Governance - a guide to monitor listed companies

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"ASCI Governance Guidelines: A guide for superannuation funds to monitor listed Australian companies" by the Australian Council of Superannuation Investors, July 2013

For some people, governance is akin to Mogadon. It certainly isn't as exciting as discussing the direction of markets, or the outlook for the residential property market. Nonetheless, good corporate governance is vital if we are to have a healthy, well-functioning capital market. Without it, we cannot have faith in what our companies tell us is going on.

So exactly what is governance? It is just the practice of 'governing' or managing an entity - a company, a family, a super fund. *Good* governance is about having the right policies and procedures to make sure issues are identified and decisions are made in a transparent, logical and consistent way. Good governance does guarantee the right decisions will be made, but it does provide the processes to make well-informed decisions. Good governance is as important for large listed companies as it is for a professional practice.

So, the most recent ACSI (Australian Council of Superannuation Investors) Governance Guidelines - while specifically aimed at superannuation funds and listed companies - hold a lot of information which may be valuable on a day-to-day basis for any investor or business owner.

The Guidelines are premised on three core principles, which recognise that:

- Good governance requires boards to consider and manage all material risks facing the company, including ESG risks;
- Effective board governance contributes to shareholder value creation and risk-reduction, creating the conditions in which sustainable long-term investment can prosper; and,
- Superannuation funds can, and should, protect and manage their investments for the long-term through the consideration of ESG risks in their investment decision-making processes.

Specifically, the Guidelines consider:

- Board responsibilities;
- Board composition and processes;
- Remuneration;

- Company meetings;
- Disclosure; and,
- Financial integrity

In terms of board responsibilities, the Guidelines tell us that, unfortunately:

> "Rules and regulations alone are insufficient to instil high standards of governance, corporate conduct and deliver the best protection to shareholders.
>
> The 'glue' that binds companies to good governance is a strong ethical outlook from the board of directors down.
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> Further, the board is entrusted to oversee a company's business and to formulate, in conjunction with management, a company's policies and strategies. A board must therefore ensure it is adequately informed about key business issues and is properly equipped to encourage management to optimise the long-term performance of the company.
>
> In practice, this means boards must not blindly follow the advice of experts, and should actively assess all matters put before them.

Other board responsibilities discussed in detail in the paper include:

- Promoting good governance;
- Familiarity and capacity to oversee corporate operations;
- Considering the role of the Chairman;
- Risk management;
- Company strategy;
- Capital raisings and looking after pre-emptive rights of existing shareholders;
- Oversight of takeovers; and,
- Oversight of related-party transactions.

The Guidelines then turn to Board composition and processes. They tell us:

> Boards should be comprised of individuals able to work together effectively to steer a viable, profitable and efficient company. Directors must have the competency and commitment to oversee the activities of the company and its officers.
>
> A properly structured board should include skilled directors who have diverse backgrounds (e.g. core expertise, age, gender). Each

> director must have a high degree of competency, integrity, skill, capacity, experience and commitment to discharge their duties and responsibilities.

The ACSI Guidelines also discuss how boards should be structured and reviewed – composition, independence, performance evaluation, board committees, liabilities.

> Executive remuneration should be aligned to the delivery of company strategy and should be designed to promote sustainable long-term performance, and shareholder value creation. An appropriate remuneration policy is one tool for boards to achieve these aims.

On company meetings, the Guidelines state:

> Participation in company meetings is a critical right of shareholders and a cornerstone of corporate governance practice.
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> Exercising a vote is one of the most visible tools available to influence the governance practices of the companies in which we invest.
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> Voting enables investors to demonstrate participation and interest in the governance practices of investee companies.

The paper also points out that:

> Disclosure is the key to building confidence and allowing investors to better understand, evaluate and assess investment risk and return.
>
> The timely release of, and equal access to, information is fundamental to market integrity and ensures that all investors are properly informed.
>
> Investors require enough information from companies to be reassured that material governance risks are being considered, and that there are effective processes in place to manage those risks.
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> Companies should ensure that they have the appropriate processes and structures in place to effectively meet continuous disclosure requirements. All information provided to shareholders should be true and fair, even where contentious issues arise. Companies should ensure that they release sufficient information to enable all investors to make informed and accurate judgments.

Lastly, the Guidelines consider financial integrity:

Companies must provide an accurate and true representation of their financial management, performance and reporting in line with relevant legal and accounting standards.

As Justice Middleton held in the Centro Case:

All directors must carefully read and understand financial statements before they form the opinions which are to be expressed in the declaration required... Such a reading and understanding would require the director to consider whether the financial statements were consistent with his or her own knowledge of the company's financial position. This accumulated knowledge arises from a number of responsibilities a director has in carrying out the role and function of a director.

In all, these Guidelines provide all of us with good direction and understanding of how companies should be run - be they multi-billion dollar monoliths, listed large-, mid- or small-cap companies - or even, the smallest professional practice.

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