

3 May 2024

**Submission to the ASX CGC regarding the Consultation Draft for a 5<sup>th</sup> Edition of the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations.**

Thank you for this opportunity to provide a submission to the Council on the proposed 5<sup>th</sup> edition of the Corporate Governance Principles and Recommendations.

We are two academics with a strong interest in corporate governance and responsible business.

**Associate Professor Alice Klettner, UTS Business School** is an expert in corporate governance regulation and sustainability, interested in how soft law instruments such as corporate governance codes change behaviour and facilitate the integration of environmental and social issues into corporate decision-making. She has worked with industry bodies such as the Australian Council of Superannuation Investors and the Chartered Governance Institute to explore the experiences of governance practitioners. Prior to her career in academia, she was a solicitor practicing at Freshfields Bruckhaus Deringer in London and then at a boutique Sydney firm. She has published a book exploring the effects of corporate governance codes: *Corporate Governance Regulation: The changing roles and responsibilities of boards of directors*, Routledge 2017 as well as academic articles published in journals such as the *Australian Journal of Corporate Law*, the *Journal of Business Ethics* and the *British Journal of Management*.

**Associate Professor Martijn Boersma, University of Sydney Business School** has expert knowledge about the intersection of business and society. His work covers several issues relating to the environmental and social responsibilities of business, with a specific focus on modern slavery, business and human rights, and supply chains. Martijn has engaged in research consultancies for several large organisations, including UNICEF and the United Nations Development Programme. For the latter he co-developed and delivered a blended-learning curriculum on business and human rights. His work has been published in high quality presses and journals, and Martijn makes regular contributions to ongoing debates in the media about the role of business in society. Before entering academia, he worked for several departments at the head office of Greenpeace in Amsterdam, and as a researcher in the trade union movement, which gives him intimate knowledge of the environmental and social responsibilities of business.

## **INTRODUCTION**

Environmental and social, issues have become critical in corporate governance. Inadequate governance of these issues can lead to a range of ethical transgressions, such as human rights abuses, adverse effects on local communities, workers' rights violations, mistreatment of customers, and negative impacts on the environment. We appreciate the Consultation Draft's increased emphasis on stakeholder relationships. However, we are concerned that they do not adequately address the effective governance of human rights risks. It is universally recognised that all businesses, regardless of where they operate, have a duty to respect human rights.<sup>1</sup> This responsibility, along with the management of human rights risks, is detailed in the UN Guiding Principles on Business and Human Rights (UNGPs), the foremost global standard for this issue. Failure

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<sup>1</sup> United Nations Human Rights Office of the High Commissioner. (2011). Guiding Principles on Business and Human Rights—Implementing the United Nations “Protect, Respect and Remedy” Framework. United Nations. [http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR\\_EN.pdf](http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf)

to respect human rights and other non-financial risks poses both short- and long-term material threats to businesses.

We wish to comment in relation to Questions 2, 3, 4, 5, 9, 10, 13 and 19 where, together or individually, we have conducted relevant research that could inform the Council's decision-making.

## **FEEDBACK ON SELECT QUESTIONS**

### **Question 2: Disclosure of whistleblower policy**

We believe Recommendation 3.3 should not be deleted and should remain in the 5<sup>th</sup> edition to encourage full transparency (over and above the legal requirement to disclose the policy to officers and employees). This would enable stakeholders such as investors and independent researchers to assess corporate commitment to whistleblowing. Public disclosure of this kind of information is important in facilitating the stewardship role of investors.<sup>2</sup>

### **Question 3: Board skills**

Human rights risk management requires specific expertise compared to environmental risk management. However, disclosures of Board skillsets in ASX reports often lump these areas together under categories like 'Sustainability'. This practice can obscure whether board members have expertise in environmental issues, human rights, or both. This lack of clarity can diminish stakeholders' confidence in the board's ability to effectively oversee human rights risks. We suggest that human rights and environmental skills be evaluated and reported on separately.

### **Question 4 Objective for board gender diversity**

We support the proposal to raise the ASX300 measurable objective to 40% to maintain progress in pursuing gender diversity. Our past research shows the importance of measurable targets in promoting cultural and strategic change at the heart of the corporation.<sup>3</sup> Now that the target of 30% has been achieved, it is essential to move towards a recommendation of gender parity.

### **Question 5 Disclosure of other relevant diversity characteristics**

On the same basis as above, we support the disclosure of other relevant diversity characteristics. This will raise awareness of other factors such as ethnicity and age.

### **Questions 9 and 10 Stakeholder relationships**

In our opinion, the changes to Principle 3 and the new Recommendation 3.3 are conservative, taking the ASX Principles no further than the agreed position almost 18 years ago when both CAMAC and a Parliamentary Joint Committee explored corporate responsibility and whether to alter directors' duties in the Corporations Act 2001.<sup>4</sup> The recommendation was that stakeholder interests could and should be taken into account by the board of directors. In this sense, the addition of Recommendation 3.3 is uncontroversial and should proceed.

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<sup>2</sup> Klettner, A. (2021) Stewardship Codes and the Role of Institutional Investors in Corporate Governance: An International Comparison and Typology, *British Journal of Management*.

<sup>3</sup> Klettner, A., Clarke, T. and Boersma, M. (2016) Strategic and Regulatory Approaches to Increasing Women in Leadership: Multilevel Targets and Mandatory Quotas as Levers for Cultural Change, *Journal of Business Ethics* 133, 395-419.

<sup>4</sup> CAMAC (Corporations and Markets Advisory Committee) 2006, *The Social Responsibility of Corporations*, Australia Government, December 2006; Parliamentary Joint Committee on Corporations and Financial Services, 2006, *Corporate Responsibility: Managing risk and creating value*, June 2006.

Associate Professor Alice Klettner, in Chapter 7 of her book, *Corporate Governance Regulation*, compares corporate governance code provisions across 13 jurisdictions in terms of their coverage of corporate social responsibility. The research (see Table 7.1 attached to this submission) shows that many jurisdictions had already moved to this kind of recommendation almost 10 years ago. Bearing this in mind, the Council may wish to extend this recommendation to keep it up-to-date with current practice by recommending, not only reporting to the board, but reporting publicly on stakeholder engagement (which is already common practice in sustainability reporting). At a minimum, the listed entity should also disclose the stakeholder engagement processes (see the amended wording for Recommendation 3.3 below:

A listed entity should have regard to the interests of the entity's key stakeholders including having **and disclosing** processes for the entity to **meaningfully** engage with them and to report material issues to the board.

We also suggest inclusion of the term 'meaningful' with the aim of preventing merely superficial stakeholder engagement. The OECD Guidelines stipulate 'meaningful engagement' with stakeholders as a component of due diligence in assessing a business's responsible conduct risks.<sup>5</sup> According to the OECD, meaningful engagement involves ongoing, two-way interactions that are conducted in good faith and are responsive to stakeholder views. Similarly, the UNGPs anticipate that an entity will conduct 'meaningful consultation' with potentially impacted groups and other relevant stakeholders, proportionate to the business's size and scope, as part of its human rights due diligence.<sup>6</sup> This process should consider vulnerable or marginalised groups at a greater risk.

### **Question 13: Reporting of material risks**

The proposed changes to Recommendation 7.4 and its updated Commentary imply that not all entities may need to report on environmental and social risks. Investors and communities expect increased transparency regarding environmental and social risks. It is highly unlikely that any ASX entity will not be exposed to any material human rights or environmental risks. The updated guidelines appear to de-emphasise these risks, potentially encouraging their non-disclosure. Moreover, as specified in the UNGPs, managing human rights risks involves identifying and addressing impacts on people, not solely on business. Consequently, human rights risks (i.e. social risks) should not be confined to stringent financial materiality assessments and should be reported by all entities.

### **Question 19 – Other proposed changes**

#### **Additional feedback on Principle 8**

We would like to see an amendment to **Principle 8** to provide more guidance on linking remuneration policy to long-term sustainable value creation. This would help connect Principle 8 to the commentary around Recommendation 3.3 on 'designing remuneration structures which drive appropriate behaviour' (page 28 of consultation draft). Principle 8 mentions long-term sustainable value creation in the introductory wording but does not go on to suggest *how* companies might

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<sup>5</sup> OECD. (2023). OECD Guidelines for Multinational Enterprises on Responsible Business Conduct. <https://www.oecd-ilibrary.org/content/publication/81f92357-en>

<sup>6</sup> United Nations Human Rights Office of the High Commissioner. (2011). Guiding Principles on Business and Human Rights—Implementing the United Nations “Protect, Respect and Remedy” Framework. United Nations. [http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR\\_EN.pdf](http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf)

achieve this. Our research finds that it is important that executive KPIs are linked to suitable non-financial measures that support the listed entity's social and environmental objectives.<sup>7</sup>

We would like to suggest an **additional bullet point in the Commentary to Recommendation 8.1** (page 49 of consultation draft). When setting the level and composition of remuneration a listed entity needs to balance:

- **the need to incentivise long-term sustainable value creation by using both financial and non-financial performance indicators;**

### **Additional feedback on Principle 3**

Recommendation 3.2 states that "a listed entity should instil and continually reinforce a culture across the organisation of acting lawfully, ethically, and responsibly". We support this recommendation. However, as Professor Paul Redmond highlights in his 2023 journal article, "The ASX Corporate Governance Principles and Recommendations and the Idea of Corporate Responsibility," the term 'responsibly' remains vaguely defined. We endorse Professor Redmond's suggestion that the definition of 'responsibly' should be informed by established, authoritative international standards on responsible business conduct, specifically the UNGPs and OECD Guidelines for Multinational Enterprises. We recommend that the proposed Commentary to Recommendation 3.2 be updated to reflect these insights, clearly defining 'responsible' by reference to these international standards.

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<sup>7</sup> Klettner, A., Clarke, T. and Boersma, M. (2014) The Governance of Corporate Sustainability: Empirical Insights in the Development, Leadership and Implementation of Responsible Business Strategy, *Journal of Business Ethics*, 122, 145-165.

**TABLE 7.1** Corporate-governance codes and CSR

<p>Australian Corporate Governance Principles and Recommendations (ASX Corporate Governance Council 2014)</p>	<p>Principle 3 Act ethically and responsibly          Recommendation 3.1 A listed entity should:          (a) have a code of conduct for its directors, senior executives and employees and          (b) disclose that code or a summary of it.          Commentary 'Acting ethically and responsibly goes well beyond mere compliance with legal obligations and involves acting with honesty, integrity and in a manner that is consistent with the reasonable expectations of investors and the broader community'.          Principle 7 Risk management          Recommendation 7.4 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.</p>
<p>Denmark Recommendations on Corporate Governance (Committee on Corporate Governance 2014)</p>	<p>The Danish code begins in Principle 1 with a statement of stakeholder inclusiveness:          'The company's investors, employees and other stakeholders have a joint interest in stimulating the Company's growth, and in the company always being in a position to adapt to changing demands, thus allowing the company to continue to be competitive and create value. Therefore, it is essential to establish a positive interaction not merely between management and investors, but also in relation to other stakeholders'.          Yet Principle 2 on tasks and responsibilities of the board of directors appears to prioritise shareholders:          'It is incumbent upon the board of directors to carefully protect the interests of the shareholders with due consideration for the other stakeholders'.          Principle 2.2 on Corporate Social Responsibility recommends simply that the board adopt policies on CSR.</p>
<p>German Corporate Governance Code (Deutscher Corporate Governance Kodex 2015)</p>	<p>4.1.1 The Management Board is responsible for independently managing the enterprise in the interest of the enterprise, thus taking into account the interests of the shareholders, its employees and other stakeholders, with the objective of sustainable creation of value.          4.2.3 The compensation structure must be oriented toward sustainable growth of the enterprise.</p>

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Greece – Hellenic Corporate Governance Code for Listed Companies (Hellenic Corporate Governance Council 2013)

1. Role and responsibilities of the board

In discharging its role, the board should take into account the interests of key stakeholders such as employees, clients, creditors and the communities in which the company operates so long as this does not go against the company's interests.

The responsibilities of the board should include:

formulating, disseminating and implementing key values and principles of conduct governing the company's relations with its stakeholders.

Iceland Corporate Governance Guidelines 4<sup>th</sup> edition (Iceland Chamber of Commerce 2012)

2.10 Ethics and social responsibility

The board should, in consultation with the employees and others which the board sees fit, determine the values and ethical norms on which the company's operation is based. By doing so, the company will not only promote a healthier economy and improved relations with stakeholders, but also reinforce its operating basis with an increased appearance of reliability and credibility, an improved sense of risk, happier employees and, in the end, improved competitiveness.

Japan's Corporate Governance Code (JPX Tokyo Stock Exchange 2015)

Companies should fully recognise that their sustainable growth and the creation of mid- to long-term corporate value are brought about as a result of the provision of resources and contributions made by a range of stakeholders, including employees, customers, business partners, creditors and local communities. As such, companies should endeavour to appropriately cooperate with these stakeholders.

The board and the management should exercise their leadership in establishing a corporate culture where the rights and positions of stakeholders are respected and sound business ethics are ensured.

**Principle 2.1** Guided by their position concerning social responsibility, companies should undertake their businesses in order to create value for all stakeholders while increasing corporate value over the mid to long term. To this end, companies should draft and maintain business principles that will become the basis for such activities.

**Principle 2.3.1** With the recognition that dealing with sustainability issues is an important element of risk management, the board should take appropriate actions to this end. Given the increasing demand and interest with respect to sustainability issues in recent years, the board should consider addressing these matters positively and proactively.

<p>The Norwegian Code of Practice for Corporate Governance (Norwegian Corporate Governance Board 2014)</p>	<p>1. The board of directors should define the company's basic corporate values and formulate ethical guidelines and guidelines for corporate social responsibility in accordance with these values.          At the core of the concept of corporate social responsibility is the company's responsibility for the manner in which its activities affect people, society and the environment, and it typically addresses human rights, prevention of corruption, employee rights, health and safety and the working environment, and discrimination, as well as environmental issues.</p>
<p>Russian Code of Corporate Governance (Moscow Exchange and OECD 2014)</p>	<p>Corporate governance should be based on the principles of sustainable development of a company and increasing long-term returns on investments in its share capital.          291. The company should disclose the following information on its social and environmental responsibility:          1) the company's social and environmental policy;          2) a report on its sustainable development of company drawn up in accordance with internationally recognised standards; and          3) the results of a technical audit, an audit of quality control systems, and the results of certification of its quality management system in terms of its compliance with international standards.</p>
<p>Singapore Code of Corporate Governance (Monetary Authority of Singapore 2012)</p>	<p>1.1 The board's role is to:          (d) identify the key stakeholder groups and recognise that their perceptions affect the company's reputation;          (e) set the company's values and standards (including ethical standards), and ensure that obligations to shareholders and other stakeholders are understood and met; and          (f) consider sustainability issues, e.g. environmental and social factors, as part of its strategic formulation.</p>
<p>King Code of Governance for South Africa (Institute of Directors Southern Africa 2009)</p>	<p>The South African code was the first code to recommend integrated reporting and an 'inclusive stakeholder approach' to governance. It includes elements of CSR in every principle:          'The philosophy of the Report revolves around leadership, sustainability and corporate citizenship.'          'A key challenge for leadership is to make sustainability issues mainstream. Strategy, risk, performance and sustainability have become inseparable; hence the phrase 'integrated reporting' which is used throughout this Report.'          Principle 1 on Ethical leadership and corporate citizenship clearly places responsibility for CSR on the board of directors.          Principle 8 on governing stakeholder relationships provides guidance on identifying and engaging with stakeholder groups.</p>

(Continued)

Spanish Good Governance Code of Listed Companies (CNMV 2015)

Principle 24: The company should deploy an appropriate corporate social responsibility policy, as a non-delegable board power, and report transparently and in sufficient detail on its development, application and results

Environmental awareness and understanding, a sense of community, innovation capacity and a forward vision stand alongside the core purpose of value creation as mainstays of business activity.

Companies should accordingly take time to analyse how their business impacts on society and vice versa. In this way, taking as reference their own value chain, they can identify social issues that lend themselves to shared value creation.

Sri Lanka Code of Best Practice on Corporate Governance 2013 (Institute of Chartered Accountants and Securities and Exchange Commission 2013)

2013 edition introduced Principle G on sustainability reporting:

G.1.7 – Sustainable reporting and disclosure should be formalised as part of the company's reporting processes and take place on a regular basis.

- Sustainability reporting is a board responsibility, and it is designed to add value by providing a credible account of the company's economic, social and environmental impact.
- Sustainability reporting should link sustainable issues more closely to strategy.

Thailand The Principles of Good Corporate Governance for Listed Companies 2012 (SET 2012)

Section 3 Role of stakeholders

The board should set clear policies on fair treatment for each and every stakeholder. The rights of stakeholders that are established by law or through mutual agreements are to be respected. Any actions that can be considered in violation of stakeholders' legal rights should be prohibited. Any violation should be effectively redressed.

The board should provide a mechanism so that stakeholders can be involved in improving the company's performance, helping to ensure the firm's sustainability. In order for stakeholders to participate effectively, all relevant information should be disclosed to them.

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