cole corporate

ASX Corporate Governance Council
C/- ASX Limited
PO Box H224
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12 June 2018

Attention: Mavis Tan
By Email to: mavis.tan@asx.com.au

Dear Mavis,

Consultation Draft (CGC Principles and Recommendations 4th Edition) - Submission

I attach for your consideration a schedule of our submissions in response to your invitation.

The opportunity afforded to make a submission is very much appreciated.

Given contemporary developments in society's attitude to corporations and our societal institutions generally, it is timely and appropriate for a review of the 3rd Edition to be undertaken.

About Cole Corporate

Cole Corporate is a boutique corporate governance consultancy firm based in Perth, Western Australia.

It's principal is Steven Cole Llb(Hons) FAICD whose relevant extensive experience with respect to listed entities includes:

- Chair of NMT (ASX code)
- NED of MCE (ASX code)
- formerly chair of 3 other ASX listed entities
- active corporate governance consultant, author and conference/seminar speaker in Australia and internationally
- former State President (WA) and national board member of AICD.

Regards,

Steven Cole

Schedule of Comments in response to the ASX Corporate Governance Council's request for submissions on the consultation draft of the 4th edition of its Corporate Governance Principles and Recommendations ("CGP&R")

1 General Comments

1.1 Timeliness of review in the context of increasing social commentary, including via Banking Royal Commission, concerning corporate culture and social licence to operate.

(a) The Council is to be complimented on its proactive response to these matters.

(b) In particular the general thrust of the revised Principal #3 "Instil the desired culture" has some qualified merit.

(c) However, the CGP&R should be framed as an enduring instrument with appropriate balance across the full spectrum of governance structures, systems and cultural attributes which have relevance, not only in response to contemporary issues, but also sustainably for the future.

(d) Despite the contemporary reactive importance of matters which collectively may be embraced by descriptors such as "culture", "values", "code of conduct" and "licence to operate" it is perceived that the extent and detail to which these matters are addressed in the CGP&R is given too great a degree of focus in the overall context and balance of the CGP&R.

(e) More specific comments are included in paragraph 2 below.

1.2 The degree of detail and extent to which the supporting "Commentary" is expressed, risks the CGP&R becoming too "prescriptive" of asserted governance practice rather than the CGP&R being high level "descriptive" statements of accepted good governance practice. Given the extent to which the CGP&R have become quasi-regulatory in their effect, then the practical risk of this more "prescriptive" approach is to suppress the innovative evolution of governance practices, which may not be consistent with the CGP&R, but which may lead to "better" governance outcomes.

It would be arrogant and naïve to suggest that even the proposed draft 4th edition of the CGP&R is the pinnacle of good governance practice for time immemorial, especially as by definition with the evolution of the 3 editions to date, there will always be future opportunities for continuing improvement.

2 Comments on specific sections of the CGP&R

2.1 Recommendation 1.2 – Commentary

With respect to candidates standing for election as a director for the first time the commentary states that the following should be provided to security holders:

(a) "confirmation that the entity has conducted appropriate checks into the candidate's background and experience and the outcome of those checks" (emphasis added).

This requirement to disclose the "outcome" may be pernicious and problematic depending on the outcome of the checks, the relevance of any background issues to the candidate's role as a director, the historical age of the matters revealed and the extent of any contention surrounding the veracity of the outcome of the checks.

Perhaps the relevant words could be re-expressed "and any material concerns arising from those checks reasonably considered by the board to be material to the candidate's suitability for office".

(b) "a statement by the board as to whether it supports the election or re-election of the candidate and a summary of the reasons why".

It is suggested that this paragraph be deleted in its entirety. There is a body of belief in the marketplace that boards are currently over-influential in the election and succession of fellow

board members, notwithstanding the counter "good governance" practice of boards being active in succession planning. By deleting this paragraph it still will be open to boards to make recommendations (and give reasons for so doing should they so desire), but not to expressly mandate the practice.

2.2 Recommendation 1.5(c)

The requirement for a S&P/ASX300 index entity to have a prescriptive measurable objective of having "not less than 30% of its directors of each gender within a specified period" prospectively may:

(a) breach discrimination laws, unless a caveat was included to qualify the approach within the scope of anti-discrimination laws;

(b) result in other than the best candidates for the role being appointed;

(c) trigger a drive to exit from the role incumbents who are currently performing to an exemplary standard for the benefit of the company and its security holders.

These comments apply irrespective of whether the minority of board members are male or female.

Also we are not convinced that the specificity of diversity classifications in the second paragraph of "Commentary", and in paragraph 2 of Box 1.5, is necessary or warranted. I would recommend the deletion of all words after "facets" in each of those paragraphs. Of note these paragraphs are more extensive in their descriptions of diversity classifications than is the paragraph on page 15 that is penultimate to Box 1.5 dealing with board diversity. This leaves open the question as to why this difference in expression between these paragraphs exists, especially as the less descriptive paragraph deals specifically with board composition, thus arguably implying that those omitted diversity classifications are not as relevant or meritorious for consideration in connection with board appointments than they are in connection with other endeavours of the company. That would be an unfortunate implication.

2.3 Recommendation 1.6(a)

The addition of the words "for each reporting period" are too prescriptive and unwarranted. They imply that each of the full board, each committee and each individual director's performance should be evaluated annually. As a person actively and professionally engaged in board evaluations, their structure and their optimal utility, my strong professional belief and recommendation is that such a prescriptive approach would likely to be counterproductive.

Recommendation 1.6(a) of the CGP&R obliges the process of the evaluation to be disclosed, and Recommendation 1.6(b) requires disclosure of whether a performance evaluation in accordance with that process was undertaken for that reporting period.

We note that a number of companies with which we interact phase their evaluation processes over a 3 year triennium with more detailed focus on different groups (board, committees, individual directors) each year.

2.4 Recommendation 2.3 – Commentary

With respect to the paragraph immediately preceding Box 2.3 it is recommended that all bar the first sentence be deleted. The effect of this paragraph (other than the first sentence) is to effectively reverse the onus of establishing "independence", thus giving greater paramountcy to the prescriptive criteria in Box 2.3 than is otherwise warranted. Neither the case has been made not the evidence provided to justify this reversal of onus.

2.5 Recommendation 2.7

With respect, this is a matter for the individual director to resolve in accordance with his/her legal duties and responsibilities, and desirably for the board/company to assist with, in accordance with inclusive and supportive good governance for its board members. It is not a matter that warrants disclosure generally to the market. The deletion of this unwarranted recommendation is suggested.

2.6 Principle 3 : Instil the desired culture

Although supportive in general terms of the concept of Principle 3, the specificity and prescription with which the issues under this Principle are dealt with are troubling.

Importantly our primary concern is not to extend the class of persons to whom a director's duty is owed (expressly or implicitly) beyond the company itself, nor to implicitly create a new (un-legislated) quasi-regulatory responsibility upon directors of listed entities.

In addition, care must be taken to ensure that unintended consequences of the CGP&R do not mischievously increase the prospective of class action claims being funded against listed entities.

To guard against these risks we recommend that the Principle be amended by deleting all words after "lawfully" and replacing them with "and ethically".

We also recommend that the closing words of paragraph 1 of "Commentary" read "….unlawfully or unethically".

We further recommend the deletion of all words after "stakeholders" in line 6 of the 2nd paragraph under "Commentary" (in relation to Principle 3 itself) until the commencement of Recommendation 3.1

We also note that these bullet points recommended to be deleted are not fully aligned with those items in Box 3.2, but are to an extent repeated in Box 3.2.

2.7 Recommendation 3.1

Although the concepts of "core values" and "principles" (and their disclosure) are supported, the prescriptive specificity as to what should be included and who within the company should do what in their development and embedding throughout the company is not supported.

We recommend that the Recommendation be left at a "high level" allowing the company to apply the principle as best suits it. Thus the final 3 paragraphs of "Commentary" are recommended to be deleted.

2.8 Recommendation 3.2(b)(2)

We recommend the rewording of this subparagraph to include after the word "that", the words ", in any material respect,".

With respect to code breaches by other than directors and senior executives, it should not be required for the board to be informed unless:

(a) there is a material breach of the code; AND

(b) that breach, in a material respect, calls into question the culture of the organisation.

The inclusion of the words "in any material respect" also need to be included before the word "call" in line 3 of the 3rd paragraph of "Commentary".

2.9 Recommendation 3.4 (anti-bribery/corruption policy)

Although we do not question the desirability of companies adopting such policies, I enquire why these policies have been specifically targeted for greater priority and focus than say policies concerning:

- occupational health and safety
- director conflicts of interest
- the environment
- privacy/cyber-risk

to mention but the tip of a raft of other governance related policies that might be included.

We recommend the deletion of Recommendation 3.4.

2.10 Recommendation 3.3(b) – (Whistleblower policy)

To some extent we question the need for the inclusion of this recommendation on the same grounds referred to under 2.9 above. However, we accept it has greater tangential legitimacy due to its closer tie to Principle 3 generally.

However, on a similar basis as expressed under paragraph 2.8 above, we recommend the inclusion of the words ", in any material respect," after the word "that" in Recommendation 3.3(b).

2.11 Recommendation 4.4

We recommend:

(a) in line 1 delete "validate" and replace with "reasonably assure";

(b) in line 3 delete "and provide…..investment decisions".

The word "validate" is too strong a word. Line 3 risks imposing fresh obligations beyond existing legislative and ASXLR requirements that may be used to encourage securities' class action claims.

2.12 Recommendation 6.4 (all resolutions to be decided by poll)

It is difficult to argue against the mandated use of a poll for substantive resolutions of security holders where there may be contention involved.

However, as a general proposition for ALL resolutions at meetings of security holders, we strongly believe the recommendation to be fundamentally flawed, including for the following reasons:

(a) some resolutions at meetings of security holders may be "procedural" and at law it is those present in the room or at the meeting who have the right to decide, especially as the "procedural" resolution may be called "from the floor", and not those people who did not attend, or found prioritised time and interest to attend, and have filed a proxy vote only (especially as the procedural motion for resolution probably would not have been included in the notice of meeting).

(b) At a time of criticism of the AGM, for all resolutions to go to a poll, even those supported by an overwhelming absolute majority of meeting attendees and proxy holders, is an unreasonably burden upon the natural flow of business at the meeting, and enjoyment by attendees of the meeting process.

(c) The meeting chair is responsible for the proper conduct and business of the meeting. If the chair is failing in his/her responsibilities by allowing voting on a "show of hands" when the prospective proxy position is to the contrary, or even close, then the chair should be held to account for breach of duty/responsibility.

(d) If any shareholder(s) wish to insist upon a poll, then both the law and most company constitutions facilitate this.

Recommendation 6.4 should be removed from the 4th Edition.

2.13 Principle 7 : Recognise and manage risk

(a) We recommend the deletion of the words "the key drivers of an entity's long term success" in lines 1 and 2 of the last paragraph of "Commentary" under the main part of Principle 7.

The words are superfluous and restrictive to "long term" only. Of note "short, medium and long term" are used later (appropriately) in the next sentence.

(b) Of general interest we have always been bemused why "risk" draws special mention in the CGP&R yet its cousin "strategy", which is of equal importance and relevance from a governance perspective, does not receive comparable attention. Should not both the "upside" of strategy be featured in the CGP&R comparably to the "downside" of risk?

2.14 Recommendation 8.4

Although we support the broad concept that directors (or related entities) should not be providing services (whether consulting or otherwise) directly or indirectly to companies upon which they sit, except in special circumstances, we wonder why the Recommendation has chosen to single out "consultancy or similar services" for such special treatment. Why not any supply provided to the company by a director or a related entity?

Further, the concept of the company first having taken independent advice as to the criteria mentioned in the Recommendation is as problematic as the issue being sought to be addressed with inordinate costs and commercial timing delays.

Finally the requirement for full disclosure of material terms is burdensome (for minor consultancy matters) and is non-specific as to the timing of that disclosure.

The Corporations Act already addresses related party contracts and arrangements with severe penalties for those in breach.

The Recommendation is unwarranted, unnecessary and poses more problems than it seeks to resolve. It should not form part of the CGP&R.

2.15 Glossary – "social risks" – Recommendation 7.4

We recommend all words after "… local communities)" be deleted. The remaining words are too problematic and imprecise for a company to make an appropriate comment concerning its risks in the terms of Recommendation 7.4. In particular, what are "accepted community standards" (what "community"?; what constitutes "acceptance"?).