduction to this principle.

- b) Recommendation 7.1 requires the board of a listed entity to form a risk committee or include within the responsibilities of an audit committee the responsibilities normally undertaken by a risk committee.

³ Standards Australia, Draft 33, *Risk management guidelines — Companion to AS/NZS ISO 31000:2009*, p 8, issued for public consultation June 2013

Governance Institute of Australia Members note that many listed entities divide the responsibilities of a risk committee between different committees. That is, there may not be just one committee with the responsibility for risk. For example, many listed entities have one committee with oversight of safety and environmental impact risk and another for investment risk, while the audit committee may deal with operational risk. This may need to be explained in the commentary.

Governance Institute of Australia recommends that this recommendation be amended to state that:

- (b) include within the responsibilities of the audit **or other relevant** committee the responsibilities normally undertaken by the risk committee; or
- (c) if it does not have a risk committee (whether as a stand-alone committee or as part of the responsibilities of the audit **or other relevant** committee) ...'

We also recommend that the commentary (in the first paragraph on page 27) also be amended to state that: 'While ultimate responsibility for an entity's risk management framework rests with the full board, having a risk committee (be it a stand-alone committee or part of the responsibilities of the audit **or other relevant** committee) ...' and explanation of how listed entities divide the responsibilities of a risk committee between different committees be included in the commentary.

- c) Recommendation 7.2(a) appears to be seeking disclosure by the board that a risk management framework has been put in place that is appropriate to the entity. It is good governance for an entity to ensure that all directors and senior executives have a shared understanding of risk, which is the effect of uncertainty on an entity achieving its strategic objectives and maintaining its long-term viability and reputation.

However, Governance Institute of Australia is of the view that the current drafting is open to different interpretations. One is a broader interpretation that, at least once a year, the board should turn its mind to whether the risk framework is sound, whether there are changes in the material business risks and whether the risks identified remain within the company's risk appetite.

A more literal interpretation is that the Recommendation appears to assume a formal annual review (when, in reality, many entities will maintain an ongoing review of risk management practices and frameworks over the course of the year) and that it does not provide for the real possibility that there could be material business risks that arise beyond the risk management framework that has been put in place. That is, new risks need to be taken into account as they arise, and the board may therefore not be in a position to ensure that all material business risks remain within the risk appetite it has set.

Governance Institute of Australia recommends that Recommendation 7.2 needs to be reviewed to ensure the drafting is not ambiguous and speaks to the broader interpretation and not the literal one.

Principle 8: Remunerate fairly and responsibly

- a) Recommendation 8.2 — Guidelines for executive remuneration currently refers to equity-based remuneration including options or performance shares. Our Members note that since the tax treatment changed, the terminology employed also refers to rights.

Governance Institute of Australia recommends that the guidelines for executive remuneration be amended to also include reference to rights, so that the section would

read: 'Equity-based remuneration: well-designed equity-based remuneration, including options, rights or performance shares ...'.

- b) The commentary on page 31, under the Guidelines for executive and non-executive director remuneration currently states that: 'A listed entity which is not subject to these Corporations Act requirements should separately disclose this information in its annual report or on its website'.

This commentary is currently ambiguous. It can be read as requiring listed entities not subject to the Corporations Act requirements in relation to the remuneration report to have to disclose similar information as is contained in the remuneration report. It can also be read as requiring listed entities not subject to the Corporations Act requirements to disclose the information required by Principle 8 in its annual report or on its website. Given that the commentary cannot impose compliance with the Corporations Act, it therefore must be referring to Principle 8. However, our Members are of the view that the commentary could be clearer, so that those who may not be as familiar with the interaction of the listing rules and the commentary in the guidelines are not confused.

Governance Institute of Australia recommends that the commentary on page 31 be redrafted to state that: 'A listed entity which is not subject to these Corporations Act requirements should separately disclose the information required by Principle 8 in its annual report or on its website'.

- c) Recommendation 8.3 requires a listed entity to disclose a clawback policy. There has been significant debate in the UK and Europe, following the financial crisis, about the concepts of malus and clawback. Malus refers to an entity's ability to deny vesting of unvested equity instruments (even those that have no further performance conditions, and are time-limited only), while clawback refers to the return of awards or a part of awards, or the proceeds of awards, that have already vested. In the UK, malus provisions are far more common than clawback provisions, as defined here, although the generic term 'clawback' is sometimes used to refer to both. To avoid confusion, however, it would be helpful for Recommendation 8.3 to articulate exactly what is intended: malus, or clawback, or both. In addition, our Members note that many listed entities may not have a formal policy but instead include a clawback mechanism in the individual share plan applicable to executives under the employee share plan, or within the individual contract of employment and the Recommendation should include provision for this to coincide with the explanation dealt with in the commentary which states, 'To deal with this, a listed entity should have in place a clawback policy (either as a stand-alone policy or as part of its broader remuneration policy)...'.

Governance Institute of Australia recommends that the commentary attached to Recommendation 8.3 and the Recommendation itself be amended to:

- clarify whether it refers to malus, or clawback or both
- state that a listed entity should '(a) have a "clawback policy" or other mechanism which sets out the circumstances in which the entity may claw back performance-based remuneration from its senior executives'.

- d) The commentary on page 32 also states that: 'Generally speaking, a listed entity should include contractual provisions in the service agreements with its senior executives that conform to the clawback policy ...'. This commentary needs amending, given that the clawback provisions may be dealt with in the share plans of senior executives.

Governance Institute of Australia recommends that the commentary be amended to state that: 'A listed entity should, where necessary, include contractual provisions in

the service agreements with its senior executives that conform to the clawback policy ...'

- e) The commentary to Recommendation 8.3 on page 32 states that a policy should 'set out the circumstances in which the entity may claw back a senior executive's remuneration and how those amounts will be clawed back (for example, by requiring the senior executive to pay back remuneration, by reducing any earned but as yet unvested incentives, or by adjusting current year incentives or fixed remuneration to take account of the previous overpayment)'

Our Members note that it is unlikely that fixed remuneration can be clawed back from a practical perspective in cases where an executive does not comply with applicable contractual provisions that provide for claw back.

Governance Institute of Australia recommends that the commentary listing examples of how remuneration can be clawed back refer to the *equity-based components* of performance-based remuneration.



Good Governance Guide

Director induction packs: content

When a new director is appointed to the board of an entity, it is good governance to include the following items in the induction pack to enable the director to be as fully briefed as possible before attending the first board meeting. This also assists the company secretary to meet the statutory obligations arising from the appointment of the director. Ideally, the material should be discussed with the company secretary.

To collect

Information about the director

- consent to act as director
- completion of a standing disclosure document which records potential or actual conflicts by virtue of positions (such as other directorships) or shares held in other companies etc. This should be tabled at the director's first board meeting in accordance with s 192 of the Corporations Act
- information required for pre-vetting checks, (for example, APRA fit and proper requirements) or any other personal information that may be required to fulfil such obligations
- undertaking required from the director under s 319 of the Corporations Act in relation to the trading of shares in the company
- name and former name, if applicable
- residential address
- date and place of birth
- other, as required by relevant authorities
- contact information including business address, telephone, fax and email details
- name and contact details of personal assistant, if applicable
- name of partner/spouse, if applicable
- relevant current shareholdings in the entity.

To provide

Information about the entity

- copy of constitution/by-laws and relevant documents, for example, shareholder agreements
- copy of the company code of conduct
- copy of last annual report/half-year report
- monthly financial reports
- copy of current corporate plan and most recent risk register presented to the board
- copies of corporate communications such as staff magazines, advertising brochures
- copies of stakeholder publications, if applicable
- recent public statements, for example ASX disclosures, significant media releases recent reports/disclosures to the relevant minister or government department, if applicable
- corporate structure and names of senior management team. The latter document may also include contact details of senior managers, depending on the company's protocol on direct access by directors to senior management other than the CEO
- glossary of any industry-specific terms
- recent analyst and rating agency reports, if applicable.

A structured induction program would also include:

- introduction to senior management — briefings
- site visits.

Information about the board

- details of board members — names, addresses, contact details
- board and committee meeting schedules, including meeting times, dates and venues
- committee memberships and terms of reference/charters
- board processes and policies

- distribution of board papers — process and document management of board-related materials
- previous minutes of board and committees, for example, minutes of last six meetings and agendas for whole year.

Information about the director's appointment

- terms and conditions of appointment
- term of office
- fees and share schemes available
- committee memberships
- travel and reimbursement details
- insurance cover — directors' and officers', travel, spouse, beneficiary nomination
- appointments to other boards — restrictions/conditions
- share trading guidelines and policies
- disclosures/prior consents required
- agreed announcement of appointment (and draft Appendix 3X for listed entities)
- deed of indemnity and access
- director-related policies, for example, the seeking of legal advice.

See also *Good Governance Guide: Roles, duties and responsibilities of Company Secretary*

Handling confidential, market-sensitive information: Principles of good practice

Australasian Investor Relations Association



CHARTERED SECRETARIES
AUSTRALIA

Leaders in governance

Chartered Secretaries Australia

Chartered Secretaries Australia (CSA) is the peak body for over 7,000 governance and risk professionals. It is the leading independent authority on best practice in board and organisational governance and risk management. Our accredited and internationally recognised education and training offerings are focused on giving governance and risk practitioners the skills they need to improve their organisations' performance.

Our Graduate Diploma of Applied Corporate Governance sets the standard for entry into the profession. It is the only applied postgraduate course in governance with higher education accreditation that includes tailored public and private sector subject options, as well as a dedicated subject on Risk and Compliance.

Our Certificates in Governance Practice, Governance and Risk Management and Governance for Not-for-Profits provide vocational governance and risk management training, and a qualification for a wide range of professionals who are responsible for corporate accountability functions and processes within an organisation.

Members of CSA deal on a day-to-day basis with regulatory bodies and the government. Given the diverse roles our members play in the business community and their expertise in governance, CSA sees the principles of good practice relating to handling confidential, market-sensitive information as fulfilling its mission of the promotion and advancement of effective governance and administration.

Australasian Investor Relations Association

The Australasian Investor Relations Association (AIRA) was established in 2001 to advance the awareness of and best practice in investor relations in Australia and New Zealand and thereby improve the relationship between listed entities and the investment community. The Association's 155 corporate members now represent over A\$760 billion of market capitalisation or over two-thirds of the total market capitalisation of companies listed on ASX.

This guide will assist listed entities to implement policies and processes that protect confidential, market-sensitive information. AIRA believes this is important to reduce the risk of leaks and insider trading, preserving market integrity.

Introduction

Chartered Secretaries Australia (CSA) and the Australasian Investor Relations Association (AIRA) believe that adherence to the principles of continuous disclosure by listed entities is integral to the integrity and proper functioning of our equity markets,

Confidence in the integrity of Australia's markets could be undermined if investors believe rumours are actively spread in the market to distort proper price discovery.

It is therefore essential that corporations develop and adopt sound practices that support and adhere to the principles of continuous disclosure, ensure the effective management of confidential information and facilitate the responsible handling of rumours..

CSA and AIRA have jointly developed principles of good practice that corporations can implement, taking into account the nature, size and sensitivity of any particular transaction and the circumstances of the corporation.

CSA and AIRA believe that the guidance set out in the principles will provide a strong foundation for improving practices for the handling of confidential information. The principles are applicable in the context of capital raisings and mergers and acquisitions, and other transactions which corporations may undertake. They are designed to assist corporations and their advisers to implement robust policies and procedures to maximise the protection of confidential, market-sensitive information. In turn, this will ensure that corporations can manage the timely release of information in accordance with the continuous disclosure rules.



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Handling confidential, market-sensitive information: Principles of good practice

It is considered good governance for companies to establish policies and procedures to maximise the protection of confidential, market-sensitive information. Reducing the risk of leaks or insider trading promotes and preserves market integrity.

The Corporations Act prohibits a person with market-sensitive information from trading or procuring trading by someone else or communicating the information to someone likely to trade or procure trading. The board, senior executives and other internal or external persons who have access during a confidential, market-sensitive transaction to inside information relating directly or indirectly to the entity need to clearly understand their obligations to protect this information and maintain its confidentiality where it is premature to disclose such information, for example, because it concerns an incomplete proposal or negotiation or is insufficiently definite to warrant disclosure.

ASX Listing Rule 3.1¹ requires immediate disclosure of market-sensitive information if it has ceased to be confidential. This obligation relates only to information that is market-sensitive and not to all information held by an entity. These guidelines set out measures that can be considered when designing and implementing the policies and procedures that protect confidential, market-sensitive information, which is likely to be handled by a number of people within an entity as well as external parties. The measures any particular company may take will depend on its circumstances, the nature, size and sensitivity of any particular transaction, and the nature and timing of the transaction. On this basis, the guidance provided should be applied flexibly. It is up to the company to determine which measures are most applicable to each particular transaction, within an overarching context of focusing the attention of all those who are party to a transaction on ensuring that they keep the market informed, on a timely basis, and maintaining confidence in market integrity.

The principles that companies should adopt to maximise the protection of confidential, market-sensitive information are set out below.

Summary of principles governing good practice

- 1 It is good practice for companies to have in place internal systems to protect confidential, market-sensitive information.
- 2 It is good practice for companies to maintain an insider list when conducting a confidential, market-sensitive transaction.
- 3 It is good practice for companies that deal with confidential, market-sensitive information to ensure their directors, executives and employees are aware of their confidentiality obligations.
- 4 It is good practice for companies to bind their advisers and other service providers by entering into confidentiality agreements before passing on confidential, market-sensitive information, and to require confirmation from their advisers and other service providers that they have in place policies and practices relating to the handling and control of confidential, market-sensitive information that satisfy the terms of the agreement.
- 5 It is desirable for companies to know which, when and how potential investors are being sounded on their behalf in relation to a transaction involving the company .

¹ Reference should be made to ASX Listing Rules Guidance Note 8: Continuous Disclosure — Listing Rules 3.1 — 3.1B in relation to the requirement to disclose confidential information should confidentiality not be maintained.

Internal policies: Protection of confidential, market-sensitive information

Principle 1: It is good practice for companies to have in place internal systems to protect confidential, market-sensitive information

A clear, documented policy which establishes the standards of behaviour and procedures for handling confidential, market-sensitive information with which all employees are expected to comply will assist a company to protect that information.

It is good practice to assign clear responsibility within the company to an individual to oversee the implementation and enforcement of these policies and controls, as well as regular reviews of how the policies are working in practice. This in turn will help to ensure they are being implemented effectively.

Companies that are most successful at protecting confidential, market-sensitive information embed practices for protecting that information in the culture of their company and reinforce these through regular messages from top management. Individuals need to be aware of their personal obligations to preserve the confidentiality of company information and the purpose of various systems that are used to protect confidential, market-sensitive information.

Any policy on protecting confidential, market-sensitive information must be consistent with the company's communication policy, and, if the company is a disclosing entity, its disclosure policy.

The 'need to know' principle

It is good practice to limit the number of people with access to confidential, market-sensitive information to the minimum number possible in the circumstances. That is, consideration needs to be given to how a company can limit access to information to only those people who absolutely require the information to undertake their business role.

Physical document management and information barriers

Taking particular care with documents relating to a proposed transaction can assist in minimising the leakage of confidential, market-sensitive information. Companies should consider implementing the following practices:

- ensuring that employees who have access to confidential, market-sensitive information are aware of its status — the information should be marked as confidential and market-sensitive where appropriate
- ensuring physical copies of documents relating to confidential, market-sensitive transactions are securely stored when not in use and disposed of when no longer required, with access restricted to authorised staff only ('clean desk' policy)
- allocating dedicated printers, faxes, photocopiers, data rooms and other mechanisms for market-sensitive transactions, where reasonably practicable and justified by the circumstances of the transaction. Ideally, these will be password-protected printers if used by other persons outside the team
- adopting appropriate code names for transactions to disguise the nature of and parties involved in the transaction
- regularly reminding staff not to read confidential, market-sensitive documents in public places (for example, airports, planes) or have confidential discussions in places they could be overheard by others (for example, lifts, taxis), and
- ensuring that employees do not make unauthorised physical or electronic copies of confidential information and ensuring appropriate security measures are adopted where it is necessary for employees to remove or access physical or electronic copies of confidential information outside their workplace.

Handling confidential, market-sensitive information

Companies should also, when necessary, ensure that systems and controls are in place to quarantine confidential, market-sensitive information from contractors and other service providers that share access to the company's systems.

Consideration should be given to establishing discrete physical work areas for project teams if the project is likely to last for a significant period and involve large numbers of personnel. Off-site locations may be appropriate in some cases.

Information technology controls

It is important that information technology systems and practices are sufficiently secure to ensure that confidential, market-sensitive information is not inadvertently disclosed. The levels of security that a company will implement will depend on the sensitivity of the transaction and the nature of the company's information technology infrastructure, as there could be cost constraints for small companies. Systems and practices that may help include:

- storing confidential, market-sensitive information on systems that implement logical access controls and only allow access to authorised personnel — external servers and cloud-based systems may need to be reviewed to ensure security of access is maintained
- ensuring that all documents are password-protected from the outset
- providing separate passwords when transferring confidential, market-sensitive documents electronically. Also, such documents may be encrypted
- installing password-protection mechanisms for all electronic equipment, such as laptops, smartphones, tablets, USB drives and other storage media containing confidential, market-sensitive information or providing physical tokens for access that generate a new number each minute that can be provided via a smartphone, which replaces the password and ensures that directors, executives and external parties do not need to write down passwords which can be lost or stolen.. Automatic locking should be activated after periods of inactivity on these devices
- installing appropriate software so that confidential, market-sensitive information held on a tablet or smartphone can be remotely deleted, to prevent unauthorised third party access should the tablet or smartphone be lost
- placing appropriate controls over staff access to other employees' electronic mail
- careful use of PINs for conference calls, for example, using a PIN for a conference call on market-sensitive transactions once only rather than using the same PIN multiple times, and dedicating such PINs to conference calls on market-sensitive transactions rather than using group PINs accessed for general purposes. The person chairing the call should make every effort to be aware of the security procedures available to minimise the chance of inappropriate persons attending the conference call. This ensures that only the intended parties to the call can participate
- operating a document management system, depending on the size and resources of the company, that has the capacity to log who has accessed particular files and when the access occurred, and
- conducting regular reviews to ensure data storage and controls are up-to-date and secure.

Contact with external parties

- Given that the media and other external parties are likely to actively contact people they believe have inside knowledge, companies' policies should explicitly cover contact with the media and other relevant external parties. The existence of a binding policy and appropriate training assists employees in dealing with these approaches.

Leak investigations

- It is good practice for companies to have written policies and procedures on how a suspected leak of confidential, market-sensitive information is to be investigated, and employees should be made aware that such a process may be undertaken if there is a suspected leak. It is also good practice for companies to develop whistleblower policies that make it easy for employees to report instances of confidential, market-sensitive information being handled inappropriately.

- Companies need to have in place procedures to announce confidential, market-sensitive information immediately should such information be leaked and confidentiality is lost. A company could have a draft announcement prepared as a risk management measure in relation to such an eventuality.
- If a leak of confidential, market-sensitive information occurs, the company needs to consider whether to undertake or instigate a leak investigation that may include requesting its advisers to undertake a leak investigation of their own. Whether an investigation should be undertaken, and the level of formality and intensity of that investigation, will depend on the significance and impact of the leak. A review process not only highlights any risk areas but also acts as a deterrent, raising awareness and signalling to employees that the matter is taken seriously.
- Companies should develop clear guidelines as to when leaks, or the results of leak investigations, should be referred to external regulators or law enforcement agencies.
- Legal advisers may need to be involved in the investigation in the event that there is a subsequent external investigation by a regulator such as the Australian Securities and Investments Commission (ASIC) or the Australian Prudential Regulatory Authority (APRA).

Reasonable person test

- The disclosure obligations under Listing Rules 3.1, 3.1A and 3.1B require that, 'Once an entity becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of an entity's securities, the entity must immediately tell the ASX that information'. Companies need to be aware of the 'reasonable person' test in relation to market-sensitive confidential information, which may apply regardless of whether relevant transactions have completed.

Insider lists

Principle 2: It is good practice for companies to maintain an insider list when conducting a confidential, market-sensitive transaction

It is good practice for companies to maintain a register of both internal and external people (including directors and their staff) who are insiders on market-sensitive transactions, and efforts should be made to keep the number of these insiders to a minimum. A company may arrange for some or all of its advisers and other service providers to maintain their own insider lists. Where such an arrangement is adopted, the company should ensure that the list maintained by the adviser or service provider will be made available to it immediately upon request. Good practice is for companies to have a developed process for how and when people are brought 'inside' on sensitive transactions. It is appropriate for individuals to be reminded of their responsibilities each time they are made an insider.

It is also good practice for a company to implement a mechanism for removing from the insider list those people who are no longer involved in the transaction, as not all people remain insiders when the transaction takes place over a long period of time.

Unless advisers or other service providers are maintaining their own lists, they should provide the company with a list of the people within their firm that have been or will be given access to the company's confidential, market-sensitive information on engagement, and then ensure it is updated regularly. Lists need only be maintained until all the information about the transaction becomes public.

Insider lists should detail individually the people who are actively working on a transaction and indicate their role. People who are provided with confidential, market-sensitive information about a transaction on an ancillary basis — such as those acting in a compliance role, or those who are providing word-processing, editing, IT or printing services — could be listed by category in circumstances where they might not be expected to see the details of a proposal. Some management personnel not involved in the transaction may also be covered by this principle.

Confidential, market-sensitive information should only be provided to those authorised to receive it. Company insiders should be made aware of the person to contact should they need to know who

Handling confidential, market-sensitive information

else is on the insider list, including those from external advisory firms and other service providers that have been given access to confidential, market-sensitive information in relation to a transaction.

If an external adviser or other service provider needs to outsource a service in circumstances where confidential, market-sensitive information may be disclosed, it is good practice for the company to ensure the adviser or service provider first seeks the company's consent and ensures insider lists are maintained by that third party.

Internal policies: Individual confidentiality obligations

Principle 3: It is good practice for companies that deal with confidential, market-sensitive information to ensure their directors, executives and employees are aware of their confidentiality obligations

Employment contracts

Appropriate confidentiality obligations and securities trading restrictions should be incorporated into employment contracts and directors' appointment letters (by way of reference to the company trading policy for public listed companies) or other arrangements with all staff (including temporary employees) who may have access to the company's confidential, market-sensitive information. To ensure that a company can actively monitor any potential insider trading, employment contracts should also explicitly include the employer's right to access all communication records including corporate email and phone records. An employee's confidentiality obligations should survive beyond the termination of their employment.

Staff training

It is good practice to support policies dealing with confidentiality obligations with regular training programs and internal communications, as well as covering these matters in induction programs for new employees who might handle such information in their position. It is recommended that staff undergo training on the importance of not improperly or inadvertently divulging confidential information, with particular focus on employees with access to market-sensitive information.

Staff should be made fully aware of the implications of improper disclosure of confidential, market-sensitive information and insider trading, and the potential civil and criminal liabilities for both an individual and the company.

Exiting employees

When employees who have access to confidential, market-sensitive information leave a company, it is good practice to conduct an exit interview with them. This provides an opportunity for the company to secure the return of confidential information from the exiting employee and remind them of their ongoing responsibility to maintain the confidentiality of inside information. It may be appropriate to require written acknowledgement of this.

Securities dealing

Public listed companies are required to have a securities trading policy that covers directors and executives (key management personnel). It is good practice for the trading policy to extend to include all executives and employees on an insider list for any transaction. In addition to complying with the ASX Listing Rules, the following are measures that can be considered to implement a sound framework in relation to securities trading while a company is engaged in a confidential, market-sensitive transaction.

- Trading restrictions should extend to securities in companies with which the company is engaging in market-sensitive transactions.
- Where there is a transaction underway and employees are in possession of confidential, market-sensitive information, a company should consider putting in place blackout periods restricting trading for those employees in its and the securities of other relevant entities.

Where companies are not subject to the ASX Listing Rules, it is good practice to develop and implement a securities trading policy applicable to directors, officers and employees on an insider list relevant to a transaction. Such a policy would restrict trading in the company's and/or other parties' securities by employees who have possession of confidential, market-sensitive information. The trading policy should address the legal prohibition on insider trading.

Internal policies: Confidentiality agreements

Principle 4: It is good practice for companies to bind their advisers and other service providers by entering into confidentiality agreements before passing on confidential, market-sensitive information and to require confirmation from their advisers and other service providers that they have in place policies and practices relating to the handling and control of confidential, market-sensitive information that satisfy the terms of the agreement

Engaging advisers (such as investment banks, lawyers, accountants, tax advisers, specialist valuers, financial communications consultants and investor relations consultants) or other service providers (such as credit rating agencies, trading banks, stock brokers, registries and printers) to assist with market-sensitive transactions will necessitate the disclosure of confidential, market-sensitive information to those advisers. Companies need to consider how to minimise the risk that confidential, market-sensitive information provided to an adviser or other service provider is inadvertently or deliberately misused.

All advisers should be required to sign confidentiality agreements for specific transactions (unless an umbrella agreement or some other engagement arrangement fully sets out the confidentiality arrangements applicable to the transaction or a fiduciary obligation applies). These confidentiality agreements should be entered into as soon as possible once an adviser accepts a role in a specific transaction, and not delayed until the commercial terms of a transaction are finally negotiated. Among other things, these agreements should restrict an adviser's use of the company's confidential, market-sensitive information, including limiting the number of individuals within the adviser's business that are given access to the information. The agreements may also cover conflicts of interest.

Where an adviser has both private and public sides to its business, or needs to manage conflicts of interest, for example, between different clients, companies need to be confident that the adviser has sufficiently robust systems and controls in place to mitigate the risk of the company's confidential, market-sensitive information leaking from the private to the public side, or being used inappropriately within the firm.

It is good practice for the confidentiality agreements to confirm that the advisers and other service providers engaged by companies have in place the policies and practices relating to the handling and control of confidential, market-sensitive information that satisfy the terms of the agreement.

Umbrella agreements

Companies that are active participants in merger and acquisition transactions or capital raisings and use the services of investment banks and other advisers on a regular basis may consider setting up umbrella agreements. These types of arrangements set out in advance the general principles and practices an adviser must adhere to when undertaking work for the company.

Specific transactions may require additional side agreements, which would be negotiated at the time of the transaction, but all general principles, including how third parties are to handle confidential, market-sensitive information, would be set out in the general umbrella agreement.

Handling confidential, market-sensitive information

Specific terms relating to confidentiality that an umbrella agreement might incorporate include:

- requiring advisers to:
 - comply with the ‘need-to-know principle’ in relation to all confidential, market-sensitive information provided to them by the company, thereby restricting the people in the adviser’s firm to whom the confidential, market-sensitive information can be disclosed
 - keep all documents and information belonging to the company in a safe and secure manner and, if such action is consistent with legal obligations, promptly return or destroy such material at the company’s request
 - at the company’s request, establish and maintain an insider list in relation to any matter on which the company has instructed the adviser;
 - conduct and report on any leak investigation requested by the company, and
 - have in place appropriate IT systems and controls, including in relation to external servers, cloud-based systems, laptops, smartphones, tablets, USB drives and other storage media, and
- prohibiting advisers from:
 - publicly disclosing they are acting for the company without prior approval from the company, and
 - speaking to third parties in relation to the company without specific prior approval from the company.

Companies can also give consideration to how their information may be used by other divisions of a service provider, and consider restricting how it may be divulged by the provider in an umbrella agreement (for example, the credit division of a trading bank not advising the capital markets division).

‘Beauty parades’

Conducting a tendering process, often referred to as a ‘beauty parade’, to select advisers for a specific confidential, market-sensitive transaction involves a high degree of disclosure, including to parties that miss out on a role in the transaction and have no ongoing relationship with the company. Before releasing any confidential, market-sensitive information to potential advisers, companies should require them to sign confidentiality agreements. If investment banks are participating in the tender, the confidentiality agreement should include restrictions on the particular business units of the bank that are permitted access to the confidential, market-sensitive information. Where possible, companies should keep the number of parties invited to tender to a minimum, taking into account the importance of competitive tension in selecting advisers.

Sounding the market

Principle 5: It is desirable for companies to know which, when and how potential investors are being sounded on their behalf in relation to a transaction involving the company

Sometimes it is important to obtain direct market feedback from potential or existing investors about a transaction, depending on the company’s circumstances and on market conditions in general. However, it is important that, when the company is involved in the process, the confidentiality of market-sensitive information is maximised when taking a sounding on capital raisings or merger and acquisition proposals, and formal procedures should be adopted to ensure there is no breach of continuous disclosure or insider trading laws.

Companies should have a good understanding of the process that their banks or advisers intend to undertake if they sound the market in relation to a potential capital raising or other transaction. In order to arrive at this understanding, it is useful to request details of the actual process including:

Handling confidential, market-sensitive information

- the specific investors the bank or adviser intends to approach and whether the investors have appropriate controls for protecting confidential, market-sensitive information and not using it to trade until it is generally available
- the timing of any approaches
- the proposed limit on the time that information will be available to potential investors, and
- the intended number of potential investors, with a view to keeping it to the smallest number possible
- consideration of whether there is a need for a cleansing statement to be issued.

Appendix A: Checklist for companies when engaging advisers who will handle confidential, market-sensitive information

Advisers who regularly deal with confidential, market-sensitive information relating to transactions from a range of parties should have comprehensive and restrictive controls over personal trading in financial products by their directors and employees. The scope of these practices and procedures will depend on the specific circumstances of the advisory firm and its activities.

It is good practice for companies engaging such advisers to enquire whether the adviser:

- maintains lists of restricted entities. Among other things, these lists should ordinarily cover:
 - entities the firm is currently advising or acting on behalf of, and
 - entities about which the firm has confidential, market-sensitive information
- requires pre-clearance of all securities trading.

In addition, further controls may be appropriate for investment banks and financial advisers. Therefore, it is good practice for companies engaging such advisers to enquire as to whether the adviser's securities trading policy requires employees who may receive confidential, market-sensitive information to:

- disclose, on joining the firm, all their investments in financial products (both listed and unlisted)
- disclose, on joining the firm, all brokerage and trading accounts they control or in which they have an interest
- trade through an approved broker, and where that broker is not the firm itself, authorise the firm to receive copies of all contract notes or records of trade directly from the employee's broker, and
- impose, depending on the particular business area of the adviser, additional restrictions on trading including:
 - minimum holding periods, and
 - prohibitions on trading in financial products of issuers in particular industry sectors or competitors of particular clients.

It can also be useful for companies to enquire of their advisers if they have implemented an IT compliance system that tracks, audits and oversees employees' securities transactions.

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