31 December 2012

Mr John Kluver
Executive Director
Corporations and Markets Advisory Committee
Level 16, Metcentre
60 Margaret Street
SYDNEY

Dear Mr Kluver

FSC SUBMISSION – FUTURE OF THE AGM

Thank you for the opportunity to provide a submission on this discussion paper.

The Financial Services Council (FSC) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, trustee companies and public trustees. The FSC has over 130 members who are responsible for investing $1.8 trillion on behalf of more than 11 million Australians.

The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world. The FSC promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

Our recommendations can be found throughout the document.

Please find our submission enclosed. We look forward to discussing the contents with you. I can be contacted on 02 9299 3022.

Yours sincerely

ANDREW BRAGG
SENIOR POLICY MANAGER

FSC SUBMISSION CONTENTS

1. AGMs: Timing

In normal circumstances companies are required to hold their AGM within 5 months of the end of their financial year. This in itself appears to be a reasonable stipulation, allowing sufficient time to complete and audit accounts and send the appropriate disclosures to shareholders. In practice, it takes most companies up to two months to prepare reports and circulate the relevant information. They will then usually announce the AGM date but it is not until about two weeks before the cut off point before the AGM that the detailed voting information is circulated to investors.

The issue for investors is that with the majority of companies' fiscal year ending on either 30 June or 31 December, many AGMs will be bunched between mid-October to late November or between early April to May. With the information on resolutions which will be voted on at the AGM from companies coming to investors via registries and custodians, albeit electronically, the timeframe in which investors should decide whether to vote in favour or oppose resolutions is limited to little more than two weeks. Where items are "routine" and can be voted through with confidence this is not an issue. Where it becomes an issue is where investors question or disagree with a proposal which a company has made. In this case they may simply vote against the proposal or abstain but most will seek to engage with the company in order to achieve further clarification or an alternative outcome.

It is in the cases where the fund manager decides to engage with management over a contentious issue that the tight deadline restricts a dialogue. Investors need to put a well reasoned case to the company and the company needs to consider carefully its response. If the company is prepared to modify its position this will also require time. Where many companies are reporting within a brief period the fund manager will not have sufficient time to do its research and raise issues with the company so more of the responsibility for this analysis is devolved to the proxy advisers. This group has become increasingly influential as a result, albeit they are not shareholders in the company.

Recommendation: To alleviate "AGM season", the period between the notification of the company's resolutions for the AGM and the deadline for votes to be received should be extended.

It would be preferable for this to be achieved within the current 5 month timeframe which means that the company should be encouraged to publish the relevant information sooner. The alternative, of pushing back the AGM would also create a better window for dialogue with the company but would run the risk of leading into the subsequent reporting season when elements of the dialogue might be overtaken or become redundant.

Another possibility might be for companies to loosely agree to hold their AGM within certain timeframes, e.g., early, mid or late in the reporting season so that all those within a broad sector report in close proximity to each other but overall the AGM season is extended. The mechanics of such a change would need to be explored in detail before a proposal could be framed.

We believe that companies should be encouraged to engage sooner rather than later in the reporting period. This provides investors with necessary time to consider the company's performance and forward approach.

2. Proxy voting

For many years, the FSC and a number of our members have advocated reform of the proxy voting process in Australia. As noted in the issues paper, the current arrangements give rise to inefficiency and integrity concerns which could be obviated.

In our submission to the 2008 PJC inquiry "Better Shareholders, Better Companies" we argued a number of necessary regulatory changes. We made recommendations following substantive engagement with the proxy voting, custodian and share registry industries (as well as our own members).

Although the PJC adopted our recommendations, there has not been an opportunity for reform via adoption of the PJC findings potentially until they were captured in this CAMAC issues paper. During the course of this particular inquiry, a number of our members worked with the Australian Council of Superannuation Investors (ACSI) and Ownership Matters to undertake the most comprehensive assessment of the proxy voting system to date.

Their report "Institutional Proxy Voting in Australia" found again that there are deficiencies in the current system and recommended change. The FSC broadly endorses the 6 recommendations for regulatory reform outlined in the / ACSI Ownership Matters report.

The proxy voting process represents a key element of our corporate governance framework. Ensuring that the process operates effectively and with a high degree of integrity is of vital importance to maintaining confidence in the mechanisms that allow shareholders to exercise their voting rights.

FSC believes the system needs to be improved and that key flaws with the present system need to be addressed. We set out a series of recommendations which, if adopted, will result in a significantly improved proxy voting system.

Recommendation: FSC's view is that electronic voting with increased integrity provisions including an audit trail should be facilitated. This will require cooperation of issuers, sub custodians, owners, managers and the Government broadly.

These recommendations are outlined below under the subheadings required of each party in the chain of the proxy voting process.

<u>Superannuation trustees and investment managers</u>

Superannuation trustees and investment managers should immediately commence requesting issuers in which they hold shares to receive proxy instructions by electronic means as a matter of course at all members' meetings.

<u>Issuers</u>

All S&P/ASX 300 companies should put appropriate electronic proxy voting arrangements in place as soon as possible.

Issuers should develop an electronic proxy voting capability that will provide a meaningful audit trail from issuers & their registrars to shareholders so that superannuation funds, investment managers and other appointed proxies are able to confidently declare how they voted in any instance.

The audit capability should allow for acknowledgement within 24 hours of the record cut-off date for any proxy instruction submitted electronically. The industry is prepared to discuss mechanisms to allow issuers and share registry service providers to recoup any development costs by charging a fee (based on cost-recovery) for using such a system.

Should, as soon as practicable, make publicly available on the corporate governance part of their websites a clear policy surrounding how they will deal with unclear proxy forms and cases where the votes lodged do not reconcile at the proxy appointment cut-off date with the shares actually held by that registered shareholder at the record cut-off date.

The policy should also provide that in cases where there is a discrepancy in the shareholding, the company will direct its share registry service provider to conduct a reconciliation process so that the correct entitlement is voted as opposed to disregarding the entire number of votes.

Financial Market operators

In consultation with issuers and institutional and retail shareholders, FSC will continue to work with the financial market operators towards the development of a template to facilitate standardised disclosure of proxy voting results.

The template could include details of the number of votes lodged against each resolution including as a proportion of issued capital. We believe there would be significant benefit in having a template in which issuers could report the outcome of voting on resolutions. This would reduce inconsistency and improve readability and potentially future engagement. The ASX Corporate Governance Council may be in a position to assist in template development.

We seek the support of CAMAC in this area.

Government (Treasury/ASIC)

Regulation 7.11.37(3) of the *Corporations Regulations 2001* should be amended to extend the record cut-off date to "5 business days before the meeting". The ASX Listing Rule definition of "business day" should be adopted for this purpose.

Additionally, FSC suggests that ASIC issue a Policy Statement or 'no action' position letter clarifying that any issuer that accepts electronic proxies without a relevant company constitution change will not be taken to have breached the relevant sections of the Corporations Act.

Alternatively, in the event that such a statement is unable to be provided by ASIC, FSC recommends that companies seek to amend their constitutions at the next meeting of members to explicitly provide for electronic lodgement if this is not already included in their constitution.

Companies should also be required to report to the market the total number of proxy votes exercisable by all parties and declare the final result tallies.

Further, we also endorse the recommendations for regulatory reform in the ACSI / Ownership Matters report submitted to this review.

3. Shareholder resolutions / engagement

The FSC supports the expansion of the ability of shareholders to submit to companies for inclusion on the AGM agenda non-binding resolutions. Over the last 12 months we have seen instances in relation to both climate change disclosure (Woodside Petroleum) and electronic gaming machines (Woolworths), where resolutions which might otherwise had been put to shareholders as non-binding resolutions instead had to be put as constitutional amendments. Aside from requiring a greater portion of shareholders to pass (75% as opposed to a simple majority) constitutional amendments are not the most appropriate medium for achieving change in areas like these.

The FSC does not accept the arguments put forward by CAMAC report that allowing non-binding resolutions could blur the distinction between the role of the board and that of the general meeting, diminish director accountability, or be equivalent to the company being run through 'shareholder plebiscite' because these concerns have not been realised in the introduction of non-binding resolutions related to executive pay.

To the contrary non-binding resolutions in relation to executive pay have proved a valuable tool for shareholders to express concerns over remuneration practices without causing broader unintended consequences for the company (as per a constitutional amendment) and importantly has increased the level and quality of director engagement with shareholders on remuneration practices.

Coupled with changes to threshold tests, particularly in relation to minimum holding periods, broadening the scope for non-binding shareholder resolutions has the potential to provide a new and important tool for shareholder engagement with companies on issues of interest to long term shareholders, particularly as they relate to the long term sustainability of the company. The coupling of these mechanisms could (as part of a broader package of reforms) prevent some of the negative impacts of short-termism identified by the Kay Review in the UK in relation to the in UK equity markets.

Recommendation: Expand the ability of shareholders to submit to companies for inclusion on the AGM agenda non-binding resolutions. Where a company rejects the request to include a non-binding resolution, an independent arbiter determines which proposals are placed on the agenda.

Section 5.4 looks at the legal requirements and practical mechanisms by which shareholders can place a matter on the agenda of a company's AGM. Currently shareholders are only able to place very specific items on AGM agendas with little scope for non-binding resolutions being put and significant scope for companies to refuse resolutions.
In considering this issue, the FSC takes the broad view that shareholders should:

- Not be impeded by misaligned or inefficient processes from placing matters on the notice of meeting; and
- Be able to place non-binding resolutions on the agendas of companies' general meetings so long as safeguards are in place to prevent vexatious or unjustified resolutions.

The review asks a number of questions regarding these issues which all warrant responses, but should be taken together with regard to the principle stated above.

Questions

Should there be any change to the timing requirements for the calling of an AGM, including for shareholders to place matters on the agenda of an AGM, to seek the circulation of statements concerning any resolution, or to nominate persons for the position of director?

Should companies be required to publish a pre-agenda notice and, if so, what should be the contents and timing of that notice?

The FSC supports the timing changes suggested by the review, whereby companies should provide three months' notice of the date of the AGM and provide shareholders one month to submit any resolutions or director nominations. The current system requiring the notice of annual general meeting to be lodged with the ASX 28 days prior to the AGM should be increased to 42 days. Further, the current requirement for the annual report to be lodged with the ASX 21 days before the AGM should also be lengthened to 42 days. To fit it with the notification of the date of the AGM (3 months prior to the meeting) and the lodgement of the notice of meeting with the ASX (42 days prior to the AGM) shareholders who want to submit a proposal on the AGM agenda should do so within one month of the notification of the AGM date.

Longer periods will permit increased scrutiny but also more informed engagement and deeper consideration of the issues at hand.

Question

Does the current law concerning excluded material either create undue difficulties for shareholders who wish to criticise directors or, conversely, unduly restrict directors in vetting out information to be circulated to shareholders at the company's expense?

The FSC supports a framework where defamatory resolutions against individual directors can be excluded as there are other forums, in particular director elections and the ability for shareholders to obtain the shareholder register, where shareholders who are critical of directors can express their views. However, this should not extend to the board or company as whole, where resolutions critical of a course of action or decisions should still be permissible in non-binding form proposed below. *What about an independent arbiter such as in the US – the SEC determines which proposals make it onto the agenda*

Question

Should there be any rule regarding the failure to present a resolution at an AGM?

The FSC agrees with the CAMAC Report and does not support penalties for not presenting a resolution at the AGM.

4. Reporting content

Issue: CAMAC, as part of the terms of reference on the future of the annual general meeting, is required to review whether documents in relation to the AGM - in this case specifically the annual report - should be changed to better meet the needs of shareholders in the future. This will require an examination of such matters as: reduction of unnecessary information ('clutter') in annual reports; integrated reporting (a more forward looking strategic approach to communication); any issues of liability in relation to proposed changes, and technology to improve communication.

The FSC shares the view that annual reports are limited in usefulness due to a combination of complexity, detail and 'clutter', and lack of a consistent strategic focus by most reporting entities to explain the creation of long term value. The introduction of s 299A was intended to address some of these issues by providing for what is in effect a new operating and financial review (intended to address the limitations of audited accounts in providing a transparent assessment of the financial progress of companies). The FSC welcomes the forthcoming guidance by ASIC (CP 187 - Effective disclosure in an operating and financial review).

Nonetheless, it is clear that the current requirements for the annual report remain suboptimal and, further, there are competing views on how to most effectively address these problems. The FSC's view is that the most promising work in this field is being undertaken by the International Integrated Reporting Council (IIRC). The IIRC is currently piloting a draft integrated reporting framework with organisations, including some Australian companies.[1]

The IIRC will publish a complete draft framework by the end of 2013 (with interim reports on technical matters to be published throughout 2012 and 2013). The FSC notes that the Financial Reporting Council has established an Integrated Reporting Taskforce specifically to monitor IIRC developments and outputs.

Recommendations:

- CAMAC should acknowledge and reference the work of IIRC and consider recommendations for amendments to annual report requirements as the work of the IIRC evolves.
- There should be focal points for consideration of the IIRC integrated reporting framework, as well as for those technical issues that arise in the lead-up to publication of the completed integrated reported framework in 2013. The FSC is of the view that the logical place for that focus point in the short term is with the ASX Corporate Governance Principles and the longer term, the Financial Reporting Council.
- The FSC is of the view that changing reporting requirements to provide for a strategic report and an annual directors' statement, as outlined in the CAMAC discussion paper at 4.2.6, would be beneficial. However, that proposed change should be considered in the context of the review referred to above and should not be undertaken in isolation.

5. Stewards code

Corporate governance in Australia has benefitted from a series of self-regulatory and legal requirements which govern the way in which institutional shareholders conduct their affairs as fiduciaries.

The FSC has maintained a number of self regulatory tools to assist asset managers, asset owners and companies in meeting high standards of corporate governance. Other bodies such as the ASX Corporate Governance Council are well-established institutions which play an important role in achieving high standards of corporate governance in Australia.

[1] "Integrated Reporting brings together material information about an organization's strategy, governance, performance and prospects in a way that reflects the commercial, social and environmental context within which it operates. It provides a clear and concise representation of how an organisation demonstrates stewardship and how it creates and sustains value. An integrated Report should be an organization's primary reporting vehicle" (IIRC, May 2012).

For example the FSC has maintained the Blue Book – a corporate governance guide for fund managers and companies for over a decade in addition toa mandatory standard on proxy voting disclosure on all Australian company resolutions.

In superannuation (asset ownership), the FSC has developed a mandatory governance standard which requires our superannuation company members to have a majority of independent directors, independent chair, conflicts provisions and member disclosures of proxy voting and ESG risk reporting. Other bodies such as ACSI have undertaken significant bodies of work in guiding super trustees on meeting contemporary governance standards expected of asset owners.

In 2011, in conjunction with ACSI, the FSC published a reporting guide for Australian companies on disclosing their ESG risks to investors.

We strongly believe in the value of high standards in corporate governance which recognises the stewardship and fiduciary nature of investment management and trusteeship in superannuation. A number of the elements in the UK Stewards Code have been developed comprehensively by the FSC and other bodies in Australia – therefore we would prefer that there not be duplication.

This is particularly salient given self regulation in Australia has been effective. For example, investors in a pool managed investment scheme can view the manager's proxy voting record and the ASX Corporate Governance Principles (which drive company disclosure) have consistently been updated to ensure they remain fit for purpose.

Accordingly we would not support a "hard" regulatory approach whilst self-regulation is maintaining its effectiveness. The UK Stewardship Code has seven principles, some of which are presently covered by legal or self-regulatory obligations in Australia. The FSC is prepared to review the viability of creating further standards for asset managers in addition to Standard 13: Proxy Voting.

Further, the FSC is prepared to work with other stakeholders to develop a consolidated set of "codes" which could continue to apply through self-regulation.

6. The 100 member rule

3.84 Section 249D(1) of the Corporations Act stipulates that:
(1) The directors of a company must call and arrange to hold a general meeting on the request of:

(a) members with at least 5% of the votes that may be cast at the general meeting; or
(b) at least 100 members who are entitled to vote at the general meeting.

Our view is that the rule may be open to abuse This is a widely shared view, for instance, in the recent PJC inquiry, Treasury stated that the ability of relatively small groups of shareholders to impose the cost of an extraordinary general meeting (EGM) on companies gave them 'significant and undue leverage when negotiating with large companies'.

As noted in the PJC paper, the Exposure Draft of the Corporations Amendment (No. 2) Bill 2006 proposed to abolish the 100 member rule and leave the five per cent requirement, which would have brought Australia's law into line with comparable jurisdictions. It is further noted that the states may need to agree with the Commonwealth on executing this change.

We believe this warrants further consideration, accordingly we propose a variation of recommendation 7 of the PJC report: "The government should continue to negotiate with the states to have the 100 member rule abolished." Our variation is designed to continue permitting minority shareholders access to calling meetings providing they meet criteria which demonstrates their commitment as investors.

Recommendation: retain the 5% threshold.

Amend the 100 member threshold to require that each of the 100 members have a:
(1) A minimum holding period of 12 months; and
(2) A $1,000 minimum holding value.

In order to bolster the proxy voting recommendations above, we believe that shareholders should be permitted (where they comprise more than 5 per cent of a company) to appoint an independent reviewer / scrutineer of a poll.