

16 February 2016

John Stanhope
Chairman
Business Reporting Leaders' Forum

By email: john.v.stanhope@gmail.com

Dear John

Integrated reporting

Governance Institute of Australia (Governance Institute) is the only independent professional association with a sole focus on whole-of-organisation governance. Our education, support and networking opportunities for directors, company secretaries, governance professionals and risk managers are second to none.

Our members have primary responsibility to develop and implement governance frameworks in public listed, unlisted and private companies. Many of our members have responsibility within organisations for the narrative reporting aspect of the annual report. While the CFO has responsibility for financial reporting, the narrative in the directors' report, the operating and financial review and the chair's report, providing the context and background to the financial statements, is most often drafted by the company secretary, acting on behalf of the board. The company secretary is also most often the person charged with drafting the corporate governance statement in the annual report on behalf of the board — this statement is mandatory for public listed companies in Australia. Our members are therefore very familiar with the requirements of corporate reporting.

Our members recognise that there is a range of issues and opportunities affecting long-term business value that is much broader than can be reflected in a set of current-year financial measures. Governance Institute is on the public record as calling for improvement to corporate reporting. This is not due to any lack of disclosure requirements in current legislation, or an unwillingness of companies to engage with their investors through enhanced reporting.

Governance Institute strongly supports the simplification of reporting requirements. The aim of reporting should be to ensure that shareholders want to and can read the disclosures, and remain knowledgeable about and engaged with the entity in which they invest. Disclosure needs to be more than simply comprehensive. It needs to be meaningful and comprehensible. The cumulative impact of increased disclosure requirements in relation to corporate reporting has seen much reporting become largely incomprehensible to investors, particularly retail investors, despite strenuous effort on the part of issuers to not only meet statutory requirements but also provide meaningful disclosure.

The most formidable barrier to effective engagement with shareholders is the sheer volume of statutory-driven information that they are required to digest. It is not unusual for the statutory annual reports of large listed entities to run to 300 pages or more of detailed financial and accounting disclosures. Remuneration reports have also become long and complex documents, as more and more disclosure requirements are added in piecemeal fashion to the legislation.

Governance Institute also strongly supports the aims of integrated reporting (<IR>). The Institute itself has issued an integrated report for the past few years and is of the view that this approach to reporting is a work in progress that can be improved year-on-year.

While supportive of <IR>, Governance Institute is of the view that it should continue to be voluntary. There are particular reasons for why <IR> is moving at a faster pace in other jurisdictions than in Australia, the key one being the challenges faced by directors in providing forward-looking disclosures.

If companies are required to detail strategy and also the risks attached to achieving that strategy, they are moving to disclosure of outlook. If directors are releasing prospective information, issues of personal liability arise. Directors are subject to statutory and common law duties which require them to act with reasonable care and diligence and in good faith in the best interests of the company and for a proper purpose. A defence may apply to decisions taken by directors in relation to breaches of care and diligence but it is not available where the process leading up to the decision is defective (such as where the decision is made on the basis of clearly inadequate information). Providing forward-looking reporting means that the information provided could well be based on inadequate information, given that circumstances can change rapidly. This in turn exposes directors to actions against them, including class actions, which are becoming increasingly prevalent. Indeed, the majority of class actions in Australia have been concerned with disclosure. Class actions are also, at present, unregulated in Australia.

Furthermore, at present, a 'safe harbour' from liability for directors and executives has not been adopted in Australia, whereas other jurisdictions, such as the UK, have specific safe harbours from liability in place for disclosures made in operating and financial reviews.

There are important questions relating to director liability for forward-looking statements and risk-oriented disclosures that need consideration in Australia. The current liability framework is sub-optimal and can generate inappropriate incentives and harsh outcomes for conduct that is otherwise fair and reasonable. However, it is also important that any regulatory framework continue to protect investors.

While we appreciate the work undertaken by the Australian Institute of Company Directors (AICD), Dr Robert Austin and yourself in seeking to develop alternatives to the current business judgment rule and a due diligence defence in relation to forward-looking statements, the members of Governance Institute do not support these proposed alternatives. Each has been rigorously appraised by Governance Institute members, and each raises significant issues of concern.

We remain of the view that consideration of a due diligence defence in relation to forward-looking statements and risk-oriented disclosures should take place and that it needs to involve all stakeholders. To this end, we have convened a Roundtable to be held on 5 April to facilitate a robust discussion. Importantly, we need to see if we can achieve consensus on the part of all stakeholders that a safe harbour is needed — without such consensus reform will not be feasible.

Until these matters have been resolved, Governance Institute does not believe that further work should be undertaken to determine whether <IR> should be adopted in Australia on an 'if not, why not' basis in the ASX Corporate Governance Council's (the Council) *Corporate Governance Principles and Recommendations* (Principles and Recommendations).

Following a comprehensive review in 2012 and 2013, the 21 members of the Council agreed that it was an appropriate time to issue a 3rd edition of the Principles and Recommendations. The 3rd edition was issued in 2014. The references to 'financial reporting' throughout the Principles and Recommendations were amended to refer to 'corporate reporting' instead, reflecting the trend towards greater reporting on non-financial matters. However, the Council was of the view that it was inappropriate to introduce commentary concerning <IR>, given that the <IR> framework had not been finalised at that time, and in light of the issues concerning director liability set out above as well as the recent introduction of ASIC's Regulatory Guide 247 on the operating and financial review.

The Council was of the view that it would be timely to review either commentary or 'if not, why not' reporting in regards to <IR> when a 4th edition of the Principles and Recommendations is under discussion in the future. Governance Institute continues to support this approach.

Governance Institute strongly supports a review being undertaken of the total sum of mandated corporate reporting that is sent to shareholders, as an audit is necessary before streamlining can take place. We consider that this is best undertaken by The Treasury, or through its existing body the Financial Reporting Council, or the creation of a separate body or task force. Irrespective of the institutional arrangements, any review of corporate reporting requirements needs to consider not just financial reporting requirements but all statutory requirements.

Yours sincerely

A handwritten signature in black ink, appearing to read 'S. Burrell', with a long horizontal flourish extending to the right.

Steven Burrell
Chief Executive