

Attachment 3

(following)

No direction

Peter Wilson says it's time company directors had an education

At the end of a recent rowdy annual meeting of shareholders for an ASX-listed company, an elderly woman turned to me and said: "This board of directors is like a group of badly behaved teenage boys in their mid-60s."

She was understandably perplexed after witnessing a dismal attempt to defend a contentious remuneration report. It brought home to me two critical characteristics that have bypassed the world of company directors: compulsory training in professional standards; and a licence to operate.

When visiting a lawyer, medical practitioner, architect or accountant, the expectation is that the person sitting opposite is thoroughly trained and has satisfied the full and continuing education requirements of an esteemed professional body. Failure to achieve the required standard will result in denial of entry to the field of professional practice, and failing to maintain the standard will result in disqualification.

Company directorships are one of the few noteworthy areas of professional practice for which no formal barrier to entry exists.

A significant informal barrier to entry exists, however, and it operates to exclude all but an intimate few. A scene from a *Yes Minister* television episode illustrates this. The minister asks a top British bank chairman how he was appointed. "In my walk of life, chaps look after chaps," was the reply.

While I am a strong believer in the value of personal networks and sharing experiences

with colleagues, ordinary shareholders should not have to rely on that alone to safeguard their interests.

The annual reports of large listed companies reveal that about 10 per cent of directors are women. Among the major resources company boards, there are no indigenous Australians. Male caucasians, often in their late 60s, rule the roost on top listed boards and many are on multiple boards. Executive search firms will say they have all this in hand, but they play a part in only a minority of appointments and are inherently conflicted by the link between their source of future income and board appointments.

How different it might have been had objectively structured standards of ability, independence, governance and training been applied to the appointment of global banking directors over the past 10 years.

In the immediate and medium future, much attention is likely to be directed at the issues of executive pay and accounting disclosure standards, but any efforts in those areas risk missing the main game - how to train, select and appoint the captain and officers of the corporate vessels to whom are entrusted the welfare of workers, shareholders and the general community.

At present, directors largely recommend board appointments from a self-selected number, supplemented by recently retired CEOs, CFOs and ex-auditors. From my experience in dealing with institutional shareholders, their capacity to provide checks and balances is limited by their reluctance, often as a matter of policy, to intervene in

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board appointments. That practice underpins a default bias for director incumbency that can drag on for many years.

A century ago, an English judge hearing a company law matter was reputed to have observed that the board of directors in the case was akin to a class of mediocre students who had marked their own exam papers. A hundred years later that observation still rings true.

Being a company director carries high levels of financial accountability, ethical responsibilities and fiduciary duties covering investors, employees, customers and the wider community. It should not be a club operating in accordance with an informal and discriminatory entry system where "chaps look after chaps".

When the financial crisis is behind us, the community will once again look to company boards to accelerate the economic recovery into continuing prosperity.

The time has come for directors to be subject to compulsory education and regular independent assessment of their competence to serve.

In the case of directors of large listed companies, the standards required and licence to practice as directors should be comparable with other professions. At present any professional development undertaken through bodies such as the Australian Institute of Company Directors is discretionary.

Compulsory education would include coverage of relevant legislation, judicial decisions and case studies to demonstrate the complexity at times of having to act in shareholders' interests. Assessment by an independent panel of examiners would be followed by the posting of results and rankings on the websites of the Australian Securities and Investments Commission and the Australian Stock Exchange, thus ensuring transparency.

A licence to practise should be retested every few years and strict time limits put on holding an independent directorship with any one large company. Family-owned and small businesses where directors and shareholders are the same people would be excluded. Ultimately, any reforms should become part

of the Corporations Act, including giving ASIC the power to issue a licence for a person to operate as an independent company director and the power to revoke it when necessary.

The reforms would not change the existing responsibility of boards to recommend director appointments to shareholders, whose vote would determine the outcome. However, the recommendations would be based on transparently qualified candidates meeting the standards prescribed by law.

The outcome would be to boost the quality of board members and community confidence in them.

A reform blueprint of this order will be likely to cause dissent among many present directors who have relied on their networks alone to secure appointments. However, many directors would welcome such a reform as a way of lifting standards and purging the ranks of free riders who can imperil business decisions that have far-reaching effects on employees, customers and ordinary shareholders.

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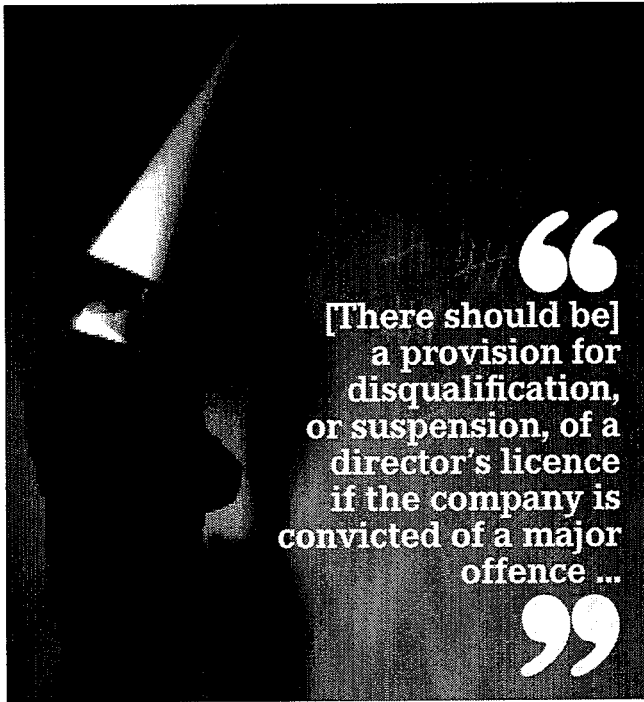
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Company director reform – A blueprint

1. A compulsory basic professional education qualification, which could be delivered through an accredited private body or a public institution. As a minimum the curriculum would cover company law and practice, including key landmark judicial decisions; other federal and state laws with which companies are required to comply; taxation law; employment laws and people management practices; accounting standards and principles; and complex case studies around acting in the best interests of shareholders.
2. Completion of an independent directors’ assessment process with standards set and results overseen by a statutory body established under the Corporations Law.
3. A minimum level of continuing professional development.
4. Regular retesting and re-licensing, say every five years, as a precondition for appointment to a board of directors for a third term.
5. Even more advanced training and testing for very large ASX listed corporations, where the skill and experience requirements must be of the highest level.
6. A compulsory maximum term of 10 years for holding a directorship on the board of any significant company, with no provision for exemptions. Boards need to be exposed to turning themselves over with a frequency akin to movements in CEOs and top management.
7. Publication online of all qualified director lists by ASIC, and a requirement for corporations to publish their directors’ qualifications

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- and dates of assessment, license tenure terms and testing results in annual reports - much the same as the scores published for year 12 students so there is transparency on whether the best professionally trained and assessed directors are getting through to the boards of the largest, most challenging and complex organisations. If not, the ordinary shareholder can then be at liberty to ask: why not?
8. Transition provisions of up to 24 months for current directors to either become accredited in this new world or step down in favour of someone who is.
 9. Provision for disqualification or suspension of a director's licence if the company is convicted of a major offence or suffers a significant loss of its market capitalisation value during a year, with any shareholder having the right to petition such action once certain thresholds have been reached.
 10. As a corollary, ASIC should be authorised to appoint an interim board of trustee directors from an approved director list in the event that more than half of a board is lost due to disqualification, or where the board size minimums are invoked through suspension or dismissal.
 11. Exemptions to these procedures would be available for small businesses and family owned companies where the owners constitute all the directors, and possibly charitable institutions and not-for-profit boards, where "other shareholder's money" is not involved. Government boards could comply with this by ministerial consent, depending on the entity's nature. Being directors of such businesses would still carry the obligation to comply with basic laws affecting companies.
 12. These principles and standards should apply to CEOs who wish to assume the role of managing director as well.
 13. Rigorous assessment of directors' performance to be undertaken annually. Best practice boards would commit to external assessment of their performance.
 14. If a professional education system like this is shown to work well, it could be used to enhance efficiency in the functioning of the labour market for non-executive directors. Specifically, directors could indicate their candidature for forthcoming board vacancies - online via such a new director's qualification list to target companies on the ASX or private ones via the ASIC. Candidates could then be selected for short-list interviewing based not only on their experience (as at present), but also based on their relative scores for demonstrated contemporary knowledge and ability; target companies, and indeed shareholders and the public, would thus have objective and recent data available on the web informing them of high potential men and women candidates for board posts. ●
- AHRI national president, Peter Wilson has worked as a senior executive in two ASX 30 companies and has served on two ASX listed company boards as a non executive director. He has chaired and served as a director on a number of public and private boards. He presently chairs the boards of the Australian Human Resources Institute and Yarra Valley Water, and is a director of two offshore corporations. He is a Fellow of the Australian Institute of Company Directors, and a member of CPA Australia.**

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