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Shazia Parviez
ICGN Company Secretary:
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By email: shazia.parviez@icgn.org

Dear Shazia

Draft Revised Corporate Risk Oversight Guidelines and Draft Revised Integrated Business Reporting Guidelines

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

Our members are all involved in governance, corporate administration and company secretarial within their organisations. They deal on a day-to-day basis with the Australian Securities Exchange (ASX), have primary responsibility for communicating with regulators such as the Australian Securities Investments Commission (ASIC) and have a thorough working knowledge of the operations of the markets, the needs of investors and the listing rules, as well as compliance with the corporations law. Our members also hold primary responsibility within listed companies for developing governance policies and supporting the board on all governance matters.

Governance Institute of Australia (Governance Institute) welcomes the opportunity to comment on the m Draft Revised Corporate Risk Oversight Guidelines (Draft CROC Guidelines) and Draft Revised Integrated Business Reporting Guidelines (Draft IBR Guidelines) and draws upon the experience of our members in providing our response.

General comments: prescriptive approach of guidance

We commend ICGN for expanding the focus in the Revised Draft Guidelines from board responsibilities to investor responsibilities. Building alignment between companies and their investors enables them to work together to help the company perform well over the long term and to counter short-term pressures in the market inimical to sustained long-term performance.

However, we wish to reiterate a point that we made when we commented on the *Draft ICGN Global Governance Principles* in 2014 concerning the multiplicity of governance guidelines in existence that all seek to apply their specific approach to governance and risk management. Governance guidelines are now issued by multiple parties, including intermediaries acting collectively on behalf of asset owners as well as individual asset owners, fund managers, proxy advisers and shareholder groups (including the ICGN). However, while there can be commonality in some areas between these multiple guidelines, they can conflict at times. The approach can also at times be prescriptive. This creates particular challenges and tensions for corporations and their governing bodies and those providing governance advice to them.

In Australia, the primary governance document is the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* (Principles and Recommendations). The key principle underpinning the Principles and Recommendations is the 'if not, why not' model. This model recognises that governance cannot be a 'one-size-fits-all' model and that if an entity considers a Recommendation is inappropriate to its particular circumstances, it has the flexibility not to adopt it — a flexibility tempered by the requirement to explain why. That is, this model provides for other approaches to governance than those set out in the Recommendations, subject to explanation. A similar approach is taken in the United Kingdom with the 'comply or explain' model.

The last decade has shown that the approach taken by the Council in the Principles and Recommendations is key to their success in being adopted by listed entities as the primary governance document. The Principles and Recommendations have played a vital role in improving corporate governance in Australian listed companies since the release of the first edition in 2003. Their history is one of practical statements on governance which have brought meaningful change to governance practice.

We recognise that an effort has been made in the Draft CROC Guidelines and Draft IBR Guidelines to clarify that listed entities have a degree of flexibility in how they apply the guidelines, given the existence of differing local approaches to governance. The Preamble in the Draft CROC Guidelines currently states that 'Users need to exercise their judgment when applying the guidelines to specific jurisdictions, companies and circumstances.' The Preamble in the Draft IBR Guidelines states that 'As global guidelines, they should be read with the understanding that the local rules and cultural norms may lead to different approaches to governance practices.'

However, both sets of Draft Guidelines are intended to be used by institutional investors who have holdings in corporations in any jurisdiction. Moreover, the Preamble in the Draft IBR guidelines specifically states that 'The ICGN Integrated Business Reporting Guidance is intended to be for general application globally, irrespective of national legislative frameworks or listing rules.'

This prescriptive approach undermines the key principle of good governance, which is that there is no 'one-size-fits-all' approach. It is also of concern that any guidance issued by ICGN should state that its approach should apply irrespective of national legislative frameworks or listing rules. Governance guidance should never seek to put listed entities in conflict with the legislation and listing rules governing them in their jurisdiction.

In Australia, for example, the corporate regulator, the Australian Securities and Investments Commission (ASIC) released Regulatory Guide 247 on the Operating and Financial Review (OFR) in 2013. The OFR deals with the commentary required to be given to investors in the directors' report under s299A of the *Corporations Act 2001* (the directors' report forms part of the annual report). The OFR provides the listed entity with the opportunity to disclose and discuss the risks facing the entity and the OFRs of listed entities are reviewed by ASIC. The regulator accepts that the OFR is performing the role of an integrated report in many respects, but the approach taken at law in Australia differs in part from that set out in the Draft IBR Guidelines.

Another example of how the prescriptive approach set out in the Draft Guidelines (particularly the Draft IBR Guidelines) is counter-productive is that there has been significant emphasis in Australia in the 3rd edition of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* on providing listed entities with the capacity to disclose information to investors on governance and risk management on websites and in other fora, rather than solely in the annual report. This aligns with our continuous disclosure regime —

simultaneous reporting of information that all shareholders can access in order to ensure their equitable treatment — and also with the regulatory push to make disclosures more investor-friendly and accessible. Determining in the Draft IBR Guidelines that all relevant non-financial disclosures to investors must be in the annual report is at odds with our regulatory regime.

We are of the view that the statements in the respective Preambles are insufficient to confirm that those using the Revised Guidelines to assess board oversight of risk management in and non-financial and financial reporting by listed entities will not 'mark down' those listed entities that have practices other than those set out in the Revised Draft Guidelines. We recommend that greater emphasis should be placed on the flexible application of these principles, to avoid any misunderstanding that they are prescriptive in nature.

Inclusion of questions to the board for shareholder engagement

The volume of questions intended for shareholder engagement in both Guidelines do not accord with the reality of shareholder engagement.

Firstly, the chair may meet with investors to discuss governance issues, which may include discussion of environmental and social issues. However, other directors do not meet with investors to discuss these matters, apart from the chair of the remuneration committee, who may meet to discuss remuneration issues.

Secondly, such meetings of chair and investors generally take place once or twice a year, and last for approximately one hour. In that period of time, only a few questions concerning governance and potentially environmental and social matters can be canvassed. It is simply not feasible for a meeting of chair and investors to canvass the volume of questions suggested, particularly the volume suggested in the Draft IBR Guidelines.

Finally, the chair cannot speak to any matter beyond that which is publicly available, or they would be in breach of their continuous disclosure obligations. Management meets more frequently with investors and some of the questions may be more relevant to management.

It would be more helpful if the introduction to the questions addressed to the board in the Guidelines noted that they are not intended as a checklist for shareholder engagement, but as questions that may arise if there are gaps in the publicly available information.

Our more detailed comments on the Revised Draft Guidelines are set out on the following pages.

Yours sincerely

A handwritten signature in black ink, appearing to read "Tim Sheehy". The signature is written in a cursive, flowing style.

Tim Sheehy
Chief Executive

Specific feedback: Revised Draft Corporate Risk Oversight Guidelines

- a) It would be useful if the Guidelines acknowledged that disclosure of risks need to be meaningful, that is, material to that particular business. Importantly, disclosures require board oversight. They should not be left to the discretion of lawyers without input from the board.
- b) At 2.9, Chief Risk Officer, the Draft CROC Guidelines take a prescriptive approach to the executive management of risk management. In Australia, for example, financial institutions are regulated by the Australian Prudential Regulation Authority (APRA), which has issued a series of prudential standards relating to the governance and risk management of such entities. The focus is on a large assurance team, of which a Chief Risk Officer may be but one component. Of importance is that the assurance team is independent and with a direct reporting line to the board. While we recognise that the Draft CROC Guidelines state that it is for the board to determine if the position of Chief Risk Officer is required, the current drafting does not accommodate the large assurance team that many listed entities have in place.
- c) The interplay between strategy, risk appetite and risk oversight is very theoretical, and does not canvass the practical aspects of risk management implementation and oversight.
- d) The use of the term 'material risks' should be better referenced to the context of the organisational strategy and its industry sector. Reference should also be made to the context of the investor's expectations, as these will differ from investor to investor.
- e) 1.3 on Risk culture could be better framed as that the board should specify their expectations of a risk culture, model the behaviour and measure the risk culture.
- f) The board has a dedicated second line of audit, compliance and risk management teams to support it in its oversight role of the first line of the business. The work of these teams feed into the board committees, such as audit and risk. This could be better communicated in the Draft CROC Guidelines.
- g) The annex containing a table on steps a board should take during a crisis sits oddly in a document in which 'risk is defined as the effect of uncertainties on corporate objectives, recognising that the effect can be either positive or negative'. We are of the view that crisis management is likely to be required if insufficient risk management frameworks are in place. However, giving prominence to crisis management suggests that it is risk management. This would be an unfortunate emphasis.
- h) The guidelines could incorporate a risk oversight framework or model to give the reader an appreciation of effective risk oversight.

Specific feedback: Revised Draft Integrated Business Reporting Guidelines

- a) The prescriptive and somewhat evangelical approach taken in the Draft IBR Guidelines is at odds with the principles-based approach taken in Australia. We recognise that ICGN is a supporter of integrated reporting, and that the guidelines are intended to facilitate investors seeking an integrated approach to annual reporting across jurisdictions, but there is little recognition that each jurisdiction will have its own approach to this topic. For example, in Australia, the issue of integrated reporting was canvassed in a review of the 2nd edition of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*, and the feedback from all market participants, including shareholders and shareholder representative groups, was that it was too early to introduce a recommendation on integrated reporting in the Principles and Recommendations. The 3rd edition introduced new Recommendation 7.4, which states 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 new recommendation (against which all listed entities must report under the listing rules) attracted very significant support from a large number of investor groups and organisations associated with the sustainability movement in Australia, as well as support from some listed entities that currently produce sustainability reports. Investor groups in particular commented that its inclusion represents a significant step forward in encouraging disclosures in an increasingly critical area that impacts sound long-term investment decision-making by investors. The Draft IBR Guidelines should more clearly state why ICGN supports integrated reporting, but also accommodate the reality that different jurisdictions are managing their moves in this direction in varying fashion.
- b) There is also no recognition in the Draft IBR Guidelines that any move to integrated reporting will also need to be a 'journey' for companies. There needs to be recognition that companies can start small and expand as they build the capacity for integrated thinking and the metrics for integrated reporting. This is particularly relevant in Australia, where many listed entities do not currently issue a sustainability report — to move to the GRI reporting framework, with its multiple KPIs, would be a massive imposition on many smaller listed companies, which form the greater number of entities listed on ASX. They have not developed the internal processes for capturing all relevant data nor have they developed the capacity to measure various sustainability-related functions and activities. Governance Institute has detected considerable interest and enthusiasm among Australian listed entities to explore integrated reporting, but in a great majority of instances the companies are not in a position to prepare a report in accordance with the Draft IBR Guidelines. That is, issuers may be keen to adopt integrated thinking and want to develop the capacity to build metrics in relation to many of the six capitals and the IBR Guidelines should support this enthusiasm by encouraging reporting entities to prepare an integrated report that is consistent with the principles set out in the guidelines without demanding slavish adherence to a 'one-size-fits-all' approach. In a similar fashion, companies with multiple business models, for example conglomerates, might choose to start with an integrated report on one business rather than the group, or do an integrated report on each business with an additional layer providing a synergistic explanation of how they fit together, as it builds capacity to integrated thinking — again, the emphasis should be on encouraging the move to integrated thinking rather than an insistence on one approach.
- c) The Draft IBR Guidelines do not recognise that the reality of annual reporting in companies is that management prepares much of the report, with the directors reviewing and providing feedback, challenge and input. That is, management executes and the board supervises. The Preamble captures the role differentiation, but the Draft

IBR Guidelines would be stronger and more applicable if the sections devoted to reporting and disclosure better communicated the separate roles. It could be confusing to infer that the board and management issue separate disclosures, which the Guidelines currently do.

- d) The suggestion that forward-looking statements could be up to 10 years into the future belies the reality of what a board can and cannot confidently disclose. The annual report — whether integrated or not — is historical information, not a prospectus for investors on expected future performance. While at present entities verify facts and ensure that forward-looking statements are underpinned by appropriately robust assumptions and analysis, the process is still much less rigid and formal than that undertaken for a prospectus. The Draft Guidelines refer to disclosures of the business strategies and prospects for up to 10 years, which is more than the forward 12-months period. Current practice within Australian companies is that no board would release an OFR without auditor approval, but auditors will be extremely uncomfortable signing off on forward-looking information covering 10 years.
- e) In the Preamble, the first sentence in the second paragraph would make more sense if it was rewritten as ‘The aim of the ICGN Integrated Business Reporting Guidelines is to emphasise the importance of companies providing a holistic account of how they create and sustain value by reporting non-financial as well as financial information’.
- f) In the Preamble, the second sentence in the third paragraph contains an absolute statement in relation to strategic decisions. This would be better rewritten as ‘...and strategic decisions will often need to be based on a broader set of factors than just financials’.
- g) In 2.1, the second sentence in the second paragraph needs to be turned around, that is, it should state that ‘The existence of the “value gap” has heightened the importance of incorporating intangible value drivers into investment decision making, including environmental, social and governance (ESG) analysis’. In its current form it assumes that ESG issues may be the biggest material business risk, but this is not necessarily the case.
- h) This point arises again in 3.1, where the assumption is made that the biggest material business risks are ESG factors.
- i) The questions in Part 4 belie the reality of shareholder engagement. Firstly, the chair may meet with investors to discuss governance issues, which may include discussion of environmental and social issues. However, other directors do not meet with investors to discuss these matters, apart from the chair of the remuneration committee, who may meet to discuss remuneration issues. Secondly, such meetings of chair and investors generally take place once or twice a year, and last for approximately one hour. In that period of time, about four questions of those set out in the Draft IBR Guidelines are likely to be canvassed — it is simply not possible for a meeting of chair and investors to canvass the volume of questions suggested in Part 4. Moreover, the chair cannot speak to any matter beyond that which is publicly available, or they would be in breach of their continuous disclosure obligations. Management meets more frequently with investors and some of the questions may be more relevant to management. For example, Question 10 is aimed at the processes a company has put in place to keep its board abreast of regulatory, governance and environmental trends that potentially affect the company. It would be more helpful if the introduction to the questions addressed to the board noted that they are not intended as a checklist for shareholder engagement, but as questions that may arise if there are gaps in the publicly available information.