

Elizabeth Johnstone, Chair
Corporate Governance Council
Australia Stock Exchange
20 Bridge Street
Sydney NSW 2000
Australia

06 May 2024

Dear Ms Johnstone,

Subject: 5th edition of the Corporate Governance Principles and Recommendations

The Monash Centre for Financial Studies (MCFS), Monash Business School, is pleased to provide comments in response to the Australia Stock Exchange (ASX) Corporate Governance Council (“the Council”) consultation questions on the 5th edition of its Corporate Governance Principles and Recommendations.

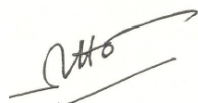
Based in Australia within Monash University's Monash Business School, MCFS conducts leading-edge research into issues of practical relevance to the Australian and global finance industries. Through its industry engagement programs, it also facilitates two-way exchanges of knowledge between academics and practitioners. The centre's evolving research agenda is broad but primarily focuses on issues relevant to the asset management industry, including environmental, social and governance (ESG) issues, superannuation, sustainable finance and technological disruption.

As an academic institution, our comments are based on insights obtained from our research and industry engagement with ASX-listed companies and global investors in ESG. Overall, we welcome the direction of the revisions proposed in the 5th edition, which will promote clearer board responsibility and accountability, a sound control environment, and better disclosure and transparency.

Our detailed responses to the consultation questions are set out in the Appendix.

Thank you once again for the opportunity to share our perspective. Should you have any questions or wish to discuss any of our comments further, please feel free to contact our Director of Research Impact, Nga Pham (nga.pham@monash.edu).

Yours sincerely,



Nga Pham

Senior Research Fellow
Director of Research Impact
Monash Centre for Financial Studies

RESPONSE TO CONSULTATION QUESTIONS

1. Do you support deletion of the following 4th Edition Recommendations, on the basis that there is significant regulation under Australian law?
 - a. Recommendation 3.4 (disclosure of anti-bribery and corruption policy)?
 - b. Recommendation 4.2 (CEO and CFO declaration for financial statements)?
 - c. Recommendation 6.4 (substantive security holder resolutions on a poll)?
 - d. Recommendation 6.5 (offering electronic communications to security holders)?
 - e. Recommendation 8.2 (separate disclosure of remuneration policies for non-executive directors, other directors and senior executives)?
 - f. Recommendation 8.3 (policy on hedging of equity-based remuneration)?

As there have been other significant regulations addressing these recommendations applicable to listed companies, we support the deletion of these recommendations.

2. In particular, the Council encourages feedback on the proposed deletion of Recommendation 3.3 (disclosure of whistleblower policy). Would you prefer to retain this Recommendation?

We recommend retaining this Recommendation as outlined in the 4th Edition, which specifies that companies are expected to disclose their whistleblower policy on their website or in their annual report. This not only meets legal requirements to make the policy accessible to officers and employees but also extends access to third-party whistleblowers such as former employees or suppliers, enhancing the reach and effectiveness of such policy.

We can use the modern slavery disclosure practice as an example to illustrate this point. In line with the Commonwealth Modern Slavery Act 2018 Guidance for Reporting Entities¹, it is crucial for entities to publicly communicate the availability and details of their grievance mechanisms and remediation processes, including whistle-blower policy and hotlines. These measures are essential for identifying and addressing modern slavery practices within the entity's operations and supply chains. The Guidance advises entities to consider developing ways to actively promote their grievance mechanism to workers in supply chains.

Given the growing emphasis on due diligence concerning human rights, environmental, social and labour practices and concerns in the supply chain, it is increasingly important for companies to make their whistleblower policies accessible on their website or in their annual report. This ensures that stakeholders, including those external to the company, are aware of and can easily access whistleblowing channels and the protections offered.

3. Recommendation 2.2: The Council already recommends disclosure of a board skills matrix or skills a board is looking for. Do you support disclosure of the following information about board skills?
 - a. Recommendation 2.2(a): current board skills and skills that the board is looking for?
 - b. Recommendation 2.2(b): the entity's process for assessing that the relevant skills and experience are held by its directors?

We welcome the inclusion of Recommendation 2.2(b) and related comments regarding the disclosure of the entity's process for assessing the relevant skills and experience of its directors. While the current comments emphasise the need to disclose how it is determined that a director possesses the requisite skills and experience, we believe it is equally critical to disclose the methods used to identify emerging skills and experiences required by the board. Additionally, it is important to outline the entity's strategy for addressing these evolving skills needs. As sustainability issues grow increasingly complex, it is essential for entities to keep pace with the evolving skills required for their boards to exercise their oversight of material sustainability risks and opportunities effectively.

¹ Commonwealth Modern Slavery Act 2018 Guidance for Reporting Entities, May 2023*

We, therefore, propose the following revision to Recommendation 2.2(b): “the entity’s process for identifying newly emerging skills and experiences needed by the board and assessing that the relevant skills and experience are held by its directors”, and adding further comments in the Commentary explaining the importance of having a process to identify new skills and the entity’s strategy for addressing these evolving skills needs.

4. Recommendation 2.3: Women hold approximately 35% of all S&P/ASX300 directorships. This exceeds the existing measurable objective of at least 30% of each gender for those boards. Do you support raising the S&P/ASX300 measurable objective to a gender balanced board?

We commend the achievement of 35% female representation in S&P/ASX300 directorships and support the goal of achieving a gender-balanced board. With women occupying 36.9% of leadership roles globally, as reported by the World Economic Forum, there is strong momentum within the business community to further enhance gender diversity. Indeed, it has been reported that the gender-balanced board has been achieved within certain segments of the S&P/ASX300. According to the study in 2023 by Watermark Search International and the Governance Institute of Australia, while the ASX 201 – 300 companies have 44% women representation on board, the ASX50 companies achieve 39%².

The Australian Council of Superannuation Investors (ACSI) Gender Diversity Policy³ reflects the expectations of the country’s largest investors for S&P/ASX300 companies to have at least 30 per cent of board positions filled by women, along with a clear timeline to reach a gender balance of 40:40:20 on their boards. Similarly, overseas, the Alliance for Board Diversity set a goal of 40% diversity on Fortune 500 boards. ACSI members’ expectations will lead to action by voting against companies that have made no progress in improving board gender diversity. Therefore, it is in the best interest of S&P/ASX300 companies to embrace the value of gender diversity and actively work towards achieving a gender-balanced board.

5. Recommendation 2.3(c): The Council already recommends disclosure of a board’s approach and progress on gender diversity. Do you support the proposed disclosure of any other relevant diversity characteristics (in addition to gender) which are being considered for the board’s membership?

We highly support the proposed disclosure of any other relevant diversity characteristics in addition to gender being considered for board membership. Ethnic diversity on boards is an area that requires significant improvement. Although Australia has become increasingly multicultural in recent decades, board membership has not kept pace with the cultural diversity of the Australian population, particularly in terms of representing Indigenous and other ethnic groups. Other factors, apart from gender and ethnicity, that could contribute to the diversity of thinking and perspective include age, physical ability and neurodiversity⁴.

Additionally, we suggest updating the language in the Commentary of this Recommendation, where it refers to the “diversity and inclusion policy” to ‘diversity, equity, and inclusion policy.’ The reasons for this change are further explained in our response to Consultation Question 6.

6. Recommendation 3.4(c): The Council already recommends disclosure of an entity’s diversity and inclusion policy and disclosure of certain gender metrics. Do you support the proposal to also recommend disclosure of the effectiveness of an entity’s diversity and inclusion practices?

² Board Diversity Index 2023 by Watermark Search International and the Governance Institute of Australia.

³ ACSI Gender Diversity Policy, 17 May, 2023, [https://acsi.org.au/policies/acsi-gender-diversity-voting-policy/#:~:text=In%20pursuit%20of%20these%20aims,%3A20\)%20on%20their%20boards.](https://acsi.org.au/policies/acsi-gender-diversity-voting-policy/#:~:text=In%20pursuit%20of%20these%20aims,%3A20)%20on%20their%20boards.)

⁴ <https://www.mckinsey.com/featured-insights/mckinsey-explainers/what-is-diversity-equity-and-inclusion>

While we support the proposal to recommend the disclosure of the effectiveness of an entity's diversity and inclusion (D&I) practices, we suggest replacing the term "diversity and inclusion" with "diversity, equity and inclusion" in the context of corporate policy and practices.

We welcome the additions to the Commentary of this Recommendation, which now defines the diversity and inclusion policy as "one or more policies designed to foster a diversity of backgrounds in a listed entity's board and broader workforce, equity (fairness) in treatment regardless of background and an inclusive environment in which those different backgrounds can participate and contribute to the organisation". This definition acknowledges equity as fundamental component of a D&I policy. Consequently, the term "diversity, equity and inclusion" (DEI) more accurately captures the essence and broader implications of the policy. It is also worth noting that the term DEI has become increasingly prevalent among companies when referring to such policies⁵. The International Corporate Governance Network (ICGN), representing institutional investors with more than USD 70 trillion value of assets under management, also refers to "Diversity, equity and inclusion" in the ICGN Global Governance Principle 3.1⁶.

We also recommend that the Council expand the commentary on measuring and reporting the "effectiveness" of an entity's diversity and inclusion practices. The current proposed Commentary seems to focus more on setting diversity objectives and measuring and reporting on the achievement of those objectives. Additional guidance on evaluating an entity's effectiveness in fostering equity and inclusion is necessary. Recent literature on DEI can provide some insights, such as the global study on 10,000 knowledge workers evaluating their companies' DEI practices, reported by the Harvard Business Review⁷. The study utilises a theoretical framework of the five stages of DEI maturity namely Aware, Compliant, Tactical, Integrated and Sustainable. Companies moving beyond the Compliant stage are those who can leverage DEI to meet other goals, i.e., the ultimate outcomes and impact of DEI. Such frameworks could provide valuable benchmarks for entities looking to assess and enhance their DEI policies and practices.

7. Recommendation 2.4: Do you support increasing the security holding reference included in Box 2.4 (factors relevant to assessing the independence of a director) from a substantial holder (5% or more) to a 10% holder (10% or more)?

We would not support the proposed increase from a substantial holder to a 10% holder (10% or more) in Box 2.4. Assessing a director's independence involves various factors, among which ownership often emerges as a key factor that can compromise their independence. While the ownership structure in most markets today has become more concentrated, as reported by the OECD (2023)⁸, Australia is among the three markets with the lowest ownership concentration, measured as the combined holdings of the three largest shareholders, together with Finland and Ireland. The OECD Capital Market Series dataset reports that for Australia, the largest shareholder, on average, owns less than 10%, and the three largest shareholders own less than 20%. On the other hand, in the United States, Canada and the United Kingdom, the average combined holding of the top three shareholders ranges between 33% and 36% of the company's equity capital. Given the dispersed nature of the ownership structure of Australian companies, we believe that the 5% remains a relevant and reasonable threshold for indicative independence.

In order to consider a revision to the current threshold, the Recommendation should also take into account the current definitions of independence being used by investors, as their interests are likely to be significantly impacted if board decisions are unduly influenced by a lack of independence. The International Finance Corporation (IFC), for example, defines an independent director as one who does not hold a material interest in the Company or its Affiliates, for which "material interest" shall mean a direct or indirect ownership of voting shares representing at least [two per cent (2%)] of the outstanding voting power or

⁵ <https://hbr.org/2022/11/the-five-stages-of-dei-maturity>

⁶ ICGN, *Global Governance Principles* (2021)

⁷ <https://hbr.org/2022/11/the-five-stages-of-dei-maturity>

⁸ OECD Corporate Governance Factbook, 2023

equity⁹. BlackRock's Proxy Voting Guidelines for Australian Securities (2023), in its assessment of director independence, specifies a threshold of not more than 5% or more of the company's voting securities or being an executive or other representative of a company that owns or controls more than 5% or more of the company's voting securities.

8. Recommendation 3.2(c): The Council already recommends that a listed entity should have a code of conduct and report material breaches of that code to its board or a board committee. Do you support the proposed disclosure (on a de-identified basis) of the outcomes of actions taken by the entity in response to material breaches of its code?

We fully support this Recommendation and particularly appreciate the proposed disclosure of the outcomes of actions taken by the entity in response to material breaches of its code, as well as the added commentary that highlights the role of the board in overseeing the corporate culture. The provided indicators of a healthy organisational culture and the inclusion of the entity's key stakeholders in these considerations in the commentary are highly commendable.

9. Principle 3: Do you support the proposed amendments to Principle 3 (acting lawfully, ethically and responsibly), to include references to an entity's stakeholders?

We fully support this Recommendation and are pleased to see a strong emphasis on considering stakeholders and their interests, both in this specific Recommendation and throughout the entire 5th Edition.

According to the OECD/G20¹⁰ (2023), corporate governance involves a set of relationships between a company's management, board, shareholders and stakeholders. The new edition of the OECD/G20 Corporate Governance Principles incorporates the considerations of "The Role of Stakeholders in Corporate Governance", previously included as Chapter IV in the earlier version of the Principles in the new Chapter on "Sustainability and Resilience". There is a strong focus of the new Principles on having a sound framework for corporate governance with respect to sustainability matters to help companies recognise and respond to the interests of shareholders and different stakeholders, as well as contribute to their own long-term success. We are pleased to see a similar spirit in the new edition of the ASX Principles and Recommendations.

10. Recommendation 3.3: Does this new Recommendation appropriately balance the interests of security holders, other key stakeholders, and the listed entity? "A listed entity should have regard to the interests of the entity's key stakeholders, including having processes for the entity to engage with them and to report material issues to the board."

We fully support this Recommendation and are pleased to see a strong emphasis on considering stakeholders and their interests, both in this specific Recommendation and throughout the entire 5th Edition. The added Commentary on the importance of stakeholder mapping and designing a stakeholder engagement program for the creation of long-term sustainable value for security holders further enhances the Recommendation's strength and relevance.

11. Recommendation 4.2: Do you support the proposed disclosure of processes for verification of all periodic corporate reports (including the extent to which a report has been the subject of assurance by an external assurance practitioner)?

⁹ IFC also mentioned that local law may specify a different relevant percentage, for example, in the United Kingdom, a shareholder is treated as having a material (disclosable) interest in a publicly listed company if it holds 3% of the shares; in the United States, the equivalent threshold is 5%. <https://www.ifc.org/content/dam/ifc/doc/2023/IFC-Indicative-Independent-Director-Definition-062719.pdf>.

¹⁰ OECD (2023), *G20/OECD Principles of Corporate Governance 2023*, OECD Publishing, Paris, <https://doi.org/10.1787/ed750b30-en>.

While we fully support the Recommendations under Principle 4, we believe that it is a missed opportunity not to emphasise the emerging challenges of corporate reporting, particularly regarding sustainability information. The importance of robust oversight of corporate reporting cannot be overstated. The new OECD/G20 Corporate Governance Principles (2023) highlights that sustainability and financial reporting should be interconnected and stress the need for consistency and comparability among corporate sustainability disclosures. This connection is crucial for ensuring transparency and accountability in corporate governance.

The OECD/G20 Corporate Governance Principles (2023)¹¹ recommends that phasing in of requirements should be considered for annual assurance attestations by an independent, competent and qualified attestation service provider in accordance with high-quality internationally recognised assurance standards in order to provide an external and objective assessment of a company's sustainability-related disclosure.

A study on 1,400 companies in 22 jurisdictions, including Australia, recently published by the International Federation of Accountants (IFAC) reports that 98% of companies reviewed reported some level of detail on sustainability, and 69% of companies that reported obtained assurance on at least some of their sustainability disclosures. 82% of assured reports had limited assurance. 58% of assured reports were signed by audit firms, suggesting a large number of reports signed by other service providers. Specifically on assurance of sustainability information, the scope of assurance engagements broadened with 59% of companies obtaining assurance on disclosure in greenhouse gas (GHG), other environmental, social and governance categories, and 60% of companies that obtained assurance over their emissions covered all Scope 1, Scope 2, and Scope 3 emissions. In Australia, approximately 70% of companies obtaining assurance over GHG emissions covered all three scopes. The report also finds that the mix of reporting standards used by companies remains fragmented.

Another significant change is the transition from voluntary to mandatory reporting and assurance requirements in some jurisdictions, led by those in Europe.

The evolving landscape of corporate reporting and the increasing reliance of investors, lenders and other stakeholders on corporate information for their decision-making have heightened scrutiny of corporate disclosure and increased the demand for external assurance.

The complexity of sustainability information, such as climate-related financial disclosure, poses significant challenges for companies, consultants, assurance and audit practitioners. This complexity underscores the importance of companies implementing stringent processes for selecting high-quality service providers to meet their reporting and assurance needs effectively.

In this context, we are pleased to note the clarified wording of Recommendation 4.1 that the board of a listed entity should oversee appropriate processes to verify the integrity of its periodic corporate reports, which enhances the focus on the board's responsibility.

Regarding Recommendation 4.2, we concur that the entity should disclose processes for verification of all periodic corporate reports (including detailing the extent to which a report has been the subject of assurance by an external assurance practitioner). As the global regulations and standards on sustainability reporting grow increasingly complex, companies might require professional assistance in preparing corporate reporting and obtaining external assurance to bolster credibility among users of corporate information. Companies need to be transparent about their own internal process for verification of corporate reports as well as the criteria and procedures to select external assurance practitioners. We suggest that the Council expand on the current Commentary to reflect the evolving landscape of corporate reporting and the significance of disclosing the details of selecting and engaging external assurance providers.

¹¹ The OECD/G20 Corporate Governance Principles (2023) VI.A.5.

12. Recommendation 4.3: Do you support the proposed disclosure of an entity’s auditor tenure, when the engagement was last comprehensively reviewed and the outcomes from that review?

We fully support this Recommendation as it serves to enhance the auditor’s independence and effectiveness.

13. Recommendation 7.4: The Council is seeking to enhance the quality of existing reporting of material risks to an entity’s business model and strategy, such as in the operating and financial review in its directors’ report. Do you support the proposal that the entity identify and disclose its material risks, rather than identifying specific risks for all entities to disclose against?

While we support this Recommendation, similar to our comment to Question 11, we believe that it is a missed opportunity not to emphasise the emerging challenges of corporate reporting, including reporting of material sustainability risks to an entity’s business model and strategy.

We concur that it is important that the entity identify and disclose its material risks, as it would not be practical to identify specific risks for all entities to disclose against. On that premise, we think that the Recommendation would benefit from more guidance in the Commentary on what constitutes “material” and the process for an entity to identify its material risks. The OECD/G20 Corporate Governance Principles (2023), for example, defines “material” through the lens of investors, “Material information can be defined as information whose omission or misstatement can reasonably be expected to influence an investor’s assessment of a company’s value. This would typically include the value, timing and certainty of a company’s future cash flows. Material information can also be defined as information that a reasonable investor would consider important in making an investment or voting decision.”¹² The OECD also recommends dialogue between a company, its shareholders and stakeholders to exchange views on sustainability matters as relevant to the company’s business strategy and its assessment of what matters ought to be considered material¹³.

In addition to the examples of cyber risk and climate change-related risk in the Commentary, we suggest including the risk of human rights violations and modern slavery practices in a company’s operations and supply chains to reflect Australian companies’ focus on combating modern slavery.

While the new OECD/G20 Principles have introduced a significant focus on sustainability and resilience, it appears that the 5th Edition has not sufficiently addressed the aspect of corporate resilience. This oversight could be a missed opportunity to align with global trends and enhance the robustness of governance frameworks in responding to dynamic challenges.

Consequently, we suggest that the Council consider in its Commentary for this Recommendation how corporate resilience could be enhanced if the entity could appropriately identify, manage and disclose its material sustainability risks.

14. Recommendation 8.2: This proposed Recommendation reflects and simplifies existing commentary in the 4th Edition. Do you support this proposed Recommendation that non-executive directors not receive performance-based remuneration or retirement benefits?

We fully support this Recommendation. Best practices for remunerating non-executive directors (NEDs) involve balancing fair compensation with their roles and responsibilities. Typically, NEDs receive a fixed fee to maintain their independence, avoiding performance-based incentives that could skew their objectivity. Additional fees can be allocated to chairpersons and committee members for their extra duties.

¹² The OECD/G20 Corporate Governance Principles (2023): Principles IV, Page 27.

¹³ The OECD/G20 Corporate Governance Principles (2023): VI.B

Performance-based bonuses, equity compensation and retirement benefits other than superannuation, while aligning NEDs' interests with the company's goals, can undermine their independence by incentivising short-term gains over long-term stability and ethical governance.

Excessive compensation can also lead to conflicts of interest, shifting a director's focus from the company's long-term value to personal re-election concerns. It is essential that an entity conduct regular reviews of director compensation against industry standards to ensure fair and effective compensation.

This Recommendation aligns with major global corporate governance codes and principles, including ICGN Global Corporate Governance Principles and the new OECD/G20 Principles.

15. Recommendation 8.3: Do you support the following proposed clawback Recommendations? a. Recommendation 8.3(a): remuneration structures which can clawback or otherwise limit remuneration outcomes for senior executive performance-based remuneration? b. Recommendation 8.3(b): disclosure of the use of those provisions (on a de-identified basis) during the reporting period?

We fully support this Recommendation. The implementation of malus and claw-back provisions is recognised as good practice. These provisions give a company the authority to withhold or reclaim compensation from executives in specific situations, such as managerial fraud or when financial restatements are necessary due to significant noncompliance with financial reporting requirements. This mechanism serves as a safeguard, ensuring that executive compensation aligns with the company's ethical standards and financial integrity.

16. Do you support the inclusion of the following new Recommendations for entities established outside Australia, on the basis that these Recommendations generally reflect expectations under Australian law?

- a. Recommendation 9.3 (CEO and CFO declaration for financial statements)?
- b. Recommendation 9.4 (substantive security holder resolutions on a poll)?
- c. Recommendation 9.5 (offering electronic communications to security holders)?
- d. Recommendation 9.7 (policy on hedging of equity-based remuneration)?

We fully support these Recommendations to ensure that entities established outside Australia are subject to the same governance requirements and standards as the Australian entities do, if they are to be listed on the Australian Securities Exchange.

17. Should any new or amended Recommendations in the Consultation Draft apply differently to externally managed entities, compared to the manner proposed in the application of the Recommendations to externally managed listed entities?

We do not have any comments on this question.

18. Do you support an effective date for the Fifth Edition of the first reporting period commencing on or after 1 July 2025?

We fully support this Recommendation.

19. Do you wish to provide any other comments on the content of the Consultation Draft, including any other changes you would propose?

We would like to provide additional comments on Recommendation 4.1(b), “If it does not have an audit committee, disclose that fact and the processes it employs that independently verify and safeguard the integrity of its periodic corporate reporting”. The current wording could be interpreted as permitting companies to operate without an audit committee, in contrast with the spirit of Recommendation 4.1(a).

We suggest that the Council remove Recommendation 4.1(b) as it is indeed not needed. If a company does not have an audit committee, it would have to provide an “if not, why not” explanation anyway under the “Comply or Explain” nature of the Principles. The explanation would detail the reasons why the entity chooses not to establish an audit committee and disclose any alternative governance practices to safeguard the integrity of its corporate reporting.

Removing Recommendation 4.1(b) would demonstrate the Council’s commitment to maintain a strong stance requiring all listed companies to establish an audit committee, considering its crucial role in upholding the quality and integrity of corporate reporting.