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Executive Remuneration Inquiry  
Productivity Commission  
Locked Bag 2  
Collins Street East  
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By email [exec\\_remuneration@pc.gov.au](mailto:exec_remuneration@pc.gov.au)

Dear Sir

#### Regulation of Director and Executive Remuneration in Australia

In view of widespread community interest in executive remuneration, particularly in light of the global financial crisis and the Government's recent changes to legislation governing termination payments, the ASX Corporate Governance Council (Council) welcomes the release in April 2009 by the Productivity Commission (Commission) of the issues paper – Regulation of Director and Executive Remuneration in Australia.

The Council notes that the Commission is calling for submissions by 29 May 2009, will hold an initial round of public hearings starting 16 June 2009 and proposes to release a draft report with preliminary findings in late September 2009 to elicit feedback through further submissions and a second round of public hearings. The Council also notes that the final report from the Productivity Commission is expected to be provided to Government on 19 December 2009.

The Council has previously made representations to Government warning against the enactment of laws as a “knee jerk” response to current issues and Council very much appreciates the approach of referring these matters for public consideration and community consultation so that decisions about whether there needs to be change to laws or regulatory practice can be made on mature reflection, taking into account a range of perspectives about the desirability of change and the impacts that they are likely to have in operation.

#### Council and its Principles and Recommendations

The Council is a very diverse independent body, bringing together 21 businesses, investment and shareholder groups. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be an effective practical guide for listed companies, their investors and the wider Australian community. The Council's diverse range of voices is one of its strengths. Its striving for consensus is consistent with maintaining balance in regulatory and reporting affairs.

Since 2003, the guidance provided by the Council's Corporate Governance Principles and Recommendations (the 2003 Principles and Recommendations) has contributed to a high standard of corporate practice in Australia free from the agency costs of a “black letter” law approach. The Council's objective is to ensure that the Principles and Recommendations remain relevant to Australian business and investment communities. The Council believes that it is important to periodically review the corporate governance practices to ensure that they

#### Australian Securities Exchange

Australian Stock Exchange  
Sydney Futures Exchange

Australian Clearing House  
SFE Clearing Corporation

ASX Settlement and Transfer Corporation  
Austraclear

continue to reflect local and international developments and promote high standards of transparency about the corporate governance practices of listed entities.

The revision of the Principles and Recommendations resulting in the revised Principles and Recommendations introduced in August 2007 with effect from 1 January 2008 (the 2007 Principles and Recommendations) are part of that process.

In its review of the Principles and Recommendations, in November 2006, Council released a Consultation Paper (Consultation Paper) and an Exposure Draft of its proposed changes to the Principles and Recommendations (Exposure Draft) requesting feedback from interested parties. Council's proposed changes to the Principles and Recommendations were designed to remove areas of regulatory overlap between the existing Principles and Recommendations and equivalent provisions in the Corporations Act or the Accounting Standards; provide further assistance for companies and investors to better understand the application of certain Principles and Recommendations by merging principles which cover common areas of governance; refine the Principles and Recommendations to take into account internal feedback from Council review groups and feedback from users of corporate governance information; ensure consistent terminology throughout the Principles and Recommendations and to provide greater clarity and remove possible ambiguities in certain Principles and Recommendations.

Council received over 100 submissions on the Consultation Paper and the Exposure Draft. Approximately 120 listed companies put forward their views. Other submissions were from industry groups, individuals, domestic and international institutional investors, fund trustees and non government organisations. The revised principles therefore not only reflect the diverse contributions from the Council members themselves but also reflect the contributions of public submissions.

The first of the Annual Reports subject to the 2007 Principles and Recommendations are those in respect of the year ended 31 December 2008, due by April 2009.

One of the key features of the Principles and Recommendations is that they are not prescriptive, but are a set of flexible guidelines. They do not require a "one size fits all" approach to corporate governance. The Principles and Recommendations are a set of suggestions for practices designed to optimise corporate performance and accountability in the interests of shareholders and the broader economy.

If a listed entity considers a Recommendation as inappropriate to its particular circumstances, it has the flexibility not to adopt it – a flexibility tempered with the requirement to explain why – the "if not, why not" approach. The commentary that follows each Principle and Recommendation is provided by Council to assist listed entities to understand the reasoning for the Recommendation, highlight factors which may be relevant to consider and make suggestions as to how to implement the Recommendation. Where appropriate, additional guidance is provided to assist listed entities to achieve the objectives of the relevant Principles and Recommendations, to provide support and guidance to the legislative framework and to complement the direction taken by Government.

#### Background to Remuneration under the Corporate Governance Principles and Recommendations

Principle 9 of the 2003 Principles and Recommendations sought to ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to corporate and individual performance is defined and disclosed. Recommendation 9.1 required companies to adopt remuneration policies that attract and maintain talented and motivated directors and employees in order to encourage enhanced performance of the company and to demonstrate a clear relationship between performance and remuneration. The intention was that the policy underlying executive remuneration be understood by investors.

The Accounting Standards on remuneration disclosure and the CLERP 9 legislation on the non-binding shareholder vote and enhanced annual reporting requirements, including remuneration reporting, were not finalised at the time that the 2003 Principles and Recommendations were released. Consequently, much of the material in Principle 9 was not produced elsewhere at the time. The subsequent legislative and regulatory changes to the Corporations Act and the Accounting Standards resulted in overlap and duplication with Principle 9.

As a part of the review process undertaken by Council, the issues relating to remuneration were considered. The review and consultation process resulted in a number of changes, including additional guidance and also streamlining of the Principles and Recommendations. As the body with responsibility for forming views on governance matters, Council dealt with the remuneration issue in a way that on the one hand does not interfere with the ability of boards and management to make ordinary business decisions and on the other hand gives guidance on the appropriate considerations of transparency and checks and balances.

For example, Council provided additional commentary to Recommendation 8.2 in the 2007 Principles and Recommendations on equity-based executive remuneration plans that allows flexibility to companies and assisted in providing greater transparency around remuneration issues. The additional commentary addressed the requirement that companies clearly distinguish the structure of non executive directors' remuneration from that of executive directors and senior directors (Principle 8.2), provided guidelines for executive remuneration packages (Box 8.1) and for non – executive director remuneration (Box 8.2) and provided guidance that companies may find it useful to submit to shareholders proposed equity - based incentive plans which will involve the issue of new shares to senior executives prior to implementing them.

Feedback to the Council from the consultation process also showed that companies had difficulty understanding the disclosure required under Recommendation 9.4 because it implied a need for shareholder approval of thresholds set in plans for equity remuneration and it was unclear whether it related to “on-market” purchases or the new issues of shares. Neither the Listing Rules nor the Corporations Act requires shareholder approval of these plans, the issue of shares to executives who are not directors or the acquisition of shares by these executives.

Council decided that Recommendation 9.4 needed to be deleted because of its ambiguous form, to accommodate changes concerning disclosure requirements made to section 300A of the Corporations Act (and the AASB 124 Related Party Disclosure) and relied on those provisions in relation to the requirements to disclose. Council also felt that it was not the appropriate forum for dealing with the matter of shareholder approval of equity-based executive remuneration. Council invited ASX and the Government to review of the position of shareholder voting for equity based executive remuneration plans within the framework of the Corporations Act and/or the Listing Rules.

#### Review of Governance Disclosures in Annual Reports

Since 2004, a review of governance disclosures made by listed entities in Annual Reports with a year end balance date of 30 June has been conducted each year by ASX Markets Supervision Pty Limited (ASXMS) to determine the level of reporting of the Principles and Recommendations. The findings from this review are made public each year and published on ASX's website. These findings are routinely considered by the Council.

Overall reporting levels by listed entities have improved every year since 2004. The overall reporting level in 2004 was 84%, in 2005 88%, in 2006 90% and in 2007 90.5%. ASXMS has just concluded its review for the 30 June 2008. Results will be released publicly towards the end of June 2009 and will reveal that the overall reporting level for this year has increased.

The data collated for entities reporting a year end of 30 June 2008 also shows strong reporting levels for those recommendations relating to remuneration. . Although the 2007 Principles and Recommendations commenced operation on 1 January 2008, the first group of listed entities required to report against these Principles and Recommendations is those entities with a year end balance date of 31 December 2008. . The review of Annual Reports for listed entities with a year end 31 December 2008 is underway and the results of this review are also expected to be released publicly also towards the end of June 2009.

We will forward to the Productivity Commission a copy of these reports when released.

#### Next Steps

One of the key objectives of the Council's Principles and Recommendations is to seek to complement the direction taken by Government in a particular area (such as remuneration) and provide support and guidance to the legislative framework, where necessary. For this reason, should the Productivity Commission and ultimately

the Government choose to continue to provide further legislative clarity or direction in relation to executive remuneration, and support that framework with guidance on how remuneration should be structured and/or reported to stakeholders, the Council is willing to consider whether its Principles and Recommendations should form part of the overall framework.

Should the Productivity Commission wish to discuss any aspect of this letter or the issue of director and executive remuneration more generally please contact either Ms Luise Elsing on 02 9227 0612 or me on 02 9227 0405.

Yours sincerely

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