



The Hon Chris Bowen MP
Minister for Human Services
Minister for Financial Services, Superannuation and Corporate Law

Mr Richard St John
Convenor
Corporations and Markets Advisory Committee
GPO Box 3967
SYDNEY NSW 2001

Dear Mr St John

I am writing to refer an aspect of Australia's corporate governance framework to the Corporations and Markets Advisory Committee for its consideration and advice.

While Australia has a world-class corporate governance framework, the importance of continuing to assess it against international best practice has been highlighted by the recent global economic crisis. An integral part of corporate governance best practice is that boards of publicly listed companies have executive directors, who are full time employees of the company, concerned primarily with the daily management of company business, and a majority of non-executive directors (NEDs) who are independent of management. NEDs provide a corporate board with particular skills, experience and independence, performing an important function in Australia's corporate governance framework. In asking the Committee to examine what guidance is required for both executive directors and NEDs to fully understand the responsibilities of their role, I am particularly interested in what support can be provided to increase the engagement of NEDs with their position on the board and bring an independent and broad view to board decision making.

In 1992 the *Report of the Committee on the Financial Aspects of Corporate Governance* (the Cadbury Report) called for a code of best practice to enhance the standards of corporate behaviour in the UK. The report sparked interest across the globe and, following the subsequent Rutteman Report (*Internal Control and Financial Reporting*), the Greenbury Report (*Study Group on Directors' Remuneration*), and the Hampel Report (*Committee on Corporate Governance*), led to the introduction of the Code of Best Practice in the UK and similar codes in a number of other countries. In 2002 the ASX convened the Corporate Governance Council to produce corporate governance guidelines for listed entities. In 2003 the Council released the first edition of its *Principles of Good Corporate Governance Practice and Best Practice Recommendations* (ASX Principles). The overall intention of the guidelines was to help investors make more informed decisions about the company's corporate governance practices. To this end the guidelines, and the subsequent second edition developed in 2007, have been extremely effective.

Absent from the ASX Principles, however, is any guidance or recommendations for NEDs about what is expected of individuals in that position. The responsibility for clarifying the

role of executive directors and NEDs was instead placed on the company itself (Recommendation 3.1). When the ASX Principles were reviewed in 2007, the issue of providing further guidance to directors about their responsibilities (as separate from the overall workings of the board) was once again overlooked in the consultation.

In the UK in 2003, the *Review of the role and effectiveness of non-executive directors* (the Higgs Review) investigated the role of NEDs and made suggestions for the revision of the *Combined Code of Corporate Governance*, the predecessor to the Code of Best Practice, to include further guidance for NEDs (and directors more broadly). In response to a perceived lack of clarity about the role of NEDs expressed in the submissions to the review, the Higgs Review perceived that clarifying the core elements of the NED role would assist NEDs to fulfil their roles more effectively. The Higgs Review therefore recommended that a description of the role of the NED be incorporated into the Code.

A number of the recommendations of the Higgs Review were adopted by the UK Financial Reporting Council into its *Combined Code of Corporate Governance* as well as separately in the voluntary guidance, *Good Practice Suggestions from the Higgs Report*. As a result the Combined Code now provides a basic level of guidance to NEDs about their responsibilities on the board.

In Australia there is no comparable guidance for NEDs regarding the role that they are expected to play on a board. While industry representative organisations, for example the Australian Institute of Company Directors and the Investment and Financial Services Association, do provide some guidance to directors on their responsibilities, it is unclear whether this level of guidance is leaving current, and potential, NEDs confident in the expectations and responsibilities that are placed on a NED role. In light of the increasing expectations placed on NEDs today as a result of decisions in cases such as *Australian Securities and Investments Commission v Macdonald No.11*, all NEDs, not only those of Australia's publicly listed companies, may benefit from clarification around the expectations of the NED role.

I request that the Committee:

- i. examine the guidance or codes of conduct that are available overseas for corporate directors;
- ii. examine whether there is sufficient guidance provided to executive directors and non-executive directors in Australia to ensure that they have a clear understanding of their roles and responsibilities; and
- iii. advise whether the performance of directors would be enhanced by the introduction of guidance for directors, for example through a code of conduct or best practice guidance, by a relevant regulator; and if so what form that guidance should take.

I look forward to receiving your report by 31 April 2010.

Yours sincerely

CHRIS BOWEN