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27 July 2018

Ms M Tan
Australian Securities Exchange Limited
Exchange Centre
20 Bridge Street
SYDNEY NSW 2000

Via email: mavis.tan@asx.com.au

Dear Ms Tan

ASX Corporate Governance Council Corporate Governance Principles and Recommendations proposed changes to the third edition (issue of fourth edition)

I refer to ASX Corporate Governance Council's and the ASX's Consultation Papers dated 2 May 2018, relating to proposed changes to the third edition of the "ASX Corporate Governance Principles & Recommendations" (ASXGCP&R 4). Please accept our submission in relation to the proposed changes in issuing the fourth edition of the ASXGCP&R 4.

SSAMM welcomes the opportunity to comment on the ASXGCP&R 4 changes. Our detailed comment is attached. In general, SSAMM supports many of the proposals contained in the draft revised ASXGCP&R 4.

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Submission Outline

SSAMM Management Consulting (SSAMM) is pleased to submit the following observations on the proposed ASX Corporate Governance Council (ASX CGC)[1] changes to the third edition of the "Corporate Governance Principles & Recommendations" so as to issue a fourth edition. Our Submission is a commentary aimed to assist all concerned with better corporate governance practices by highlighting key matters of interest in the proposed changes to the ASXGCP&R 4. Our Submission is based on our extensive local and global experience and expertise in corporate governance.[2]

Submission focus

Our Submission will address some but not all the recommended changes. Although all the recommended changes are important and will significantly continue to generally improve corporate governance practice, we have selected the key areas of focus as Principle 3 and 8 of the 9 new Recommendations but excluded commenting on changes to Recommendation 1.5 due to its greater impact on reporting requirements and for reasons set out below. Overall, listed issuers will face greater reporting under the proposed changes in the ASXGCP&R 4. The changes will affect annual reports for financial years beginning on or after 1 July 2019 or 31 December 2020 for those entities with a 31 December balance date.

SSAMM generally supports the structural changes to the ASXGCP&R 4 in that continuous improvement benefits market integrity by enhancing transparency and therefore the confidence of all market participants, for example by not distinguishing trusts and externally managed issuers from the requirements of the ASXGCP&R 4. SSAMM will not comment on compliance with the new Guidelines in terms of possible unintended consequences and or the potential for undue compliance burdens; nor on the sufficiency of the level of commentary and guidance being provided by the ASX CGC; and we are not setting out to identify significant omissions and deficiencies in the ASXGCP&R 4 overall.

[1] The ASX CGC was convened by the ASX in August 2002 and comprises 20 industry and shareholder bodies. It has no statutory or other constitutional basis, but it is intended to have an ongoing role in reviewing the implementation of the Guidelines and a number of other advisory functions detailed in the Corporate Law Economic Reform Proposals No 9 (CLERP 9) Discussion Paper released by the Commonwealth Government in August 2002. Participating organisations include: Australasian Investor Relations Association, Australian Council of Superannuation Investors, Australian Financial Markets Association, Australian Institute of Company Directors, Australian Institute of Superannuation Trustees, Australian Shareholders' Association, Australian Securities Exchange Limited, Business Council of Australia, Financial Services Council, Financial Services Institute of Australasia, CPA Australia, Governance Institute of Australia, Group of 100, Institute of Internal Auditors Australia, Institute of Public Accountants, Law Council of Australia, Property Council of Australia, Stockbrokers and Financial Advisers Association Limited.

[2] Who is SSAMM? SSAMM is a leading provider of corporate governance research and advice to the global financial community, SSAMM issues governance research and advice on selected Australian companies giving institutional investors guidance as requested (corporate actions, board appointments, directors' remuneration reports; and other related corporate governance matters). SSAMM also provides governance advice to S&P ASX 300 clients through their Chairs and other company representatives in engaging with their institutional investors.

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Some of the substantive proposed changes to the ASXGCP&R 4 include, but not limited to, the following:

- introducing 9 new recommendations in Principles 2, 3, 4, 5, 6 and 8. This expands the total number of recommendations from 29 to 38. with a focus on corporate values, culture and licence to operate; and
- expanding the categories of relationships that may indicate that a director may not be independent to include "close personal ties" rather than family ties at box 2.3 in Recommendation 2.3.

Drivers to the proposed changes to the Guidelines

The ASX CGC states that 12 months ago it was influenced by a need to address emerging domestic and global issues in corporate governance as the driver to the changes being proposed in the 4th edition of the ASXGCP&R 4 centered around an entity's social licence to operate; its culture; whistleblower policies; corruption concerns; carbon risk and the rate of adoption of the 3rd edition changes to the ASXGCP&R.

In summary the SSAMM Submission to the proposed changes to the ASXGCP&R 4, whilst supportive also highlights that two major global governance trends are not being fully integrated into the ASXGCP&R 4 by the ASX CGC as strong sources of better corporate governance as set out below, namely responsible investing through the environmental, social and governance (ESG) lens and Risk Management practices.

The last major rewrite of the Guidelines was just in 2014 with third edition after a seven year gap with the second edition in 2007, just as the GFC was biting. The ASX CGC noted at the time that overseas legislators were facing demands for mandatory requirements to address the governance failings that allegedly led to the GFC. The ASX CGC saw the rewrite as heading off similar demands in Australia[3].

This was particularly apparent in the new requirement in the third edition, at Principle 7, that issuers disclose whether (and how) they have regard to "economic, environmental and sustainability risks". While this requirement seemed far-reaching, the ASX CGC made the point that it is considerably less onerous than some overseas requirements, such as UK's "enlightened shareholder duty"[4] [5].

In terms of ESG and Risk Management practices so much more can be done by the ASX CGC in relation to Principle 7 and its recommendations and the growing global tsunami of support for greater and deeper corporate adherence to ESG and Risk Management practices by corporate entities in response to their investors.

[3] The ASX CGC adopted the same 'principles based' approach as that taken in the UK Combined Code which governs issuers listed on the London Stock Exchange. ASX listed issuers are at liberty not to comply with the recommendations, but if they do not, they must explain why not. The Guidelines were built on the belief that one size does not fit all issuers in the Australian market. This model rejected the more prescriptive approach adopted in the US by the Sarbanes-Oxley Act 2002 and in the proposed amendments to the New York Stock Exchange's listing rules which required compliance with specific practices.

[4] Gamble, A. and Kelly, G. (2001), Shareholder Value and the Stakeholder Debate in the UK. Corporate Governance: An International Review, 9:110–117.

[5] Keay, Andrew. "Tackling the issue of the corporate objective: an analysis of the United Kingdom's enlightened shareholder value approach." Sydney L. Rev. 29 (2007): 577.

Maintaining and exporting our standard

Diversity on boards is important in terms of skills and experience in meeting a listed entity's strategic plan. Even a simple cursory review would reveal that a corporate strategy of export is a key to corporate success. However, the overall ethnic diversity of our listed entity boards appears to be stifled by a lack of skills, experience and representation in the markets Australia seeks to export our goods and services.

Much has been stated of the trust in brand Australia[6]; this also goes to our governance practices. Australia is ranked first in the region in terms of corporate governance practices when benchmarked against other jurisdictions in Asia; exporting our good governance practices through board ethnic diversity and inclusion would be a significant strategic outcome for any competitive Australian company[7]. Further in this same vein we see that other trading post jurisdictions are also reviewing their corporate governance codes; which are also an opportunity for Australia to engage with these jurisdictions[8]. Whilst we can boast our premier standing for our governance practices we are behind in our behind in our shareholder voting process (more on this point in the body of our submission)[9].

The changes being proposed in the 4th edition of the ASXGCP&R 4 are centered around an entity's social licence to operate; its culture; whistleblower policies; corruption concerns; carbon risk and the adoption of the 3rd edition changes to the ASXGCP&R which prompts the discussion below on two very relevant themes around Corporate Social Responsibility (CSR); responsible investing through ESG and Risk Management practices.

Is CSR still important?

There is a growing trend in the 21st century which may be a shift away from CSR as the driver for corporate social responsibility or perhaps a redefinition of its place in the corporate governance framework. The trend has been two-pronged; one is the rise and rise of the influence of institutional investors globally and in each national jurisdiction and their use of socially responsible investment principles using the lenses of environmental, social and governance issues, collectively known as ESG. ESG is now an accepted 'concept' applied by institutional investors such as banks, pension systems, superannuation funds and fund managers across the globe, departments in these organisations are staffed by teams of professionals managing the wealth of beneficial members – retirees, pensioners and superannuants valued in the trillions of dollars[10].

The second prong is the shift of CSR from the voluntary governance codes of the 1990s to corporate governance compliance becoming mandatory and set in

6 McCarthy, Breda L. Trends in organic and green food consumption in China: Opportunities and challenges for regional Australian exporters [online]. Journal of Economic & Social Policy, Vol. 17, No. 1, Jun 2015: [6]-[31]
7 Asian Corporate Governance Associations 2016 CG Watch survey
8 Hong Kong Exchange Nov. 2017; UK Financial Reporting Council Dec. 2017 and Singapore Exchange Jan. 2018
9 The new Recommendation 6.4 brings us into line with Hong Kong and Singapore who implemented voting by poll under their listing rules in 2009 and 2015 for Singapore.
10 Eccles, R. G., Kastrapeli, M. D. and Potter, S. J, 2017, How to Integrate ESG into Investment Decision Making: Results of a Global Survey of Institutional Investors. Journal of Applied Corporate Finance, 29: 125-133. doi:10.1111/jacf.12267

legislation, and stock exchange listing rules also backed by law[11]. Together with this shift has been the acceptance of risk management practices as integral to corporate governance and also enshrined in legislation such as the requirement of all Australian financial institutions to maintain risk management systems[12]. Finally there is the concept of 'sustainability' in that the strategy and or activity of the company must be focused beyond the short or medium term. Together these two prongs are supported by the growing trend in the rise of the application of ESG by institutional investors globally that has incorporated CSR into the ESG concept, as applied by institutional investors in their assessment of their portfolio of investments in all jurisdictions and in many ways converging a local approach to corporate governance to a global approach.

Institutional investors have a fiduciary responsibility to act in the best interests of the beneficial or ultimate owners of the funds under their management. The shift of these funds from investing in companies that are not only profitable but continue to have a growing trend to profits to being more concerned with how these profits are achieved and the internal governance of the company and the company's relationship with other stakeholders.

The exponential growth of shareholdings and subsequent influence on companies of institutional investors demands the attention of corporate citizens far more intently than does the social pressure of being responsible, as directors also have duties and responsibilities to be totally responsive to their shareholders[13].

Socially responsible investment principles and ESG

The term social investment is interchangeable with ethical investment. The origin of socially responsible investment principles can be traced to the nineteenth century and religious movements in the UK and US such as the Methodists and Quakers. These and other religious movements have consistently sought ethical and socially responsible investment of their funds by not compromising on their principles; for example the churches would not invest in companies involved in gambling or the sale, distribution or manufacture of alcohol.

This same motivation has been manifested in the twentieth century where US church groups do not invest in tobacco companies and where they do, they actively use their shareholding to change the companies behaviour to be more socially responsible; for example the investors in 1994 forced McDonald's to ban all smoking in all its corporate owned restaurants [14].

11 Griffith, S. J, 2015, Corporate Governance in an Era of Compliance.Wm. & Mary L. Rev, 57, 2075.
12 Corporations Act 2001 (Cth), s912A, Obligations of Financial Services Licensees.
13 Peter Iliev, Karl V. Lins, Darius P. Miller, Lukas Roth, 2015, 'Shareholder Voting and Corporate Governance Around the World' (Oxford University Press on behalf of The Society for Financial Studies); doi:10.1093/rfs/hhv008
14 Crosby M H, 2000, Religious challenge by shareholder actions: changing the behaviour of tobacco companies and their allies. BMJ : British Medical Journal;321(7257):375-377. "In 1972 the Interfaith Center on Corporate Responsibility was established in New York. It now comprises a coalition of around 300 Protestant, Jewish, and Catholic institutional investors who use their investments to challenge companies on various social issues".

Contemporary examples of these social and ethical investment concerns of institutional investors include human rights violations such as poor work or employment practices and conditions (the use of human trafficking or child labour in the corporate supply chain are examples); production practices that impact the environment; and genetic engineering to livestock or plants are some further examples.

Examples of 'E S and G':

There are a series of socially responsible investment filters that have been developed since the later 1980s through to the most recent in 2006 - the UN Principles for Responsible Investment (UNPRI).15 It is essential to the development of socially responsible investment that large institutional investors are actively involved in screening potential investments as appropriate as companies that are socially and ethically responsible and sustainable. The following are the series of investment filters:

- Coalition for Environmentally Responsibly Economies (Ceres) (1989) is a group of investors and advocacy groups. One of Ceres most recent publications is "the 21st Century Corporation Roadmap for sustainability."[16]
- UN Global Compact 1999 – it now has 10 principles (2004) that spans the concerns over corruption, environmental practices and human rights and labour standards amongst companies across the globe.[17]
- OECD Guidelines 1999; 2000 (multinationals); and 2004. The Guidelines are recommendations addressed by governments to multinational enterprises. They provide voluntary principles and standards for responsible business conduct consistent with applicable laws18. Some critical analysis has found them impact wanting.[19]
- Global Reporting Initiative GRI – Sustainability 2002 – 2013. This is based on a partnership formed between Ceres and the UN in 1999. The role of multinational enterprises in sustainability reporting in terms of disclosure on economic, labor and ESG indicators is captured through company-level information on sustainability reporting from the Global Reporting Initiative. The current reporting trend is high; the Winkler study covers 2,020 companies in 81 countries and 54 sustainability indicators.[20]
- UNPRI – 2006 – This initiative was convened by the then UN Secretary general in bringing together an international group of investors to respond to the ever increasing application of ESG to the investment process, signatories went from the hundreds to the thousands globally and continue to grow with not only funds signing up but also nations, including Australia[21].

ESG screening looks at the ethical behaviour of the companies that may be the

[15] The Principles can be found online at http://unpri.org/about/
[16] https://www.ceres.org/resources/reports/21st-century-corporation-ceres-roadmap-sustainability
17 See the principles at: https://www.unglobalcompact.org/what-is-gc/mission/principles
18 Zerk, J. A. (2006).Multinationals and corporate social responsibility: Limitations and opportunities in international law(Vol. 48). Cambridge University Press.
19 Siems, M. M., & Alvarez-Macotela, O. S, 2017, The G20/OECD Principles of Corporate Governance 2015: A Critical Assessment of Their Operation and Impact.
20 Winkler, D, 2017, How do multinationals report their economic, social, and environmental impacts? evidence from global reporting initiative data.
[21] Lee, D. D., Fan, J. H., & Wong, V, 2018, No More Excuses! Performance of ESG Integrated Portfolios in Australia.

target of investment, the screening assesses the conduct of these companies such as good employment practices or taking active steps to eliminate or reduce pollution or their carbon footprint in their activities or that these companies do not themselves invest in proscribed industries such are armaments. ESG screening is formulated by institutional investors into investment policies where this screening is an integral part of the investment process and to meet the objective of enhancing shareholder value – the institutional shareholders value. This process becomes an extremely influential factor in changing poor corporate governance by corporations as they seek investment capital in a competitive investment capital market.

ESG is a series of screening lenses utilized by institutional investors such as pension systems, superannuation fund managers, investment managers, and sovereign wealth funds[22] that globally manage investments on behalf of their beneficiaries to filter those investments and select those that are socially and ethically responsible investments in terms of their impact on the environment, society and the quality of the governance of the company – the investment vehicle, two examples of these globally active institutional investors using ESG, including investment in Australian stocks, are CalPERS and Blackrock.

Impact of CalPERS ?

In 2014 CalPERS surpassed $300 billion in total fund market value. This US pension fund serves more than 1.9 million members as a retirement system[23]. By comparison CalPERS total fund market value is just over half that of the Saudi Arabian sovereign fund (SAMA) which is the in the top 5 sovereign funds globally[24]. SAMA has assets of over $514 billion, according to the Sovereign Wealth Fund Institute[25]. CalPERS and SAMA invest in a variety of local and international asset classes across the globe. SAMA for example made an investment of $3.5 billion in the now ubiquitous, along with Air BnB Uber Technologies.[26]

Impact of Blackrock ?

BlackRock, Inc. is an American global investment management corporation. BlackRock is the world's largest asset manager with $6.3 trillion (USD) in assets under management as of December 2017; the company took in $264 billion in new funds just in 2017[27]. The size of Blackrock is six times greater than the sovereign fund of Norway which is the largest sovereign wealth fund in the world; Blackrock is even larger than the total of the top 5 sovereign funds in the world that include China, Kuwait and Abu Dhabi. Norway's Sovereign Wealth Fund - the Government Pension Fund Global has $1 trillion (USD) dollars in assets with the other top five

22Sovereign Wealth Funds: When countries have excess reserves, they may create investment vehicles that deploy that money and generate returns for the nation itself. The money in such funds is invested across the globe and in a range of asset classes.
23 https://www.calpers.ca.gov/page/home
24 https://www.swfinstitute.org/sovereign-wealth-fund-rankings/
25Ibid.
26 Bloomberg 2006, “Uber Receives $3.5 Billion Investment From Saudi Wealth Fund” Eric Newcomer and Glen Carey, June 2. It’s worth noting that the Managing director of Saudi sovereign wealth fund joined the Uber board.
27 https://www.blackrock.com/corporate/about-us

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funds each holding just under $1 trillion (USD) dollars in assets[28].

Increasing institutional investor influence:

Berle and Means identified the influence of large shareholders in the 1930s.[29] The influence was highlighted as increasing the separation between the owners (shareholders) and controllers (directors) of the business. Today, in the second decade of the 21st century, the trend is at its most extreme example large shareholders are institutional investors that own significant proportions of equity in many companies across the globe with an influence on their stock portfolios second to none, dominating across national jurisdictions. Institutional investors look now to play a key role in corporate governance with an internationalization of their cross border portfolios, they look at the corporate governance of the companies they hold, especially in light of financial crises that have occurred in many parts of the world and also globally in 2008.[30]

The global financial crisis (the crisis) stressed the important role of good corporate governance in reestablishing trust in the global financial markets. In statements issued by the International Corporate Governance Network (ICGN) on the crisis, during the period 2008 to 2009 it emphasized that institutional investors have a responsibility to generate long term value on behalf of their members – pensioners, savers “their beneficiaries” of these multi-billion dollar funds and fund managers. The statements focused on “taking into account governance factors …..governance is not a parallel activity ….but integrated into the investment…..by developing ….transparency …for the institutional investor to exercise their rights in a responsible, informed and considered way”.[31]

United Nations Global Compact (UN Global Compact):

The launch, in 2000, of the United Nations Global Compact as both a policy platform and a practical framework for companies committed to sustainability and responsible business practices based on universally accepted principles in the areas of human rights, labour, environment and anti-corruption, and to achieve support of broader UN goals. It has 7,000 corporate signatories in 135 countries[32]. The UN Global Compact gave rise to another UN initiative the UN principles for responsible investment (UNPRI).

As with CSR the UNPRI/ESG initiative is voluntary. In July 2004 in London, the Executive Director of the United Nations Environment Programme announced plans to create a set of neutral, global, UN-endorsed principles[33]. In early 2005, the then

28 https://www.swfinstitute.org/sovereign-wealth-fund-rankings/
29 Bendickson, J., Muldoon, J., Liguori, E., & Davis, P. E, 2016, ‘Agency theory: the times, they are a-changin’, 54(1) Management Decision,174.
30 Ibid.
31 Strenger, C, (2017), The Future of Corporate Governance. Managing for Responsibility: A Sourcebook for an Alternative Paradigm
32 Silver, N, 2017, La grande illusion. In Finance, Society and Sustainability, Palgrave Macmillan, London, 101.

United Nations Secretary-General Kofi Annan invited a group of the world's largest institutional investors to join a process to develop the Principles for Responsible Investment. A 20-person investor group drawn from institutions in 12 countries was supported by a 70-person group of experts from the investment industry, intergovernmental organisations and civil society. The Principles were launched in April 2006 at the New York Stock Exchange. Since then the number of signatories has grown from 100 to over 1,800. The UNPRI's growth has been consistent since it began in 2006.[34]

The objectives of the 6 UNPRI principles are to support, through ESG, an economically efficient, sustainable global financial system for long-term value creation to benefit the environment and society as a whole; objectives that are aligned with CSR but are backed by the hard influence of capital investment. The UNPRI also encourages the adoption of the UNPRI and ESG and collaboration on their implementation toward a sustainable global financial system by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

It may seem that the UNPRI and their ESG lens is simply another example of calls for companies to adopt CSR policies such as the EU's request for CSR policies statements by companies tendering for contracts or the Australian ASX requirements under the listing rules that require companies to report their performance under environmental legislation[35], however the focus of screening companies through ESG filters is a process that appears to achieve both better corporate governance and corporate performance, arguably borne out by ESG reporting, including sustainability reporting[36].

Reporting and Voting for CSR and ESG?

The power and right to vote: impacts on corporate governance

There is a rising trend in shareholders, especially institutional shareholders exercising their right to actively vote their shares at general meetings of shareholders, globally[37]. The central and arguably the most important right a shareholder holds is the right to vote at a general meeting of shareholders of the company; it can be seen as fundamental as a means of control in modern corporations. The right for shareholders to vote determines who will be a director of the company and may also give directors direction on the strategy the company may pursue depending on the Constitution or governing rules of the company[38].

34 https://www.unpri.org/pri/about-the-pri
35 Dumay, J., & Hossain, M. A, 2018, Sustainability risk disclosure practices of listed companies in Australia. Australian Accounting Review.
36 Dyck, A., Lins, K. V., Roth, L., Towner, M., & Wagner, H. F. (2018). Entrenched Insiders and Corporate Sustainability (ESG): How Much Does the "G" Matter for "E" and "S" Performance Around the World?.
37 Kraakman, R., & Hansmann, H. (2017). The end of history for corporate law. In Corporate Governance (pp. 49-78). Gower.
38 Chapter 2F - Members' Rights and Remedies and Chapter 2G – Corporations Act 2001 (Cth)

In most jurisdictions of the world shareholders, especially institutional shareholders, vote at general meetings of the companies in which they hold stock. The act of voting has coined the term shareholder 'activism' [39]to describe the act of voting; shareholder voting is a disruptor of potential poor corporate governance by a company[40] [41] [42]. Institutional shareholders rely on ESG reporting to inform their voting on resolutions on agenda items at shareholder general meetings. The use of voting by shareholders to engage in activism is considered by researchers as vital to good corporate governance of companies globally[43]. In the U.S. it is compulsory for institutional investors to vote on all company resolutions, this by extension also occurs on their stock holdings of non – US companies internationally, significantly including their Australian stockholdings[44].

Voting by shareholders, especially institutional shareholders is an exercise of good corporate governance in companies around the world which is supported by national laws and regulations that allow for meaningful votes to be cast[45]. Shareholders vote on the resolutions of the general meeting's agenda which includes electing or re-electing directors and other significant items that impact good governance. As such Institutional shareholders votes have governance-related outcomes in influencing better corporate governance informed by ESG reporting [46] [47]

In any jurisdiction weak shareholder protection laws and enforcement combined with low levels of corporate disclosure result in poor corporate governance whereas strong shareholder protection laws and enforcement together with high levels of corporate disclosure ensures both better corporate governance and company performance for the benefit of shareholders and in terms of ESG and responsible investment, better outcomes for the local and global community.[48]

ESG reporting informing shareholder voting

Institutional investors or shareholders register to vote by post however this is now increasingly an electronic facility, and a growing trend globally, which given the early cut-offs for electronic voting and the significant percentage of Institutional investors or shareholders ownership of stock in companies makes the holding of the traditional 'in-person' general meetings redundant as discussed by Corporations and Markets Advisory Committee (CAMAC) in their 2012 paper of matters concerning the future of

39 Peter Iliev, Karl V. Lins, Darius P. Miller, Lukas Roth, 2015, 'Shareholder Voting and Corporate Governance Around the World', Oxford University Press on behalf of The Society for Financial Studies. doi:10.1093/rfs/hhv008
40 https://www.smh.com.au/business/directors-in-crosshairs-as-agm-season-begins-20140926-10mkr9.html
41 https://www.afr.com/business/asx-director-peter-warne-suffers-high-no-vote-20140922-jftsc
42 https://www.smh.com.au/business/adviser-urges-investors-to-shun-21st-century-fox-delisting-move-20140304-3457j.html
43 Peter Iliev, Karl V. Lins, Darius P. Miller, Lukas Roth, 2015, 'Shareholder Voting and Corporate Governance Around the World', Oxford University Press on behalf of The Society for Financial Studies; doi:10.1093/rfs/hhv008
44 Advisers warn of surge in activism , June 2014, Australian Financial Review
45 Peter Iliev, Karl V. Lins, Darius P. Miller, Lukas Roth, 2015, 'Shareholder Voting and Corporate Governance Around the World', Oxford University Press on behalf of The Society for Financial Studies; doi:10.1093/rfs/hhv008
46 Behind the ESG boom - Australian Institute of Company Directors: Mar 23, 2018 -Was the focus on sustainability part of the broader CSR movement? https://aicd.companydirectors.com.au/advocacy/governance.../behind-the-esg-boom
47 http://www.companydirectors.com.au/director-resource-centre/publications/company-director-magazine/2015-back-editions/february/opinion-global-headwinds
48 Peter Iliev, Karl V. Lins, Darius P. Miller, Lukas Roth, "Shareholder Voting and Corporate Governance Around the World" 2015. Published by Oxford University Press on behalf of The Society for Financial Studies; doi:10.1093/rfs/hhv008

the Annual General Meeting of shareholders. [49].

Institutional investors or shareholders may vote 'for' or 'against' or abstain on the resolution on the meeting agenda. The 'against' vote on the agenda item by Institutional investors or shareholders, or abstaining from voting, may not directly relate to the substance of the item but may be a means for Institutional shareholders to warn the company of their concerns and influence better corporate governance[50]. Institutional shareholders votes are determined by ESG reporting and across the world this research is predominantly provided by two firms: Institutional Shareholder Services (ISS) and Glass Lewis, colloquially known as proxy advisers, who provide ESG data reports to Institutional shareholders on all listed companies across the globe in order for Institutional shareholders to vote at all shareholder general meetings.[51]

ESG reporting occurs by the company in their Sustainability Report and their Governance Statement and in Australia through their operating and financial review (OFR).[52] In Australia Company directors must provide better financial reporting about the key drivers of a business, including its strategy and future prospects and the key material business risks to achieving that strategy and future prospects. Australian Securities and Investments Commission's Regulatory Guide 247 gives guidance to listed entities on how to prepare the OFR section of the annual report in compliance with the requirements of section 299A(1)(a)-(c) of the Corporations Act 2001. A key element of the ASIC's interpretation of the Act is its expansion of the concept of "prospects for future financial years" to include "material business risks" and this is informed by ESG related issues related to the company such as mining companies creating environmental risks in their operations or manufacturing companies creating social impact risks in their operations and supply chains.

In Australia shareholder voting and in particular institutional shareholder voting is not compulsory unless that institution is a member of the Financial Services Council of Australia (FSC). The FSC has various standards which its members must adhere to; the relevant standard in this case is Standard 13. The main purposes of Standard 13 Voting Policy, Voting Record and Disclosure are:

(a) in relation to Australian investments, to require the formulation of an Operator's[read institutional investor] voting policy (including proxy voting) – [this relates to voting through the electronic platforms of ISS the 'proxy advisers'] for each Scheme it operates;

(b) whether or not an Operator engages the services of a voting or proxy consultant [read 'proxy advisers']in exercising its voting rights; and

(c) to require disclosure of the above matters and details of the exercise of such

[49] http://www.camac.gov.au/camac/camac.nsf/byheadline/pdfdiscussion+papers/$file/agm.pdf
50 Simon Evans Vote of no confidence: Proxy advisers come under fire Australian Financial Review, December 2013
51 Patrick Durkin ASIC reins in proxy firms ahead of lively AGM season, Australian Financial Review, September 2017
52 Dr Ulysses Chioatto, 2014, 'L'enfant terrible: the many challenges of adopting the RG 247 regulatory guide', Company Director Magazine, Australian Institute of Company Directors.

voting rights by the Operator (on an "entity and resolution level" basis) in respect of each financial year for each Scheme it operates ("Scheme" is defined in FSC Guidance Note 5 Industry Terms and Definitions, and includes REs of registered schemes and RSE licensees of superannuation funds).

Subject to the exceptions mentioned below, Standard 13 applies to FSC members who are Operators of a Scheme and in that capacity have the ability to exercise voting rights in relation to investments and assets of a Scheme they operate, to the extent to which those assets or investments are listed on a financial market operated by an entity holding an Australian market licence issued under Part 7.2 of Chapter 7 of the Corporations Act 2001. The Standard applies in respect of Australian-listed investments only. An Operator is free to the extent it thinks appropriate to extend and apply the requirements of this Standard to any other investments of the relevant Scheme (including ex-Australian investments).[53]

In the UK as in the US and Europe there is a longer history to institutional shareholder active voting at general meetings of shareholders to influence corporate governance, that is mandatory, and as such sometimes questionable as to its genuine impact on better corporate governance. In the cases of the UK, US and Europe institutional shareholder voting is informed by ESG issues as researched predominantly by the two global firms ISS and Glass Lewis. Voting by US, UK and European investors has a direct impact on Australian corporate governance despite out own unique corporate governance Principles and Recommendations[54].

In the UK the peak body representing institutional investors is the National association of Pension Funds (NAPF)[55]. NAPF conducted a survey in 2014[56], of their members (institutional shareholders) voting on the stocks they held internationally and found that voting rights are consistently being exercised within the UK and that pension schemes are also increasing their active voting in their investments outside the UK into overseas markets.

[53] https://www.fsc.org.au/resources/standards/
54 ASX Corporate Governance Council Principles and Recommendation 3rd Edition
55 NAPF represents over 1,300 pension schemes that provide pensions for over 17 million people with £900 billion of assets.
56 NAPF Engagement Survey 2014: Pension Fund's Engagement with Companies

UK pension funds vote on their Australian companies' shareholdings based on ESG reporting and issues that strongly impact and change Australian corporate behaviour in terms of social impact, environmental concerns and in many ways import UK corporate governance standards. If we look back to the Cadbury Report (1992) it encouraged institutional investors in "the way in which institutional investors use their power (the weight of their votes) is of fundamental importance"; the Cadbury Report is extensively cited in Australia and its principles have found their way into the primary standard source of corporate governance in Australia: the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations[57]

In Europe institutional investors actively vote their shares based on ESG issues based on the EU Shareholder Rights Directive (2014). The directive also requires institutional investors to disclose how they cast their votes in general meetings of the companies concerned and an explanation for their voting behaviour. This voting disclosure and rationale based on ESG issues is an extremely powerful influencer of corporate behavior. The background the EU Directive can be traced back to 2002 and the EU High-Level Group of Company Law Experts; the 2006 Directive on Shareholder Rights; the 2007a that was enacted into each EU members States laws and the external study commissioned by the European Commission and carried out by Institutional Shareholder Services (Europe) into "proportionality" i.e. the relationship between capital and control or 'one share one vote'. Also contributing to the 2014 directive was the 2007 OECD paper 'Lack of Proportionality Between Ownership and Control: Overview and Issues for Discussion'.

The growth in sustainability reports

The Australian Council of Superannuation Investors (ACSI)[58], report of July 2017: Corporate Sustainability Reporting in Australia[59]– found corporate sustainability reporting (including economic, environmental, social and governance risks) is improving, but significant gaps remain including in relation to climate-related disclosures by ASX200. The Report found that eighty-five cents in every dollar invested in the ASX200 flows to companies that report to a high standard. The report also found that high standards of sustainability disclosure are increasing compared to 2008, with over 50% of the ASX200 now reporting to a "Leading" or "Detailed" level (compared to 19.5% in 2008).

The report based on a review of 2016 corporate ESG disclosures and found that

57 In the UK there has been a shift from the Cadbury Report (1992) norms and rules to the UK Corporate Governance Code (2014); the Cadbury Report (1992) provided us with the definition of corporate governance as the "system by which companies are directed and controlled", and voluntary adoption of governance best practices and the "comply or explain" principle to be expressed as "if not why not" in Australia. .

58 ACSI has 38 members who are asset owners and institutional investors, collectively, they manage over $2.2 trillion in assets and own on average 10% of every ASX200 company. It was established in 2001; ACSI provides advice on environmental, social and governance (ESG) issues to their members. ACSI members believe that ESG risks and opportunities have a material impact on investment outcomes and that they have a responsibility to act to enhance the long-term value of the savings entrusted to them. ACSI members seek measurable and permanent improvements in the ESG practices and performance of the companies they invest in.

59 https://www.acsi.org.au/images/stories/ACSIDocuments/generalresearchpublic/2017-Sustainability-Report-FINAL.pdf July 2017

92% of ASX200 companies see the value in sustainability disclosure and reporting. An example of the corporate reporting found in the Report is that more than half of the ASX200 (58%) reported greenhouse gas emissions, and 44% had a policy statement or other statement acknowledging climate change as a risk.

Corporate governance statements:

In Australia ASX listed companies issue Corporate Governance Statements (the Statement) that include reporting on their approaches to ESG issues and sustainability. The Statement reports on their corporate governance framework and addresses the governance standards adopted: ASX Corporate Governance Council's Recommendations. The Statement is approved by the Board of Directors and also sets out the key structural elements of their corporate governance framework.

The Australian ASX Corporate Governance Council Principles & Recommendations (3rd Edition) published in 2014 include the Recommendation 7.4 explicitly requiring that: a listed entity should disclose whether it has any material exposure to economic, environmental and social sustainability risks and, if it does, how it manages or intends to manage those risks. This is clearly in context with global reporting trends when the following international ESG indicators are considered include:

- The Global Reporting Initiative (GRI) in 2013 with over 400 indicators on corporate sustainability performance
- The International Integrated Reporting Council (IIRC) has issued its <IR> Framework, with continued efforts to harmonise this framework with traditional financial reporting, accounting standards
- The Sustainable Stock Exchanges Initiative (SSE), co-convened by the UN-supported Principles for Responsible Investment
- The United Nations Conference on Trade and Development
- The United Nations Environment Programme Finance Initiative
- The UN Global Compact

In the United States, the Sustainability Accounting Standards Board (SASB) has issued standards for 45 industries in 6 sectors. In 2016, standards for more than 80 industries in 10 sectors were issued.

ESG reporting by companies against the various standards in their Corporate Governance Statements are commonly used as investment benchmarks by institutional investors and engender ever greater disclosure expectations of institutional investors. Listed companies are eager to meet investor expectations.

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An example of a Corporate Governance Statement is that of Bendigo Bank which includes how they have addressed ESG issues[60] in their 20 page Statement, many Statements run to over 100 pages. Further examples of reporting are available, in 2015 the two peak organisations, noted above, ACSI and FSC, that represent institutional investors in Australia issued a report as a guide to listed companies to provide better reporting to their institutional investors: ESG "Reporting Guide for Australian Companies"[61] (the ESG Report). The ACSI and FSC ESG Report highlighted a number of companies as exemplary ESG reporters:

Principle 3: Acting ethically and responsibly vs instilling a desired culture

The significant redrafting of principle 3 and the addition the new Recommendations (3.1; 3.3 and 3.4) it is submitted go to reinforcing the practical application of ESG by institutional investors globally including in their Australian portfolio of stocks as highlighted above.

In practical terms proxy advisers look to these matters each AGM season.

The two global proxy advisers have a policy on governance failures and will, under various circumstances, recommend a vote against members of the board for material failures of governance, stewardship, risk oversight, or fiduciary responsibilities.

Changes to existing Recommendations

The proposed changes in terms of relationships to referred to in the Box 2.3 i.e. from "family to close ties" will be very problematic. In terms of other director independence criteria in determining whether a director should be considered "independent" may assist to clarify service on the board for more than 9 years[62]. This recommendation might be regarded as somewhat controversial given that since the Second Edition, the guidelines have not been prescriptive about length of service being a matter impairing independence, despite earlier moves in other jurisdictions[63]. A length of service criterion was deliberately omitted when the Second Edition was adopted.

Consistency with other jurisdictions is a compelling reason for alignment[64].

60 https://www.bendigoadelaide.com.au/public/corporate_governance/pdf/Corporate-Governance-Statement.pdf
61 https://www.asx.com.au/documents/asx-compliance/acsi-fsc-esg-reporting-guide-final-2015.pdf

62 "Zombie Boards: Board Tenure and Firm Performance". Paper presented at the American Accounting Association Anaheim, CA August 3 to 7, 2013. Huang, Sterling." Available at SSRN 2302917 (2013).

63 Ryan Jr, Harley E., and Roy A. Wiggins III. "Who is in whose pocket? Director compensation, board independence, and barriers to effective monitoring." Journal of Financial Economics 73.3 (2004): 497-524.

64 While a more prescriptive approach was rejected, the Guidelines were developed against the background ofdevelopments in the US, the release of the Higgs and Smith Reports in the UK and similar work in other countries, as well as updated standards issued by many of the member bodies of the ASX CGC and consideration of information about the various corporate collapses which generated concentrated public attention on corporate governance issues at the time of the first edition.

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Risk Management, ESG and the new Recommendations

Further to Principle 7[65] of the ASXGCP&R 3rd edition the board and the senior management of some Australian listed companies have a statutory duty to develop, implement, oversee and report on an effective system of risk management[66]. As discussed further in this section, those issuers regulated by ASIC and APRA in the financial services sector must comply with mandatory risk management oversight (see Appendix A).

Where to from here?

Overall the proposed changes in ASXGCP&R 4 go some way to better alignment to ESG responsible and ethical investing practices which have a significant impact on entities improving their social licence to operate and their corporate values and culture.

When reporting, issuers should bear in mind that investors and consumers are increasingly rewarding good corporate environmental, social and sustainable practices. Ultimately, the level of detail for any environment or social sustainability disclosure is not prescribed therefore the decision currently resides with the individual company.

It will be interesting to see whether all the proposed changes if implemented, combined with the changing international regulatory environment, will lead to a change in market practice and more detailed environment and social sustainability reporting by a greater cross-section of issuers.

[65] Earlier Changes to Principle 7: Recognise and Manage Risk: the 2003 version of the Principles was updated in 2007 reducing the number of principles from ten to eight and the number of recommendations from twenty-eight to twenty-six to remove regulatory overlap with the Corporations Act (2001) and the accounting standards. The board and management's responsibilities for risk oversight, management and disclosure were more clearly defined in the second edition, the Guidelines (2007). A key change was the expansion of the scope of Principle 7: Recognise and Manage Risk to reflect the heightened concern and increasing expectations of stakeholders with regard to risk management (ASX CGC, 2008).

66 Section 912A Corporations Act 2001 (Cth)

Appendix A: Background to Risk management

Risk management is a recognised business discipline with a broad supporting infrastructure in academe and professional practice. Development of a sound framework of risk oversight, risk management and internal control is fundamental to good corporate governance (ASX CGC, 2008; ASX Markets Supervision, 2009). The board and the senior management of Australian listed companies have a statutory duty to develop, implement, oversee and report on an effective system of risk management (structures, policies, and procedures and culture) to identify, assess, treat and monitor risk to support achievement of the organisation' s objectives. This is articulated in the ASX Guidelines which are given legal authority by the Corporations Act 2001 (Cth). The services required to support a company's risk management activities can be conducted in house by employees of the company, outsourced to professionals such as accounting practices or other professional consultants or by a combination of internal and external sources.

Formal recognition of risk management can be attributed to a number of factors including major financial and business scandals in the 1980's and 1990's in the U.K, for example Mirror Group, Barings Bank, Polly Peck, Maxwell Corporation (Arena et al., 2010). The first few years of this century provided a further series of high profile corporate collapses internationally (for example Enron, HIH and OneTel), events which could be partly linked to a failure to effectively manage risk (Francis and Armstrong, 2003). More recently we have seen heightened concern and focus on risk management with the advent of the current global financial crisis in 2007 (KPMG, 2010). The Organisation for Economic Co-operation and Development concluded the global financial crisis could be partly attributed to failures and weaknesses in corporate governance arrangements including lack of risk management (Kirkpatrick, 2009). Mikes (2009) observes Chief Executive Officers (CEO) are indicating one of the most importance lessons flowing from the global financial crisis is to make risk management a strategic imperative.

Internationally, regulators have made timely responses to the aforementioned events and enacted legislation and guidelines which have significantly expanded public policy in the corporate governance and risk management arena (Beasley, Clune, and Herrnanson, 2005). The Sarbanes-Oxley Act (SOX, 2002) in the United States (U.S.) and the Combined Code on Corporate Governance (Financial Reporting Council, 2003, 2008) in the U.K. contain key elements requiring public companies to incorporate effective systems of risk oversight.