24 August 2015

Dr Kathleen Dermody
Committee Secretary
Senate Economics Legislation Committee
CANBERRA ACT 2600

By email to: economics.sen@aph.gov.au

Dear Dr Dermody,

INQUIRY INTO FOREIGN BRIBERY

Thank you for your letter of 14 July 2015 inviting ACSI to make a submission to the Senate Economics References Committee's current Inquiry into Foreign Bribery.

About ACSI

By way of background, ACSI is a collaboration between 29 Australian profit-for-members superannuation funds and 6 major international pension funds. Through ACSI these institutional asset owners exercise their collective ownership rights to improve the management of environmental, social and governance (ESG) investment risks and opportunities by Australian listed companies. Full details on ACSI and its research publications, policy positions and members are available on our website (www.acsi.org.au).

ACSI's Australian member funds in aggregate manage over $400 billion of superannuation assets on behalf of more than 8 million Australian fund members. Of this total, approximately 30% is invested in Australian listed equities, which translates to collective ownership of approximately 11% of the average ASX 200 listed company (and growing in accordance with the growth of the Australian superannuation industry generally). As fiduciary investors with such significant ownership stakes in Australian listed companies, ACSI's members have a vital interest in the adoption by those companies of high standards of probity and compliance in all areas of material risks to reputation and long-term shareholder value. Australian companies' exposure to foreign bribery risks most definitively falls into this category, and has consequently been a prominent theme of ACSI's ESG research and engagement agenda over recent years.

Focus and Limitations of Our Submission

Our main aim in making this submission is to provide some useful input into the development of "official guidance to corporations and others as to what is a 'culture of compliance' and a good anti-bribery compliance program", as foreshadowed in the Committee's Term of Reference numbered b. (viii).

This focus on best practice development stems from ACSI's experience over recent years in engaging with major Australian listed companies on their exposures to bribery and corruption risks, and on the mechanisms those companies need to have in place to improve the confidence of investors, regulators and other stakeholders that those risks are being effectively managed. Ancillary to this, we also make some suggestions as to how Australia's legal and enforcement framework might be better harmonised with those of key international jurisdictions to which Australian companies (and hence investors) are exposed by virtue of the expanding geographical scope of those companies' operations.

We would like to emphasise that we do not have sufficient information or expertise to comment on any specific incidences of alleged foreign bribery that might be being explored by the Committee, or on the efficacy or otherwise of enforcement actions being taken by investigating authorities in those cases. Rather, our comments are focused primarily on the general management and disclosure practices that should exist among Australian companies that have a material exposure to foreign bribery risks due to the nature of their businesses and/or the particular geographic locations in which they operate.

A further important limitation is that our comments are generally contained to what can be gleaned from companies' public *disclosures* (or lack thereof) around their anti-bribery and corruption policies and practices. Whilst we expect that good disclosure should generally be an indicator of good practice in this area – and that an absence of disclosure generally signals an increased likelihood of transgression, particularly in higher-risk sectors and regions - our experience has taught us that this this is not always the case. Consequently, we would caution against over-simplifying the findings of ACSI's research as an automatic proxy for "good" and "bad" Australian companies in terms of their actual practices on the ground in their offshore operations.

Despite these provisos, we believe we can provide some useful input on the topic of best practice development for a better bribery prevention culture and compliance framework. ACSI believes this would be a productive area for the Inquiry to explore, with a view to improving Australian companies' resilience to this critical aspect of legal and reputational risk to companies and consequent risk to long-term shareholder value for our members and their beneficiaries. It is in this spirit that the following comments are made.

ACSI's 2011 Research on S&P/ASX200 Bribery and Corruption Risk Exposure

In 2011, as part of its regular thematic research program, ACSI commissioned a report from independent research group CAER on exposures to bribery and corruption risks and disclosure practices among Australia's top listed companies, represented by the S&P/ASX200 Index.

This research was catalysed by a variety of factors, including:

- The then-recent experience of widely publicised incidences of alleged foreign bribery and corruption involving prominent non-listed entities such as AWB and Securency;
- The significant expansion in the offshore operations of Australian companies, particularly in the extractive and construction industries, and in countries considered to be at high risk of corruption and bribery exposure under widely-recognised criteria such as the Transparency International (TI) Corruption Perceptions Index; and
- Significant changes in the international regulatory requirements to which many ASX listed companies were subjected in their overseas operations, in particular the UK's new *Bribery Act* 2010.

The resulting report, which we attach as Appendix 1 and which is freely available on ACSI's website, made a number of high-level findings including that:

- Whilst more large Australian companies were now expressly prohibiting bribery in their publicly-disclosed Codes of Conduct than had been the case five years previously, Australian companies still lagged their international peers in the UK, US and Europe on this measure (based on commonly-applied criteria across all of these markets assessed by EIRIS Research). For example, just 69% of ASX100 companies had a stated prohibition on both the giving and receiving of bribes, compared to 97%, 86% and 76% of the Top 100 Companies in Europe, the UK and US respectively.
- Around one third of ASX 100 companies, and half of those in the ASX101-200, made only brief, limited or no reference in their Codes of Conduct to internal implementation systems and processes for managing bribery and corruption risks.

- Despite their exposure to more stringent regulatory regimes and penalties in the key offshore jurisdictions of the US and UK, 35% of ASX 200 companies with actual operations in those markets (41 companies in total) had no stated policy that expressly prohibited bribery or facilitation payments.

Company Engagement Program and Outcomes

ACSI's 2011 research was used to select a prioritised list of nine ASX100 companies which were targeted for more intensive shareholder engagement discussions by ACSI on behalf of its members in 2012 and 2013.

This process was in turn folded into a more comprehensive collaborative engagement program co-ordinated by the Principles for Responsible Investment (PRI) in 2013-15, which covered 33 companies globally that were assessed as being at high risk of corruption, using similar criteria to the ACSI research, and included 5 Australian companies (all but one of which had already been identified in ACSI's research).

The specifics of these engagement activities, including the identities of the companies concerned, are not disclosed here, as they were undertaken in confidence. ACSI believes it is important to maintain this confidentiality to preserve the integrity and candour of its relationships with Boards and managers of major ASX-listed entities.

Nevertheless, at an aggregate level, we are confident that these constructive interactions between 'at risk' companies and their major institutional investors represented by ACSI (along with parallel initiatives by other investor groups at the time and since) have led to a general improvement in the quality of anti-corruption and bribery disclosures and management practices by major Australian companies over recent years.

For example:

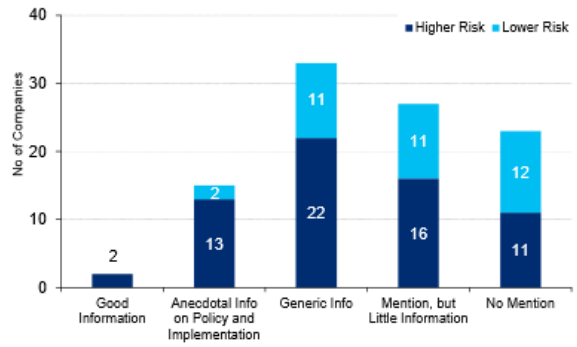
- Of the nine ASX100 companies on ACSI's original engagement list stemming from the 2011 research, all but one have now demonstrably addressed gaps in their earlier disclosure practices, whether it be through the adoption for the first time of whistle-blower policies, extension of Codes of Conduct to contractors and suppliers, prohibitions on facilitation payments, political donation policies, board oversight arrangements, or a combination;
- A similar picture emerges from the results of the international collaborative engagement through the PRI, which used a point-scoring assessment methodology based on Transparency International's 2012 TRAC (Transparency in Reporting on Anti-Corruption) criteria. Of the five ASX listed companies in this group, all of them improved their absolute scores between 2013 and 2015, (albeit that one of them – the same company that was a laggard in ACSI's earlier engagement program – remains in the bottom 5 companies globally in this research cohort).

At an overall market level, a similar pattern of improved disclosure practices has been noted in a research series by Citi Research, which has been producing reports on large ASX-listed companies' bribery and corruption disclosure practices annually since 2011.

The most recent (December 2014) version of this Citi research indicates a positive trend in the year-on-year bribery and corruption disclosure practices of 'high-risk' ASX companies, with 7 of 89 companies in that category now providing what is considered to be a 'good level' of disclosure (up from just 2 companies in 2013), and no companies in this category any longer failing to make any mention of the issue at all. As illustrated by the graphs below, this trend was evident in the most recent year-on-year comparison, and will hopefully see further iterative improvements in the current FY2015 annual reporting cycle.[1]

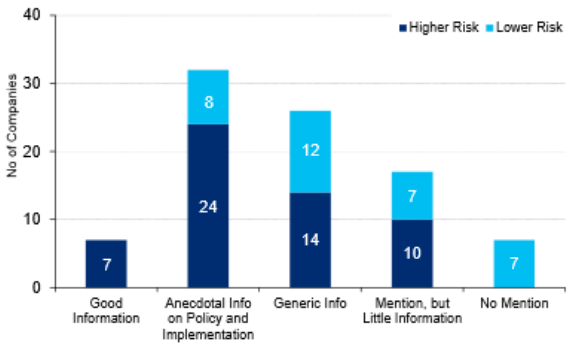
[1] Citi Research – Equities, *ASX Companies: Bribery & Corruption Risk – Analysis of the approach of 89 potentially "at risk" companies* (16 December 2014), p.10. Reproduced with permission. It should be noted that part of the

Figure 5. ASX Companies Bribery & Corruption Classification - 2013



Source: Citi Research

Figure 6. ASX Companies Bribery & Corruption Classification - 2014



Source: Citi Research

Adaptation of Investor Research Criteria to Industry Guidance

Whilst the above discussion confirms some improvement in disclosure practices by 'at risk' Australian companies over recent years, the fact remains that this has been from an unacceptably low base. More progress clearly needs to be made to embed better disclosure practices as the market norm rather than as an exception.

To this end, ACSI believes that a useful starting point for the development of official guidance for corporations as contemplated by the Inquiry's Terms of Reference, would be to distil some or all of the assessment criteria used in the investor and NGO-led research cited above to some form of industry best practice standard for companies that have a material exposure to foreign bribery and corruption risks.

The international collaborative engagement program convened by the PRI in which ACSI participated in 2013-15 (discussed earlier) was based on a series of 13 questions sourced from Transparency International's *Transparency in Corporate Reporting* (TRAC) Methodology (2012 edition). These questions probed full details various aspects of each company's anti-corruption programs, and were supplemented by a further 5 questions agreed by the institutional investors participating in the investor engagement group that more specifically addressed the company's related governance structures, risk management and supplier policies. Since the time of the PRI data collection TI has enhanced its TRAC scoring guidelines and included additional questions relating to important emerging issues such as tax disclosure and country-by-country reporting.[2]

In a similar vein, the Citi research series cited above used an assessment framework comprising 16 questions, divided into three main categories of *Commitment & Policy*, *Implementation & Management Systems*, and *Monitoring* (with a potential fourth category for future consideration, called *New Growth Areas*).[3]

In each case, the assessment of companies considered to be 'at risk' is based on filtering criteria that seek to limit the cohort of companies affected to those with a real and material exposure to the risks in question. For foreign bribery and corruption risks, these typically include a threshold score in the TI *Corruption Perceptions Index*[4] or similar framework to identify the most highly-exposed countries of operation, and a filters such as ESG research data or the *OECD Foreign Bribery Report*[5] to highlight the most

differences between the 2013 and 2014 results are due to some differences in the companies analysed; this was largely due to the decline in market capitalisations of some small mining companies from one period to the next.

[2] See *Transparency in Corporate Reporting: Assessing the World's Largest Companies* (November 2014), pp. 32-33.

[3] Citi Research (December 2014r) *op.cit*., pp. 28-29.

[4] 2014 Edition at http://www.transparency.org/cpi2014

[5] OECD Foreign Bribery Report (December 2014) at http://www.oecd.org/corruption/oecd-foreign-bribery-report-9789264226616-en.htm

exposed industry sectors, based on typical business activities and degrees of interaction with public officials. The specific filtering criteria that were used in ACSI's own commissioned report in 2011 are detailed on pp. 29-31 of Attachment 1.

These filtering criteria play an important role in ensuring that the disclosure practices addressed by investors and the management controls adopted by companies relate to genuinely material risks and are as specific as they can be to the company's own operations, governance and culture; i.e. that they don't become boilerplate 'checklists' to be slavishly filled in by companies and endured by investors for compliance purposes only.

Based on the above, ACSI believes that there should be abundant material embedded in existing investor and NGO assessments, international public agency guidance[6], and in existing examples of good disclosure by leading companies, to distil into an official guidance instrument of the type contemplated by the Inquiry's terms of reference.

In other words, the issues we are facing do not stem from a lack of information or thinking about what constitutes good disclosure and management practices – it is more a question of distilling what we already have into a workable guidance framework with generic application to all affected companies.

A variety of mechanisms could be potentially be used to auspice this guidance, ranging from mandated legislative requirements or regulator guidance, to formal industry standards or independent assurance mechanisms. In the case of listed companies, one obvious "home" for this enhanced guidance would be as a set of standards that was specifically referenced in the *ASX Corporate Governance Council Principles and Recommendations*. From an investor perspective, this would ideally appear under *Principle 7: Recognise and Manage Risk*, reflecting the reality that bribery and corruption pose direct financial risks to shareholder value and are not solely 'ethical' questions.[7]

One specific area of disclosure that should be addressed by this improved guidance framework in ACSI's view is mandatory country-by-country and project-by-project disclosure of payments to governments by extractives companies, in line with recent legislative and/or listing rule amendments in the US, Hong Kong, European Union and Norway since 2010, as an adjunct to the voluntary reporting by many companies and governments that occurs under the Extractives Industry Transparency Initiative.[8]

Recommendations:

That the Inquiry initiate the development of enhanced disclosure guidance for foreign bribery and corruption exposures Australian companies, based on the criteria established in existing investor and NGO assessment frameworks and existing examples of good disclosure practice by leading Australian and overseas companies.

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[6] E.g. OECD, UNODC & World Bank Anti-Corruption Ethics and Compliance Handbook for Business (November 2013)

[7] In the current 3rd edition of the *ASX Principles & Recommendations*, management of bribery risk is only directly referenced under *Principle 3: Act Ethically and Responsibly*, as a suggested item for inclusion in the company's Code of Conduct. This year, with the introduction of the new Principle 7.4 concerning disclosure of generic "material exposures to economic, environmental and social sustainability risks", we expect that some companies will already be lifting their disclosure in this area; however in keeping with the Inquiry's terms of reference our suggestion is that there should be a more specific guidance document developed for bribery & corruption exposure that could be referenced under this generic ASX Principle.

[8] This has been the subject of previous representations by ACSI and other investor bodies and NGOs, and we expect will be raised in detail by other respondents to the Inquiry. We have not gone into great detail in this submission given its overlap with other topical issues outside the realm of foreign bribery (e.g. the current international tax transparency debate) but would be happy to provide further details if this aspect is of specific nearest to the Committee.

This guidance should be developed in consultation with the corporate, regulatory and investor communities and in the case of listed companies, be formally referenced in the next update of the ASX Corporate Governance Council Principles & Recommendations.

That part of the improved guidance framework adopted in Australia should be a specific framework for mandatory disclosures of country-by-country and project-by-project reporting by Australian-domiciled extractive companies, as an adjunct to the voluntary disclosure framework adopted by many companies and countries under the Extractive Industries Transparency Initiative (EITI).

Beyond Disclosure

As noted at the outset of this submission, the research and engagement activities of ACSI and other investor bodies in the field of foreign bribery and corruption risk are inherently limited by being confined to material that is already in, or can readily be put into, the public domain.

While good public disclosure is generally a positive indicator, in that it signifies a commitment by the company to address the issue, many research projects in this field have discovered that seemingly-comprehensive stated policies do not always equate to the practical experience of good practices, or to the prevention of internal policy breaches throughout all corners of a large and complex organisation.

Conversely, in ACSI's own experience, we could cite examples of companies whose actual practices appear to be relatively good, but whose disclosure standards leave much to be desired (although this situation is obviously more easily remedied by simple disclosure improvements).

So ultimately, ACSI believes that improved disclosure frameworks such as those suggested above are only ever likely to be part of the answer to foreign bribery exposures of listed companies. These frameworks are clearly a *necessary* component of better management of bribery risks, but the evidence suggests that they will not be *sufficient*, on their own, to meaningfully address the full extent of the problem.

This brings us to the various options for reform of the legislative measures and enforcement arrangements for foreign bribery that are canvassed in the Inquiry's Terms of Reference.

At this stage, ACSI has not undertaken a comprehensive analysis of all of the relevant legal and enforcement options raised in the Inquiry's Terms of Reference, but the following points reflect our general view on the direction that we believe regulatory reforms should take.

- First, given that over half of Australia's leading (ASX200) companies (and increasing numbers of smaller listed and unlisted companies as well) are now exposed to much more stringent anti-corruption regulatory regimes in key markets of the UK, Europe and the US**, it makes obvious sense for Australia to align its regulatory framework and definitions of proscribed behaviors more closely to those peer markets.**
- On aspects where there is not a common approach between major peer markets (e.g. recognition or not of the legitimacy of facilitation payments), we suggest the Inquiry should err on the side of the more restrictive treatment (i.e. banning facilitation payments) unless a genuinely compelling and evidence-based case can be made for their retention by Australia in the face of clearly opposite trends elsewhere.
- **ACSI supports in principle the notion of creating an offence of "failure to create a corporate culture of compliance" as a means of establishing a positive obligation on companies operating in at-risk jurisdictions and lines of business, under Australian law.** The details of this offence and its linkages with other important mechanics of Australia's corporate regulatory framework (e.g.

director liability and business judgement rules) would obviously need to be examined in some detail, but in principle we believe this measure would provide a vital underpinning to the internal policy and public disclosure aspects of the issue raised earlier in this submission.

Recommendations:

That the Committee propose to the Government a harmonisation of Australia's legal and enforcement framework for foreign bribery with key international peer jurisdictions, in particular the UK and the US.

That an offence of 'failure to prevent a culture of bribery', or equivalent, be introduced into Australian law, in a manner consistent with the overall corporate and director liability framework.

Conclusion

ACSI trusts that the comments made in this submission and accompanying research material will be of assistance to the Committee in its review of this important area of public policy, corporate and national reputation, and risk to long-term shareholder value.

We will be following the progress of the Inquiry with interest, and would be happy to answer any questions the Committee may wish to raise about our submission. Please contact me or Paul Murphy, ACSI's Executive Manager Institutional Investment & Policy, at [redacted] should you require any further information regarding our submission.

Yours sincerely,

Louise Davidson
Chief Executive Officer

Attachment:

Research Report – *Anti-Corruption & Bribery Practices in Corporate Australia: A Review of exposure to corruption and bribery risks across the S&P/ASX 200* (Report commissioned by ACSI from CAER-Corporate Analysis, Enhanced Responsibility, October 2011)