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**JOINT STATUTORY COMMITTEE ON
CORPORATIONS AND FINANCIAL SERVICES**

Friday, 10 March 2006

Members: Senator Chapman (*Chair*), Ms Burke (*Deputy Chair*), Senators Brandis, Murray, Sherry and Wong and Mr Baker, Mr Bartlett, Mr Bowen and Mr McArthur

Members in attendance: Senators Chapman, Murray and Wong and Mr Baker

Terms of reference for the inquiry:

To inquire into and report on:

Corporate Responsibility and Triple-Bottom-Line reporting, for incorporated entities in Australia, with particular reference to:

- a. The extent to which organisational decision-makers have an existing regard for the interests of stakeholders other than shareholders, and the broader community.
- b. The extent to which organisational decision-makers should have regard for the interests of stakeholders other than shareholders, and the broader community.
- c. The extent to which the current legal framework governing directors' duties encourages or discourages them from having regard for the interests of stakeholders other than shareholders, and the broader community.
- d. Whether revisions to the legal framework, particularly to the Corporations Act, are required to enable or encourage incorporated entities or directors to have regard for the interests of stakeholders other than shareholders, and the broader community. In considering this matter, the Committee will also have regard to obligations that exist in laws other than the Corporations Act.
- e. Any alternative mechanisms, including voluntary measures that may enhance consideration of stakeholder interests by incorporated entities and/or their directors.
- f. The appropriateness of reporting requirements associated with these issues.
- g. Whether regulatory, legislative or other policy approaches in other countries could be adopted or adapted for Australia.

In inquiring into these matters, the Committee will consider both for profit and not-for-profit incorporated entities under the Corporations Act.

WITNESSES

BEERWORTH, Mr William John, Managing Director, Beerworth and Partners.....	16
COX, Ms Eva Maria, Senior Lecturer and Program Director, Faculty of Humanities and Social Sciences, University of Technology Sydney	44
DEEGAN, Professor Craig, Judge, ACCA Sustainability Reporting Awards, Association of Chartered Certified Accountants	98
FRANCIS, Mr Richard Daniel, Head, Australia and New Zealand, Association of Chartered Certified Accountants	98
FUNNELL-MILNER, Ms Linda, Director, Corporate ResponseAbility	27
HENDERSON, Dr Judy Isabel, Chairperson, Global Reporting Initiative.....	27
MacMAHON, Mr Rohan, Business Group Member, Amnesty International Australia.....	56
MATHER, Mr Erik, Head, BT Governance Advisory Service.....	67
MAYNE, Mr Eric, Group Executive, Market Supervision, Australian Stock Exchange; and Chair, Australian Stock Exchange Corporate Governance Council	1
NOLAN, Ms Justine Mary, Associate, Australian Human Rights Centre, University of New South Wales	56
SIDOTI, Mr Eric, Consultant, Compact Consulting	86
SMITH, Ms Rebecca, Advocacy Coordinator, Amnesty International Australia.....	56
VAN BEEK, Mr Harris, Consultant, Compact Consulting	86

Committee met at 9.08 am**MAYNE, Mr Eric, Group Executive, Market Supervision, Australian Stock Exchange; and Chair, Australian Stock Exchange Corporate Governance Council**

CHAIRMAN (Senator Chapman)—I call the committee to order. Today the committee will continue to hear evidence regarding its inquiry into corporate responsibility and relevant and related matters. This is the sixth public hearing of the committee. The committee expresses its gratitude to the contributors to this inquiry, including those who will be appearing before us as witnesses today.

Before we start taking evidence, may I reinforce for the record that all witnesses appearing before the committee are protected by parliamentary privilege with respect to the evidence provided. Parliamentary privilege refers to the special rights and immunities attached to the parliament or its members and others necessary for the discharge of parliamentary functions without obstruction or fear of prosecution. Any act by any person that operates to the disadvantage of a witness on account of evidence given by him or her before the parliament or any of its committees is treated as a breach of privilege. I also advise that, unless the committee should decide otherwise, this is a public hearing and, as such, all members of the public are welcome to attend. Of course, if any witness at any time wishes to give evidence in private they may request that of the committee and we would consider such a request to go into camera.

I now welcome our first witness, Mr Mayne, representing the Australian Stock Exchange. The committee has before it the Australian Stock Exchange submission, which we have numbered 124. Are there any alterations or additions you wish to make to the written submission?

Mr Mayne—No. I will be providing, by way of amplification, in my opening statement some material that is referred to.

CHAIRMAN—Fine. I now invite you to proceed with your opening statement, at the conclusion of which I am sure we will have some questions.

Mr Mayne—Thank you, Chairman. As you are aware, the Stock Exchange is involved in this area as a listed company and as a regulator of some 1,800 listed entities, with responsibility for monitoring the listing rules for those entities and also compliance with the corporate governance principles and recommendations. I am here today speaking in my capacity as a regulator with that responsibility for listing rules and also as Chair of the ASX Corporate Governance Council. In addition to the submission that the ASX has put in, I can provide the committee with an update of recent ASX and corporate governance council activity in this area. I believe the committee will be interested in the following points which will be covered: a brief overview of the council's review of its principles and recommendations, an update on the council's work on principle 7 and non-financial reporting, an update on the council's user survey announced on Monday of this week and, finally, an update on ASX's annual review of reporting by listed entities against the corporate governance council principles.

First of all, in relation to the council's review, we are currently reviewing all of the 10 principles and 28 recommendations. The council's review is designed to take into account developments including the CLERP 9 amendments, reporting trends to date, the need for any

additional guidance and the emerging debate about non-financial risk reporting. This review also encompasses the request to the council from the Minister for the Environment and Heritage, Senator the Hon. Ian Campbell, to consider ways to enhance non-financial reporting. This review is ongoing. The council will seek the views of the general public as part of this review, most likely in July 2006, and intends to complete the review by the end of 2006. The revised version of the principles and guidelines is likely to have an effective date of 1 July 2007.

On the work of the council on principle 7 and non-financial reporting: there are a number of ways in which the council could approach the issue of corporate responsibility, and the council has decided to consult publicly on a range of possibilities, including voluntary guidance in this area; however, it is too soon to predict the outcome. One issue is very clear when ASX looks at the whole issue of corporate responsibility reporting from the perspective of being the body charged with monitoring compliance with the listing rules, and that is the difficulty of monitoring disclosure in what can be quite a subjective area.

The council is concerned to look at whether it has a further role in respect of CR reporting and, if so, the practical ways in which it can assist companies in this area in the context of the principles and in a manner appropriate for the Australian market, where there are a large number of smaller companies. The council is anticipating releasing a consultation paper on this issue next month, in April. This paper will seek feedback from the market to assist the council's consideration of the role the council could have in this area. The council will request feedback on two separate issues in its consultation paper: one part of the paper will deal with reporting against principle 7, which covers material financial and non-financial risk reporting, and the second part of the paper will look at what role there is for the council in respect of other non-financial reporting.

In relation to the council's user survey, at its March meeting, held on Monday of this week, the council discussed and released key findings of its user survey. The survey was aimed at understanding the relevance of corporate governance disclosure to the investment and analyst community. The survey was undertaken between 22 November and 9 December 2005. It yielded a sample of some 729, of which 355 were private investors, being members of the Australian Shareholders Association, and 374 represented organisations and professionals.

The key finding of the survey was that 80 per cent of private investors and 75 per cent of organisations and professionals surveyed used corporate governance information in analysing or reviewing equity investments. When prompted to suggest ways in which corporate governance reporting could be improved, the main suggestion was around clarity of the reporting that is being provided by companies. Last Monday, the council issued a media release on the key findings of the survey, and I understand that the committee has been provided with a copy of this press release. We also have a five-page summary document which goes into a bit more detail around the survey. I can give that to the committee, perhaps at the end of this session.

Finally, in relation to an update on ASX's annual review of annual reports for 2005, ASX reviews annual reports as part of its monitoring compliance with the listing rules. This is the second year we have undertaken this review. ASX currently is involved in reviewing the annual report disclosures of companies that reported as at 30 June 2005. The results of this review are still in the preliminary stages and are only indicative at this stage. However, once again the results overall are quite positive. Initial indications are that there was a higher overall average

adoption rate of the recommendations for the whole market in 2005 than in 2004. As part of this review, this year ASX has also noted corporate responsibility reporting trends. When the review is completed, these trends will be taken into account in the governance council's review of this area.

I thought it might be helpful to share with the committee some of the preliminary results of our review to date. As I said, this information will help provide an understanding of how companies are currently using the corporate governance framework to assist in their reporting. It is also worth bearing in mind that the corporate governance framework is not currently intended to be used for reporting under the label 'corporate responsibility', so the review has captured reporting which is entirely voluntary under that label. We have reviewed some 696 company reports to date, of a total of around 1,300 companies which lodged reports by the 30 June deadline. This review only captured information in the annual report, not, for instance, particular information that may be found on company websites. Therefore these figures should not be used as a proxy for the extent of this type of reporting, as many companies report in other areas by way of either a separate report or the company website itself.

We found that the terminology used by companies in their reports to date comes under five basic or broad headings: (1) corporate responsibility, (2) corporate social responsibility, (3) sustainability environmental reports, (4) community reports and (5) people reporting, such as employee reporting. Of these 696 companies, 76, or 11 per cent, have included reporting which falls within one of these categories in their annual report. Thirty-four of these companies, or 44 per cent, have reported in the context of a specific principle, most commonly principle 7, which recognises and manages risk; principle 10, which recognises the legitimate interests of stakeholders; and principle 3, which deals with promoting ethical and responsible decision making. A number of these companies are reporting against multiple principles. For example, a company may have included sustainability reporting in the context of principle 10 and corporate responsibility reporting in the context of principle 7. As noted earlier, these results are only indicative at this stage. However, they demonstrate that it is currently possible for a company to voluntarily report this kind of information in the context of the existing corporate governance council framework.

ASX will release the results when it completes its review when the remaining 500-odd companies lodge their reports. To the extent that the council decides it has a role in encouraging or providing guidance in relation to this reporting, this will be considered when we have the benefit of taking into account the results of our consultation paper, which I said earlier is due to be released next month. That is all I would like to say by way of an opening statement.

CHAIRMAN—One of our witnesses yesterday was Dr Gary Johns. To quote from the paper that accompanied his submission:

It is my sincere belief that Corporate Social Responsibility is a discourse promoted by non-owner political interests wishing to use corporate wealth for their own ends. Some wealthy corporations promote CSR as a means of forestalling such political action, but also to enhance their appeal to employees and customers.

He goes on:

... the Committee should give no comfort to non-owner interests by changing the responsibilities of directors, nor should it lend legislative weight to any scheme that measures CSR, because this serves to undermine directors' duties.

Given your experience of corporate responsibility, what you have told us this morning and what is in your submission, is that a fair summation of the way in which corporate responsibility is being promoted and developed?

Mr Mayne—No, I would not say that. As I said in my statement, a lot of companies already are reporting under what might be now called corporate responsibility. I think the Business Council of Australia lodged, in their submission, a number of drivers that people and businesses use for corporate responsibility. From my experience, businesses use corporate responsibility initiatives and report against those essentially for business reasons. In relation to people initiatives, if a company is reporting on the initiatives it is taking regarding equal opportunity, occupational health and safety or activities around staff, they do that for a business reason and to make sure that they are attracting people into their workforce so that they can have the best people to do the work for that organisation, which adds to the overall strength of the company and the business success of that individual, which in turn benefits the shareholders.

When you look at each of those types of activities, companies can generally find a business reason as to why they are doing it. I think that is the driver of the activity in this area, and it is also the driver for the reporting to the public and the shareholders as to why they are doing that. And you can do the same with the community and philanthropic initiatives. People and companies involved in charitable organisations provide voluntary support for staff to engage in those activities because that is the demand that they are finding from that part of their market and that market is their employee base, who essentially want to work for an organisation that is involved in giving something back to the community that the organisation might be taking out of it. I found that, in my previous life as part of a law firm, there was a huge incentive for the law firm to provide sort of pro bono initiatives and work because that was the demand that was coming from the target market they were looking at for the employees. That actually added to the strength of the business of that organisation because it enhanced their reputation in the market. The driver of CSR, why people and companies report on that, is essentially still a business reason, not necessarily because they may have some other outside motive.

CHAIRMAN—I know there are several, if not more, studies or research projects that have been undertaken into CSR, but a recent one that reported in the UK, undertaken by Professor Chris Brooks of Cass Business School, showed that the returns of the least socially responsible companies were 24 per cent higher than for the most socially responsible companies. What is your response to that research?

Mr Mayne—That may well be the case in the short term. I would like to know what the return is of those organisations in the longer term. Are there initiatives also aimed at achieving a long-term benefit? One could assume that there will be organisations that may be there to try to achieve a short-term gain, but the short-term gain does not necessarily lead to the long-term longevity of that organisation and its sustainability into the future. I think you will find that organisations that are looking at and reporting on these areas are doing so for the long-term wellbeing of their organisations as well.

CHAIRMAN—What is your view of the request by Minister Campbell for the ASX to consider the reporting?

Mr Mayne—Yes, Senator Ian Campbell approached us in September last year. It coincided with the time that the council was already working in this space—we started work on this in the middle of last year—largely around the issue of financial risk reporting and risk reporting under the guise of principle 7. Out of that work we found that, whilst the level of reporting by companies against the financial risk reporting was quite high, the level of reporting against non-financial matters was not as high and was probably around the 60 per cent mark. The working group at that time found that we probably needed to give more guidance to companies about what was expected under non-financial risk reporting and materiality around that.

Senator Campbell approached us, the council, in September to look specifically at the sustainability point and the long-term users of that and the framework within the context of recommendation 7.2. We took that on board. The working group that was looking into this issue also then took on board Senator Campbell's request. In December at the council meeting we decided that we would look into this issue in the context of both financial risk and corporate responsibility reporting. We agreed that we would then put out a paper for consultation to find out essentially what the investor demand is for this sort of reporting, what companies in the marketplace are reporting it, what their reasons are for reporting it, to what extent the market is driving disclosure in this area and, therefore, what role the council should have within the framework that currently operates and what guidance it should provide.

The paper that we will be putting out next month will be essentially in two parts. The first part will look at the continuing issue around financial risk and non-financial risk reporting in relation to recommendations 7.1 and 7.2. It will also look at what sort of guidance we can provide specifically around the recommendation 7.2 criteria. We will also look at separately in the same paper the whole issue of corporate responsibility reporting. As I said, that will go out in April.

We will get that feedback and, assuming that the feedback is, 'Yes, this is something that the council should take on board,' we probably have four options. The first option is a framework along the lines of the GRI framework. The second is an option providing guidance only within the existing framework around some of the principles that are being used—that is, principles 3, 7 and 10. The third option is that you would provide guidance and also have a reporting trigger, so we would require them not only to report against a particular area but to explain why they were not reporting, if they chose to do that. The fourth option, obviously, would be to do nothing at all and wait to see what the findings of this committee are as well as the report from CAMEC and, in the light of that, see what role the council should take on board. I think the point to bear in mind is that the council works within the existing legal framework—that is, under existing law—and, within that framework, has principles and guidelines that essentially work within that.

CHAIRMAN—It has been put to me that the ASX corporate governance principles have become a set of quasi-mandatory rules. Do you agree with that argument and, if that is the case, would incorporation of voluntary reporting standards, such as a GRI into the ASX framework, also become quasi mandatory?

Mr Mayne—I think as a generalisation the fact that we essentially have a set of guidelines and recommendations, and ask companies to report against those, means the trend has been that

people do regard that as a somewhat prescriptive set of principles and guidelines because they want to report against what the recommendations are, especially if you have to explain why you are not reporting. I think that leads to and promotes a concentration of effort around those sorts of guidelines. It also leads to reporting in a structured way. Whether or not that should therefore mean we have a design framework, especially for corporate responsibility, is, I think, a separate question. What we need to do in that area is to balance the desire to have a framework against the cost of compliance in relation to that sort of disclosure and also the impact that might have in terms of keeping the cost of capital low and the confidence that may well be instilled into the market we are running, bearing in mind that we are confined to essentially 1,800-odd listed entities.

Senator WONG—The argument is that this is quasi mandatory because of the ‘if not, why not’ formulation. It appears to me from the evidence that it is really more the market that essentially makes people feel like that. The signals are that if you do not do it people are going to ask why. So it is not so much the council coming down hard but that people think the market may respond to somebody choosing to do the ‘why not’ as opposed to doing it. Do think that is fair?

Mr Mayne—I think that is a fair conclusion. The fact that you are under pressure to explain why you are not doing it if you do not do it leads to people wanting to report on it. The concern would be that, with all forms of guideline reporting being prescriptive, rather than bringing about a culture of corporate governance compliance it would be just ticking the box.

Senator WONG—I understand that. I suppose it just seems to me that if people are concerned, as they feel they have to do it because the market expects it, it is a little bit of a circular argument. If the market expects it, maybe it is not such a bad thing.

Mr Mayne—Correct. We should always look to what the market forces are. At the end of the day, the investors will essentially be the people that measure a company’s performance in this area, and indeed in other areas, by the way in which they direct their investments.

CHAIRMAN—CPA Australia have published a recent report based on their research that notes that the absence of a common basis for sustainability reporting undermines its value to financial markets. What is your view of that finding?

Mr Mayne—I do not necessarily agree with that. As I said at the outset, companies are actually already reporting in these areas. Perhaps this corporate responsibility proposition being put forward is about the ‘corporate responsibility’ label, if you like—and it is providing a label or a framework under which existing companies are already reporting. In other words, it provides them with a framework, a tag or a hook by which they can put reports against people initiatives, community initiatives, ethical standards and philanthropic behaviour. So I think the term ‘corporate responsibility’ is something which is probably useful to Hoover up all of the other things that companies are already reporting against.

CHAIRMAN—In their submission to us, KPMG have argued that sustainability reporting should be included in the ASX principles of good corporate governance and best practice recommendations and that listed companies who do not issue such reports should be required to explain why they have not done so. They have also recommended that sustainability reports

should require the same process for approval and issue internally within the reporting entities as required for financial statements. What is ASX's view of that argument?

Mr Mayne—Essentially, that is the reason in part for putting out the consultation paper. It is to find out from the market what clarity the market is looking for. There seems to be a lot of uncertainty at the moment about what the term 'corporate responsibility' embraces, what the level of investor demand by investors is for reporting by companies under the particular framework and what the level of reporting is that is already occurring by companies, because the market is actually dictating that they report that way, and resources companies are a good illustration of that. The investor demand, what companies are doing and the clarity around the terms is what we at ASX, through the council, are going to the market to try to find out and get clarity on. In the light of that feedback, we will then determine what the role for the council and the guidelines is and what the structure is that should be put through the guidelines with the benefit of that feedback. In one sense, it is too early to reach a view. As I said at the outset, our role is to work within the existing legislative framework, and we have the principles and guidelines. Based on the feedback we get, we will determine what sorts of guidelines we will provide, along with the three or four options that I provided to the committee beforehand.

CHAIRMAN—I note from your submission that you say:

ASX's experience to date has been that the current legal framework appears to accommodate directors' regard for all stakeholders.

So you regard the current Corporations Law as sufficiently permissive?

Mr Mayne—Yes, we do.

CHAIRMAN—How do you resolve that in the light of the view expressed by James Hardie directors that they were prevented from making adequate provision for their employees because of their directors duties and their responsibility to shareholders?

Mr Mayne—I think what we are seeing through the reporting is that there is nothing under the current legislative framework which is preventing directors from taking up and reporting against initiatives such as corporate responsibility. We would see the existing framework as being sufficiently broad to cover the decisions that are currently being made by directors in this area, as I said before. You will find that, when you analyse the decisions or the initiatives that they are taking, there is always a link back to the business reason for why they are doing it. If it has that link they can therefore quite clearly said to be acting in the best interests of the shareholders of the company, notwithstanding there may be other stakeholders who might ultimately benefit in relation to that.

Senator WONG—So you are focusing on the reporting aspect as opposed to the more difficult legal issue to which the chairman has referred?

Mr Mayne—Yes.

CHAIRMAN—Again, I refer to Dr Gary Johns and the submission from Mr Bill Beerworth, who we are hearing from later today. Their submissions and several others note the problem of

friction between some shareholders, particularly retirees who rely on their investments for income, who do not approve of what they see as directors distributing what is essentially their private property through corporate responsibility activities—in other words, approving the spending of company funds on charitable or other donations or broader community projects—when these assets could be distributed to them as dividends and they could personally decide how those funds would be used. What is your response to that view?

Mr Mayne—As I said earlier, the whole area around charitable and philanthropic activities is to analyse why the companies are making those donations and participating in that area. The reason would be that there is a community expectation but there is also that expectation essentially from the people who work for that organisation. They also would see that it is important that that organisation participate in giving something back to the community, especially where it has taken something out of that community.

The driver, therefore, for a lot of organisations in engaging in that is their overall reputation and their attractiveness to other stakeholders in the organisation, especially employees, because that is a target market they have. For the sustainability of the organisation and its wellbeing, you have to make sure that you are recruiting the best people. I think you will find that the rationale from the boards or the directors as to why they are allowing that sort of investment is that they can see the connection back to the business and the benefit for shareholders. If you find an example of where they are making donations which may go out beyond that, I think the investors or the market will be the ones that will measure that. Therefore, they will direct or move the organisation back into that business focus.

Senator WONG—I think you referred to the 6 March media release that you issued earlier this week. I was interested in the usage of annual reports that is disclosed in the user survey. It says:

Both private investors and organisations/professionals cite financial statements and annual reports as their most *important* source of information.

That is counter to some of the submissions or suggestions that have been put to me that the utility of annual reports is poor.

Mr Mayne—Yes, it is. In fact, whilst I would not say it was surprising, it was quite instructive to see the reliance that private investors and organisations and professionals have on the information that is contained in annual reports and the depth of information they are looking for.

Senator WONG—Did you give evidence about the review of the 2005 annual reports to examine the extent of sustainability reporting?

Mr Mayne—Yes, I did, in my opening statement.

Senator WONG—Yes, I thought so. What is the time frame on that again?

Mr Mayne—There is a corporate governance council meeting in May. The general rule is that we provide a report to the council of our findings. At the council meeting in May we would release the details of those findings.

Senator WONG—Can we go back to your evidence about essentially the four options that ASX might consider. I am not asking this to try to second-guess where you might end up; I just want to get a bit more detail on the pros and cons of each of the models. Can you perhaps go through them with us and tell us some of the merits and weaknesses of each of the approaches?

Mr Mayne—The first option that I talked about and which we would canvass is whether or not the council could recommend a standardised reporting framework such as the GRI framework. The council working group that has been looking at this particular option, I think it is fair to say, probably does not favour that as the option that should go forward. Whenever you have a framework like the GRI, the advantages of having a framework are, firstly, that whatever is measured ultimately is valued and ultimately therefore improves. Secondly, a framework does provide a structure and a degree of rigour which gives direction to those who might wish to report against it. Thirdly—and I think Senator Ian Campbell made this point—a framework has the benefit of enabling you to provide comparability across organisations, both within Australia and internationally. So they would be the advantages of having a framework such as the GRI.

Some of the disadvantages or things that would be of concern to the working group in its current thinking are whether or not all a framework of itself does is promote form over substance and a ticking-the-box exercise and therefore potentially a greenwashing of it. Also, even though it may well be provided as a voluntary framework, there is concern as to whether or not it becomes essentially just a prescriptive framework. The experience in relation to the principles has been that, even though it is a voluntary framework with an ‘if not, why not’ reporting requirement, as we said before, many companies do regard this as being prescriptive.

Senator WONG—The effect becomes—

Mr Mayne—Yes, the effect of it becomes potentially one of prescription. Also, I think it is probably too soon to really go into a framework. Our current thinking is that this is something that evolves over time. Also, there is the current diversity of our market. We have 1,800 listed companies. You have a very high concentration at the top end and a very long tail. The ones who currently tend to use the GRI framework are the organisations at the top end.

I think that, over time, as those organisations that adopt it require or command it from their suppliers—who may be people down the lower end of the chain—you may get an education function that will happen. The fact is that there is a very long tail. When you look at the costs of compliance that may well be involved, especially for the smaller entities, I think the current thinking of the working group is that it is not disposed to go out there and recommend a framework structure such as the one for GRI. That is the first option that we are looking at.

The second option is one of really just releasing guidance within the current framework that we have—in other words, more guidance about the sorts of voluntary reporting that could be taken under principles 3, 7 or 10. That certainly has its merits, because it will give greater clarity to the listed entities. Then we could see what the take-up of that is over the next 12 months to two years and, in the light of that, see whether anything further or more detailed is required.

The other option is to go into an ‘if not, why not?’ system straight away. Again we think it may well be too soon to embark upon that area. But, if the feedback we are getting is that that is

the way we should go, that would give an indication to the council that the framework that it should adopt will be in that context. The fourth option is not to do anything but to wait for—

Senator WONG—Yes. That was the ‘do nothing’ option.

Mr Mayne—The ‘do nothing’ option, yes. I suspect that that is probably not an option that we would embark upon.

Senator WONG—I would not like your chances, but that is your decision, I suppose. Has there been consideration of only requiring it of or applying it to certain companies, like companies of a certain size—that is, having a threshold?

Mr Mayne—That will be an option. No doubt again that will depend on what the feedback is and whether or not we do differentiate. There are examples where we differentiate already in terms of the top 300, and that is in relation to audit committees as opposed to the balance. We recognise that it is a structure where one size does not fit all, but it does provide flexibility and it is important in one sense to maintain a degree of flexibility as opposed to having different sets of standards at different levels.

Senator WONG—How would that flexibility be implemented?

Mr Mayne—It would be voluntary guidance or voluntary reporting.

Senator WONG—Can you comment on the GRI? We are hearing some further evidence about that today. You made a comment about one size not fitting all. What has been put to us—and I think one of our witnesses later today will probably be able to unpack this a bit more—is that the GRI is a reasonably flexible tool to take into account that clearly an extractive industry company and a service company can have very different issues they want to grapple with if they go down this path. I was interested to hear your view that one of the concerns is that it would be too standardised. Is it not the working group’s view or your view that there is sufficient flexibility within the GRI as a tool to cater for different sectors and different sizes of companies?

Mr Mayne—I think you can always, within a framework, provide a degree of flexibility. The concern that I or the working group—which has not reached a view on it—might have is just that, if you have a framework which applies to 1,800 companies, there will be a tendency for companies to want to report against it. You might say, ‘I will give you flexibility for you to decide,’ but people may say, ‘My competitors or other people are out there reporting against it.’ They may choose not to, but it may well require or force other companies to do something. When you look of the size or the depth of the reporting that may be required under that framework, there is a question of whether or not the benefit is being balanced off by the cost of doing it. You have got a long tail and you have got 1,800 companies. I think 1,200 of them would have capitalisation of \$100 million or less. At the very low end you can list on the exchange with a market capital of \$2 million. If you put in a requirement on them that they report against the GRI framework, which has a lot of ticking of boxes or reporting required, the costs of doing it could be quite substantial for those sorts of organisations.

Senator WONG—Have you done a cost assessment of what reporting against the GRI would mean for different companies?

Mr Mayne—No, we have not. For some organisations it may not be that great because, if they are already reporting under these various initiatives but are not giving it the label ‘GRI’, the additional costs of sort of hoovering it up under that particular label might not be that great, but those who are not necessarily doing it—

Senator WONG—In relation to smaller companies, would your view be that there is merit in voluntary guidance, given the cost impact?

Mr Mayne—Yes, there would be, but if you are going to have voluntary guidance you would have voluntary guidance across all of the listed entities.

Senator WONG—As opposed to different standards for different sizes. On the comparability issue, which I think is one of the stronger arguments—

Mr Mayne—It is.

Senator WONG—in terms of an assessment tool or a reporting tool, one of the themes across a range of sectors—companies and others—that come before us is: how do you extract value for what you are doing? Some companies do that because they see it as part of their core business—it is part of who they are and it is central to their core values. That is why people work for them and presumably why they do not go through a process of having a huge blue with the community that causes them problems. There is the question, to which Senator Chapman alluded—even though I would question some of the tenets of the research—of how you actually extract value for doing the right thing. In the absence of a reporting framework, don’t you think that becomes more difficult?

Mr Mayne—It does. Having a framework to provide that comparison is of benefit to those organisations. If they are in a competitive environment, they want to benchmark themselves or set themselves up against their competitors internally and also internationally and they have something which they can be measured against, it can provide a very good business tool. An example that comes to mind is this whole concept of being an employer of choice as something that companies or organisations aspire to. People develop a framework or a system of reporting that assists them in getting into the top 10 or indeed being categorised as the employer of choice. Why do they do that? They do it because that can help to provide a definite business advantage to them in their recruitment in the marketplace. Having a GRI framework can actually provide those sorts of benefits and that comparability.

Senator WONG—Do you have any other suggestions for the committee about how companies who are performing well in relation to sustainable behaviour or corporate responsibility can be recognised?

Mr Mayne—In terms of promoting corporate responsibility or just how they might be recognised?

Senator WONG—How we might recognise the good performers.

Mr Mayne—Nothing immediately comes to mind. Again, it is just really through the promotion of the concept of corporate responsibility reporting, whether it is by the government

or industry or organisations, as a concept and also of the recognition that might flow through to those companies who do make improvements in that area.

Senator WONG—I think more generally people say that what government should be doing and what this committee should be recommending is encouragement as opposed to doing anything. Tell us what you think we should do to encourage. It is not a trick question; it is an open-ended question.

Mr Mayne—Where the government can do something is more in, say, working with industry and promoting efforts of disclosure in this area. There are a number of organisations, like AICD and the Business Council, that can themselves promote disclosure in this area through their own education programs and by conducting seminars. Indeed, that includes any seminars that ASX might attend to report on or discuss this area and the whole continuing debate around and promotion of that area. That is one area in terms of education.

Government could, through joint efforts with industry at both federal and state level, promote awareness and therefore encourage companies to disclose in that area. As I said earlier, the council may have a role to play in this if it is decided that we should be providing more guidance. The fact that we put something into the guidelines specifically in this area of itself promotes disclosure. If listed entities are reporting against that they are essentially able to say in their annual reports, ‘We are indeed reporting and promoting ourselves under this particular area.’

Senator WONG—You mentioned in your opening statement or in answer to a question earlier the difficulty in monitoring disclosure. It is a good thing Senator Murray is here because he has been talking about how you audit these things. We have put that to some companies who already report, particularly larger companies. Their view is that they already audit, for the reason that, if they are putting it out there, they want to be able to justify it. So there are companies who already audit non-financial performance. Have you looked at that or do you intend to look at how they go about that?

Mr Mayne—We really just monitor whether or not they had made a disclosure. We do not necessarily pass judgment about the quality of the disclosure. That is essentially left to the market and the investors.

Senator WONG—I am sorry: I thought you were answering differently. You mentioned that, if we did have a new reporting regime, one of the difficulties would obviously be monitoring disclosure. I thought you meant qualitatively.

Mr Mayne—What I was getting at is that one needs to be clear about what you want companies to report against. If you go out there and say, ‘We want you to now disclose on corporate responsibility,’ unless you have got some pretty reasonable detail about what it is you want them to report against, it is difficult to monitor whether the disclosure that has been made meets the standard that has been asked to be put down from the guidelines. At ASX, we monitor whether or not they have made the disclosure; we do not pass judgment about the quality of that disclosure. If they do not make disclosure and they do not provide an explanation as to why they do not make that disclosure, we would make contact with that company to seek reasons as to

why they had not disclosed at all, not necessarily the quality of it. We would leave it to the companies and the market to determine how they assess their performance in that area.

Senator WONG—Could you have a bit of a hybrid system where there might be a general requirement to report or to consider these issues and perhaps a list of issues as guidance against which companies could report but where you essentially leave it up to individual companies or individual sectors to determine how they might do that?

Mr Mayne—Yes, you could. The material on non-financial risk guidelines under principle 7.2 provides the sort of guidance as to what one might put in there by way of example to report against where there is a material variation. Similarly, you could do the same under principles 3 and 10.

Senator WONG—Finally, were you asked a question about environmental liabilities?

Mr Mayne—I do not recall.

Senator WONG—I do not think Senator Chapman dealt with that. We have a submission from Professor Deegan who has recommended essentially better disclosure of information about environmental liabilities. He has suggested that the ASX consider forming links with state and federal environmental agencies with a view to ensuring that they are disclosed.

Mr Mayne—I think under principle 10 there is some reference in terms of stakeholders—not specifically. I think in terms of reporting—in principle 10—if we encouraged companies to report against their compliance and what they are doing in relation to our stakeholders—

Senator WONG—It is not so much compliance, as I understand it; it is talking about environmental liabilities and environmental risks.

Mr Mayne—If it is material confidential risk, that would be more likely to come in under principle 7.2. What we found with the level of reporting to date with the 2005 reports under 7.2 was that it is probably more in the field of environmental risk that there is a materiality threshold. That is where we found that sort of reporting. Also, rather than linking up with environmental authorities, I think we would say that the framework for the principles and guidelines is there for companies to report on environmental matters. If it is material, it will go into principle 7; if it is not, it can probably go under principle 10 or if you have got a broader thing around the ethical operations of the board, somewhere around principle 3. So we would say the framework—

Senator WONG—Is there any guidance around what might be considered to define ‘materiality’ in the context of environmental liabilities?

Mr Mayne—Not from us. No, it is left for the board to determine what is material and what they report against.

Senator WONG—Thanks very much, Mr Mayne. That has been very useful.

Mr BAKER—It is in your media release that the government uses survey key findings and methodology. When doing your survey regarding corporate governance, as the survey is basically on financial reporting, if you also included the word ‘social’ in there, do you believe that you would get different information? The majority of it is financial reporting: 84 per cent board structure responsibility, 69 per cent remuneration, and shareholder and stakeholder management.

Mr Mayne—The actual survey was around asking questions as to what use investors and analysts make of the corporate governance information that is contained in financial reports. That is essentially a summary of the response that came back. The main areas of interest were there, as disclosed in the press release. Financial reporting was top of mind.

Mr BAKER—When it comes to corporate governance, financial reporting does not trigger the mind for non-financial reporting?

Mr Mayne—No, it does not. We did actually ask a question. One of the questions we asked as part of the survey was very open-ended, as we asked the people what corporate governance information could be included in annual reports. So there was not a list of what could be in there—just that open-ended question. Of the 700-odd respondents we had, 510 came back and said, ‘Yes, we use that corporate governance information in the annual report.’ Of the 510, 187 chose to answer this open-ended question—in other words, give us some information as to what they would like to see in annual reports. There were 17 people who came back and said they wanted corporate responsibility information. So that meant that nine per cent of the respondents who chose to answer this question, or three per cent of the respondents who use the corporate governance section of an annual report, made reference to corporate responsibility.

In one sense, it is a relatively small number but, nonetheless, the fact that it was an open-ended question means that they told us, ‘This is what I would like to see,’ whereas, if you actually had a list of 10 issues and you put corporate responsibility there, you would be more likely to get people saying, ‘Oh, yes, I wouldn’t mind seeing some information about that.’ So I think that tells you that it is not necessarily front-of-mind in investors to look at the corporate governance section of an annual report to see what the company is doing about corporate responsibility. In one sense, we are saying it may be too soon to go straight into a framework which puts an obligation on listed entities to incur some substantial costs to provide a level of reporting without actually determining the investor demand for this sort of information. We did not specifically go out to find that; it was an open-ended question.

Mr BAKER—I understand and appreciate what you are saying. If there were another level there, from a social perspective—as in a very specific environmental or social impact in those areas; I know we cannot look into a crystal ball—it would be interesting to note the type of responses that might have been received.

Mr Mayne—The five-page summary will give you some additional information, but if you like I can take on notice giving the committee some other information that may come out of that survey.

Mr BAKER—Thank you very much. I also note ASIC’s corporate governance council. If I remember correctly, when the Group of 100 met with us in Melbourne, when asked what role the

government could play in assisting with facilitation, Tom Honan said, 'Excuse me, but just stay out of our road.' I am interested in your perspective on how the government can assist and facilitate the promotion and development of non-financial reporting. There seems to be major resistance.

Mr Mayne—I think there is a resistance to putting in legislation something that people would say that there is probably no need for. In other words, the existing law dealing with directors' duties and obligations is sufficiently couched to enable them to canvass and cover corporate responsibility. With respect to adding to the law, were the government to put a requirement in a legislative framework, there would be concerns as to what that may create. If you are going to put in a facultative provision or something that is mandatory, are you actually raising the bar in terms of the standards that may be required for directors? Are you going to create a greater tension between acting in the interests of shareholders on the one hand and other stakeholders who do not have a direct interest in the company on the other? Even if you were to provide a facultative provision, would that ultimately lead to the creation of a more mandatory type of reporting? I think with respect to the concern, 'stay out of my way', probably a more polite way to say it is that the existing law is adequate.

Mr BAKER—Following on from Senator Wong, we have had a lot of representation referring to GRI. Have you got anything further to add as to a possible framework?

Mr Mayne—Not over and above what I said when I was responding to Senator Wong's question in terms of the consideration we have given to the GRI. That is the current thinking of the working group. Whether that changed would depend upon what sort of feedback we might get out of the consultation as to whether or not, when people come back to us, they provide us with greater views about or support around a GRI framework and whether or not we would pick up that feedback as part of having a more detailed framework than may be provided within the guidelines.

Mr BAKER—Did you say that was June this year?

Mr Mayne—The consultation paper will go out in April and we will therefore expect to reach a view one way or the other around June.

CHAIRMAN—Thank you very much for your appearance before the committee and for your contribution to our inquiry. It has been most helpful.

Mr BAKER—Would it be possible to get a copy of the report when that comes down in June?

Mr Mayne—Certainly. Indeed we can give you a copy of the report from our review of the annual reports and also the consultation paper and the feedback we get from that. We said we would also liaise with CAMAC. I have had discussions with CAMAC just to let them know what we are doing and why we are doing it. It seems that there is going to be a confluence of activity around May and June for your committee, CAMAC and us.

[10.03 am]

BEERWORTH, Mr William John, Managing Director, Beerworth and Partners

CHAIRMAN—I invite you to make an opening statement at the conclusion of which we will have some questions.

Mr Beerworth—Thank you very much. My submission, in fact, to the committee was in the form of a speech quite some time ago. I thought for the assistance of the committee I would simplify and articulate my points, and I have given you my written statement. I will not read it all, obviously, in the interests of time. But if you want me to read it into the record I will do so with the first part. Would that be useful?

Senator WONG—Is this the statement you just provided us with?

Mr Beerworth—This is the one you just received, yes.

Senator WONG—I am sure we can simply receive it.

Mr Beerworth—I would be very happy if you would.

Senator WONG—I so move, Chair.

CHAIRMAN—It is moved that that be received.

Mr BAKER—I second the motion.

CHAIRMAN—That is carried. Do you wish to proceed straight to questions, in that case?

Mr Beerworth—Absolutely.

CHAIRMAN—Having read your submission—I have not, obviously, had the opportunity to read this statement—would it be fair to summarise your attitude to CR or CSR as somewhat sceptical, perhaps along the lines of what was presented to us by a witness yesterday, Dr Gary Johns? If that is the case, why do you suggest any change to the way in which company directors' duties are defined in the Corporations Law?

Mr Beerworth—I have not read Dr Johns's submission, and I am not sure I would describe myself as sceptical. I am probably—I do not know how one would apply labels—I would have thought, a very progressive or liberal conservative on these sorts of issues, although some of my colleagues on particular committees regard me as a dangerous radical, so it depends on where one stands.

Senator WONG—It is a problem when you are a progressive conservative: you can be either.

Mr Beerworth—I certainly take the traditional view that for nearly 150 years the concept of the corporation has served society extremely well, at least in capitalistic societies. It serves investors extremely well, particularly today where collective investments are so important. Individual investors, in fact, make very few decisions for themselves; it is mainly institutions, of course, which invest funds on their behalf, particularly given schemes like our superannuation in Australia. So we need to be extremely cautious in tinkering with something that already works. I do not necessarily advocate change at all. My view is that, if there were to be change, I would certainly not mandate anything under CSR. I would be prepared to allow what I would call a shield—that is to say, a business judgment rule—to be included in section 181, which would definitely protect directors who properly took into account issues of stakeholder interests and societal objectives within the broad rubric of ensuring that they are acting in the best interests of the company and on behalf of the shareholders.

CHAIRMAN—You say on page 3 of your submission that most shareholders to whom you speak are suspicious of corporate philanthropy and believe that such funds should be distributed to them as dividends and the like. What action is it possible for shareholders to take, particularly small shareholders, in that context if they do object to the way in which the directors and the executives of companies are distributing what they see as their rightful share of surplus funds to the company?

Mr Beerworth—In practical terms there is virtually no action that they can reasonably take. The cost of any attempt to restrain or any attempt to seek damages is inordinately beyond ordinary shareholders—certainly people who turn up at AGMs. So they basically have to complain at AGMs if they wish to, but they can do very little about it indeed because of the sheer weight of the corporation's money for defending actions. So it is really up to trying to get ASIC to bestir themselves in egregious cases, and that occasionally happens. But by and large I think corporations in Australia are responsible in the way they do act on behalf of the shareholders. It is only at the margin, I think—that is certainly where I see complaints at AGMs—that shareholders become very concerned about donations and what I would call corporate philanthropy.

Governments quite often talk expansively about corporations giving more back to the community and so on and so forth, but there is a taxation system, in my view, for those sorts of things. Corporations are much better off distributing their profits to the shareholders, and the shareholders, if they wish, can give all their money away. Some of the chairmen who are very keen on corporate philanthropy to particular causes can certainly give all of their money and all of their distributions, if they wish, to those causes.

CHAIRMAN—Given what is happening in that regard, it would seem that the current law is sufficiently permissive to allow directors to have regard to issues other than the interests of shareholders.

Mr Beerworth—I believe that to be correct; I think that is a correct statement of the law. I went through a large number of cases, many of which are from the 19th century. There are some interesting foreign cases on the subject in the current century. Most shareholders are not in a position to be able to do that sort of research and would not want to in any event. They do not have the libraries, they do not have the resources and they do not have legal training. The reason I suggested what is called a modest proposal in the paper you have before you is that I would

certainly not object to clarification in the Corporations Law of the extent to which directors may have regard to what I call external interests—stakeholder objectives, social objectives and so on. There is a resistance to that among some of my legal colleagues, and there is a certain irony in that because the directors' duties provisions of the Corporations Act are in fact merely a codification of the principles of common law at the time. If the common law now does permit directors and officers to have proper regard to external interests, then why not say so articulately within the statute, particularly to provide a defence if necessary—to ensure that if directors do have regard to those external interests then they have a shield if they are sued by shareholders or others?

CHAIRMAN—Could such a shield be subject to more misuse than the current provisions of the Corporations Law?

Mr Beerworth—I do not believe so. You will be familiar with section 156 of the UK bill; one could call a great deal of that, I suppose, cosmetic, but I do not think that is the intention. At the end of the day, that provision in itself—although it is not cast as a business judgment rule defence, or shield, as I put it—will have that same effect in UK law. It is pretty tentative, it is very roundabout if you read it, but it makes very clear at the end of the day that directors can have regard to external interests.

CHAIRMAN—Okay. Given your view on directors' duties and how they might be modified, can I ask you for your view on corporate responsibility or corporate sustainability reporting.

Mr Beerworth—On balance, I do not believe the time is right to impose particular reporting requirements, for several reasons. First, I do not believe there are yet appropriate standards and a reporting framework. I think those things ought to be considered very carefully first. You may well say that is part of the legislative process, and I would not argue against that. Second, most of the TBL reporting that I see, or the so-called socioeconomic and environmental reporting, is a little bit hypocritical. One has to believe that many of those reports must be written by public relations departments. Most are almost interchangeable, and I am not sure they really provide useful information to shareholders or the community. My third concern is the sheer weight of the reporting obligations we are putting on corporations and the amount of material that is being provided. These days, no ordinary shareholder can possibly begin to comprehend what is in an annual report, and those are already statutory requirements. We have the incredible irony that we have an annual report, yet there is invariably a concise report that goes to the shareholders because there is no way they can understand the annual report.

Now, I accept fully the notion that perhaps one should have full information somewhere, as they do in the United States with the registration statement—when a prospectus comes to the market, you file an enormous document with the SEC and it is on that that the company and the directors are judged. Separately, you put out a smaller prospectus. I understand that theory and in many ways I subscribe to it, but on an annual basis I myself know, having gone through corporate governance terms year after year for a number of companies, that there is already an immense amount of work and effort, and I am not sure that very much is produced at the end of the trail for the shareholders.

But I would not oppose reporting, except for those reasons. I think there will probably come a time in Australia when we do have proper frameworks and standards and we will end up with

some sort of, I hope, concise reporting in that area. It is not, of course, in the purview of your current inquiry but, frankly, I am much more concerned with seeing a proper management discussion and analysis of a corporation's performance. We do not really have that yet in Australia; that is more common overseas, such as the UK's OFR and so on. Those are areas that I would like to see examined in due course.

CHAIRMAN—Given your comments that, in your terms, there is not yet a proper reporting standard and, from what other people have described, there is an absence of a standard reporting framework, how seriously do you think the financial markets currently take the sustainability reporting and the corporate responsibility reporting that is provided by companies?

Mr Beerworth—I think that is a very good point. I think that by and large most of those reports are not taken terribly seriously. The reason, as I mentioned, is that most of them seem to be self-serving and to be public relations productions, by and large. That is not true of all companies; there are a number of companies that generally believe that they are somehow getting a competitive advantage out of putting forward progressive-sounding reports about taking into account society concerns about motivating employees et cetera. I think that is quite sincere, but I do not think the market takes it into account enormously. They do much more overseas. As you know, there are sustainable reporting indexes in some areas. There are many funds that rely on sustainability. I think ethical funds take it very seriously but as yet in Australia I do not think we have really reached that point.

CHAIRMAN—What do you think it is that has been driving corporations towards corporate responsibility activities and reporting? Is it enlightened self-interest; do they see it as a way of building their brand? Or is it pressure from particular groups to which they are responding?

Mr Beerworth—I think it is both those things. Corporations are members of society. Society has changing concerns as time goes on. I do not think there is any doubt that global warming concerns about sustainability and the environment et cetera are at the forefront today more than they have ever been. Corporations realise that they need to respond to them and that if they have antediluvian views and merely concern themselves with making money, or appear just to make money, it will offend a number of investors, their employees and so on and so forth. So it is a progress through society. The real issue at the moment is how sincerely and seriously many of the corporations take it.

Senator WONG—Mr Beerworth, I enjoyed your submission very much. It had lots of literary and cultural allusions through it. I want to focus on a very narrow point, about your suggestion of providing shields. Would you consider looking at the evidence of Professor Redmond, who appeared yesterday, if the committee were able to provide that to you? He provided an alternative formulation around how you might introduce essentially a shield, but he looked at a different formulation in section 181 to the one you have provided. Would you have time?

Mr Beerworth—I would be delighted to.

Senator WONG—There would be relevant aspects of the transcript, I think, where he clarified which of the aspects of the five options he would propose. It would certainly be useful for us if we could have a look at what you thought about that.

Mr Beerworth—Of course. I only raised it as a kind of BJR because it is already, of course, in section 180 and, when introducing that provision, the Treasurer said that, if it was successful, he would introduce it generally.

Senator WONG—Yes, I read that.

Mr Beerworth—So it seemed to me a very simple way of introducing it. But that is not the only way it could be done, by any means.

Senator WONG—I think it is probably fair to say that Professor Redmond's suggestions are more interventionist than yours.

Mr Beerworth—Okay.

Senator WONG—But he does make reference to the UK provisions, so I would be interested to hear your views about that. One of the arguments against a safe harbour provision—which is essentially what the introduction of a business judgment rule in relation to stakeholder considerations would be—is that it would, in effect, become mandatory. As I understand the argument that has been put to us, it is this: if you can have regard, if it is made clear in the legislation, you may. Then, if you did not, the question will be why you did not.

Mr Beerworth—That would be a question of interpretation and the way the corporation kept its minutes and so on. Properly drafted, I do not believe that it is a concern. I certainly would not be concerned about it. I do not think anyone would seriously argue if the BJR in section 180 were also put into 181. It is part of the reason I was trying to put up what I genuinely meant to be a modest proposal, and I was not just thinking of Dean Swift. It seems to me that it is about the least that you can put forward without going too far, if you like.

Senator WONG—It is one of the lighter-touch proposals. Would you propose an amendment to 180(2) as opposed to amending 180(1)?

Mr Beerworth—That is section 180(2)?

Senator WONG—Section 180(2) states:

Business Judgment Rule

(2) A director or other officer of a corporation who makes a business judgment is taken to meet the requirements of subsection (1) ...

Mr Beerworth—I do not have the provision in front of me. I would be happy to respond to that.

Senator WONG—It just seemed to me that if we are amending the business judgment rule, wouldn't we want to put it in that section as opposed to 180(1), which refers to good faith and civil obligation?

Mr Beerworth—As a matter of drafting, I would frankly recast the whole of that provision, but you could make a separate business judgment rule which would be applicable to both provisions. Again, that is a question of detail drafting.

Senator WONG—One of the difficulties that I am struggling with—and I am grateful that you put this option before us—is that we have had a reasonably lengthy procession of business representatives who say: ‘We don’t want the directors’ duties changed. We can have regard to sustainability issues or external stakeholders within the current legal framework.’ That is fair enough. Whilst I have an open mind on that—and I think having any requirement to consider it is intensely problematic—I am less sure about whether having a safe harbour provision is not such a bad idea. One of our difficulties is that we have people saying: ‘Don’t change it. We can already do it.’ Then we have a very high-profile case—admittedly, only of a single company but one that obviously captured a fair bit of public attention, the James Hardie companies—where the argument put forward by the directors of that company was that their duties prevented them from engaging in the settlement for some considerable period of time. That has been put quite consistently by the chairperson. This committee is in a situation where a company has said for quite a lengthy period and has continued to indicate publicly: ‘We couldn’t do this. We couldn’t enter into this arrangement for settlement because our directors’ duties prevented us from doing so.’ I am paraphrasing so I am simplifying it. Then we have witnesses who say, ‘We can already take into account stakeholder considerations.’ It is almost like the arguments are not ad idem.

Mr Beerworth—There is a dichotomy. I would think there is a great deal of reputable legal view that the James Hardie directors could have done that which they said they could not do, but I have not examined that case in detail, I should say. I should have thought that under the current law—and I would be surprised if people like Professor Ramsey would not agree; in fact, I have seen his comments on that subject—they could have done it. Whether or not it is a convenient commercial defence, I do not know and I should not speculate on that. If one did provide what you call a ‘safe harbour’ then clearly they would have been able to do it, if that were properly drafted, and so that is certainly a reason in favour of what I would call a modest proposal. Yours might be slightly more immodest but that is a debate—

Senator WONG—I am not proposing anything.

Mr Beerworth—No. But it may be that someone needs a stronger provision of some sort. My concern is that I would certainly stop short of being mandatory at any given time.

Senator WONG—That is highly problematic. I agree with that. Professor Redmond made the point yesterday—which I am sure you will agree with—that lawyers tend to give fairly conservative legal advice. That is what you are trained to do. You try and make sure your clients are in the space where they are most likely to succeed if the matter is litigated. So, even if it is theoretically possible that the Hardie board could have done what they were being asked to do, if the preponderance of legal opinion is shareholder primacy—maximisation of shareholder wealth—obviously the conservative advice would be: ‘Don’t do it.’

Mr Beerworth—I suppose it might have been possible for them to take it to an AGM—I am not sure of which company—and change the constitution. But, again, I should not speculate on the James Hardie matter. I have not considered it in detail.

Senator WONG—That is fine. I would certainly be grateful if you could have a look at Professor Redmond's evidence.

Mr Beerworth—Of course.

Senator WONG—I would really appreciate that.

Senator MURRAY—I too like the depth and originality of some of the phrasing in your submission. It also, of course, discloses your long experience in these matters. I want to first ask you about the point you made that it is not just about corporate social responsibility but it is in fact about business social responsibility. As a committee we concern ourselves with Corporations Law. If you use the term corporatist, there are many institutions, if you like, which are corporatist in nature: unions, churches as well as business. If you think of the TBL, if the clamour has been for businesses to extend their view from the economic to the social and environmental, you could spin that coin around and say to the not-for-profit organisations—churches, charities and others—that they need to have regard to the economic, not just the social or environmental. In other words, with regard to small business, legal professionals, churches, unions as well as business—and they blend, as you have indicated—they should have regard to these matters, TBL or CSR or both, where they are large enough. If you are going to suggest that a formalised reporting process goes on, it needs to extend beyond corporations. That is a thought process I get as a result of your remarks. Is that what you were meaning?

Mr Beerworth—No. I do not think you or I would have the time to read the reports that would pour forth from the churches and the not-for-profit corporations we are talking about. I think the Americans make a very useful distinction in most of their statutes between a for-profit corporation and a not-for-profit corporation. Many states have statutes, and there is a good reason for that because they impose lighter or different responsibilities on not for profits. The trick, of course, is to define what is a not-for-profit corporation. But I would not, as you put it, invert the coin. I certainly do not see that as being part of the current inquiry.

Senator MURRAY—But as you know quite a number of major not for profits are incorporated and have the same obligations under Corporations Law as a business does. The question should therefore be: what is their stakeholder milieu? Would you be of the mind that the not-for-profit legislation and regulation should be separate from for profit?

Mr Beerworth—There is certainly very good reason why it might be. You would probably make another bifurcation as well—and, again, they do this in the United States where many provisions of the corporations acts around the country provide for what are called close corporations, as you know. There is again a lighter or lesser obligation on those corporations in some areas, particularly in reporting. Here, I am sure many of the submissions you have received talk about applying reporting standards to perhaps only listed companies or companies with certain capitalisation. That is really doing the same thing in a different fashion. I think in the United States they make very useful distinctions between for-profit, not-for-profit and close or small corporations. There is another one that is beyond your purview, and that is subchapter S corporations for taxation purposes. I think they are all very sensible distinctions, but some of them are beyond the scope of the current inquiry.

Senator MURRAY—The South Africans, as I recall, introduced close corporations in the early eighties as well. It may well be much more widespread than just the States and South Africa that I know of.

Mr Beerworth—There was a faint attempt to introduce some legislation here as well, but I think it did not go very far for lack of support. I think there is a bill, although I am not sure that it ever actually became an act.

Senator MURRAY—You see, I am not so sure that your remark that it is beyond the purview of this inquiry is correct. I think one of the things that you and others have raised is the difficulty of getting a grip on this area of CSR. That does to me indicate that you have to address what it means to organisations that are organised like a business and in fact have businesslike behaviour, even if a profit may not result.

Mr Beerworth—I apologise—I did not mean to tell you how you should interpret your reference.

Senator MURRAY—No, I did not take it that way.

Mr Beerworth—I just had not seen it as extending to where you are going. But, philosophically, I have great sympathy with what you are suggesting.

Senator MURRAY—Turning to another area, implicitly and intuitively I agree that shareholder primacy does prevail as the dominant principle in board and executive considerations, although I think that often that gets lost in the network of institutional and interest groups that dominate over the general shareholder. But, as you know, the Corporations Act does not in fact enshrine that principle. It enshrines the principle of the company, and ‘the company’ means stakeholders even in a narrow sense—employees, shareholders, suppliers and those sorts of things. When you remark that CSR or TBL starts to challenge that issue of shareholder primacy, would you be suggesting that in fact the law should make that principle explicit? One of the arguments—and Senator Wong was pursuing it with you—is, of course, to explicitly say in the Corporations Law that you should have regard to stakeholders and interests other than those specifically of the company. But, of course, you could go the other way, very narrowly, and say that you do not have to have regard to any interests other than a narrowly framed responsibility.

Mr Beerworth—At present, of course, section 181, apart from common law—and as I have mentioned, it is a codification of common law—requires directors and officers to act in the best interests of the corporation. In the UK you have probably seen the interesting comment by the committee that proposed section 156 of the UK bill—that is, if you like, the stakeholder interest provision—is quite meaningless, and so it is. But it is one of those wonderful phrases like something being ‘in the national interest’. It can be interpreted with the length of the chancellor’s foot, as the expression used to be. It can be long or short like a piece of string. Sometimes it is, of course, in the various court cases.

Many people deal with the particular provision, or courts often do, by looking at it in terms of the length of vision a decision maker should have when making a decision. People talk about a short-term result or a long-term result. If you read the cases carefully, my estimation is that, by

and large, when courts are saying that you can take into account what we call here stakeholder external interests, what the court is really saying is that, if you take a very long-term view, clearly matters such as corporate reputation, your shareholders believing that your company is acting properly and so on in society are very proper and they are in fact matters to be taken into account in the best interests of the corporation. I think it is in that big circle, if you like, that all of these things are swept up.

Senator MURRAY—Do you think it is appropriate for a director to make the obvious distinction, either in rules or in the law—I am less interested in the law because I can see problems there—between direct and indirect stakeholders or, to put it another way, internal and external stakeholders? By direct and internal I mean those that have a direct and immediate relationship to the corporation—such as employee interests, financiers’ interests and suppliers’ interests as well, obviously, as shareholders’ interests—whereas external are those more traditionally regarded as the social and environmental footprints, where there is an indirect relationship. Has there been much exploration of that distinction in the literature and in the examination of this issue?

Mr Beerworth—There has in a sense. People do not normally articulate it or formulate it in that fashion, but it is certainly taken care of in the fact that normally there is an immediate list of stakeholders, being employees, those directly involved in the corporation or in financing the corporation, those who may live adjacently and so on and so forth. Those are certainly what I would call direct stakeholders or what you might perhaps call internal stakeholders.

I did not quite finish my earlier response. The thought I had in the UK provision, and it is worth looking at, is that the committee deliberately left out the words ‘in the interests of the corporation’. Instead, they talk about the success of the corporation and say that the directors are entitled to take into account a number of things in order to ensure the success of the corporation. You can argue that that is substituting one vagueness for another, but that is what is done. In that provision you also see that they do identify and articulate the direct or internal stakeholders that you mentioned—employees, creditors and so on. They are specifically referred to, although not in the terms that you mentioned.

Senator MURRAY—My understanding of the jurisprudence is that it is quite clearly indicated that the board can have regard to direct or internal stakeholders. Let me give you an easy example. It may be in the short-term interests of the shareholders for large numbers of employees to be fired, but in the long-term interests of the company’s growth and its stability and success it may be in the company’s interests to give them a very substantial package of improvements to enable the company to grow. It seems to me that the jurisprudence has said directors can easily make those decisions. Where it has become a little less clear is in the external and indirect area. Is that broad understanding correct?

Mr Beerworth—Yes. I would certainly agree with that distinction.

Senator MURRAY—I want to move to risk. I think, and I should stress to you I have been involved in corporate life all my life—rather like you, I suspect—that the assumption that directors and executives properly evaluate risk, particularly in the longer term, is often misguided. In my experience it has been the case that risk has not been properly appraised. Since my entry into political life and my involvement with the work of the Auditor-General and the

public sector generally—I should emphasise I began my working life as an auditor—I have come to understand a great deal more about assurance or performance auditing, which is risk oriented, as opposed to financial audits. Business has not to date done a great deal to formalise risk or performance audits, although the use of consultancies often fills that gap.

My feeling is that CSR and its associated concepts in fact encourage directors to pay much more attention to longer term risk, because they have to foresee regulatory risk, legal changes, societal pressures and those sorts of things. In that sense I think CSR can make a positive contribution to companies, particularly those that risk social or environmental challenge to the success of the corporation. I am thinking of mining companies—of course, mines have a great effect on things—and companies that make potentially unsafe or dangerous products, which can range from alcohol to motor cars. Do you see CSR in that positive sense of increasing better risk assessment?

Mr Beerworth—Not really, although I agree entirely with your view about risk management. The identification, articulation and management of risk has come onto everybody's screen, particularly over the last five years, although it has been out there for the last 10 years or so. As you heard from Mr Mayne, ASX principles now require corporations to have risk management plans and so on. I think you will find a very rapid increase in interest in risk management in that I suspect we have already reached the point where directors may be derelict in their general duties under section 180, 'care and diligence', if they do not have proper and due regard to risk management—that is, the need to identify, articulate and prepare plans to manage risk.

Senator MURRAY—Would you include audits in that list?

Mr Beerworth—Yes. Audit is a part of it. But my point is this: why use CSR to indirectly achieve something that I would think, if I were sitting on your side of the desk, you could achieve more directly? It would be possible to include a provision if you wished to ensure that directors do take account of risk management and so on. We seem to be light-fingered, and properly so, in including new provisions in the statute. But, given that risk management has now become front and centre a very important concern, I would tend to do it directly rather than very indirectly, in a roundabout fashion, by introducing anything particularly mandatory about CSR.

Senator MURRAY—I will use two extreme examples because that is easy to do. It is my assumption, and I do not know because I have not examined the sector in the sort of depth necessary to be conclusive about it, that a James Hardie board or a British American Tobacco board of, say, 20 years ago would well have known the downsides and the dangers of their products but were highly unlikely in the absence of CSR—which was not about then; TBL was starting to be vaguely discussed—to have done a risk assessment for their shareholders in terms of the future value of the companies and how they could be affected by what were, essentially, changing social expectations. If there is a social expectation, it eventually becomes expressed in law. That is what happens: people get worked up and politicians respond. So if CSR had existed at that time I think there would have been that inclination to ask, 'What are the social or environmental effects of our products?'

Mr Beerworth—I would not call it CSR as much as societal concerns evolving over time. Let us take the example of occupational health and safety. It was not nearly as explicit or as determined 20 years ago as it is today. In New South Wales it has reached a high point, where

there is virtually no realistic defence for directors and acting reasonably does not even get you off the hook. You could argue that, over a 10- or 20-year span, society has become sufficiently concerned about occupational health and safety that it now places unreasonable demands on directors.

Senator MURRAY—If I can interrupt so that you can expand as you reply: occupational health and safety is what I would regard as being directed towards internal or direct stakeholders—namely, employees—with insurance-covered external liability, while CSR specifically relates to the indirect, to the external. So I am not sure that occupational health and safety fits neatly into what I am trying to describe.

Mr Beerworth—The point I was trying to make, badly, was that particular concerns about products, about employee health and safety, about the environment or about sustainability start at a certain point and grow into oak trees over time. They seem unimportant in the early days. And I think that quite often for directors, like human beings, their first reaction is denial and anger and a refusal to accept, if you like, that times are changing. In the case of unsafe products—let's go back to the Ford Pinto that used to explode; the tank used to rupture et cetera—it seems extraordinary, looking back on those things, that the directors or whoever was responsible at the time could not have understood much earlier what was going on and done something about it. The usual problem is that there is what psychologists call reaction formation: people do not want to accept the truth and so on.

Similarly, if you go back to the beginning of environmental concerns, in some of the famous cases like Love Canal et cetera, the people involved in throwing the most toxic substances possible into the rivers believed that it had always been done, and why shouldn't they do it? It took nearly a generation for people to change their views about these sorts of issues. You use CSR to deal just with those indirect issues. I think CSR goes beyond that; at least in my conception of it—

Senator MURRAY—It does, yes.

Mr Beerworth—it goes beyond that. But part of the problem, as you well know, is that the nomenclature is not at all clear in any event.

Senator MURRAY—Thank you, Mr Beerworth. That was very helpful.

CHAIRMAN—Mr Beerworth, thank you very much for your appearance before the committee and for your contribution to our inquiry.

Mr Beerworth—Thank you, Chairman.

[10.50 am]

FUNNELL-MILNER, Ms Linda, Director, Corporate ResponseAbility

HENDERSON, Dr Judy Isabel, Chairperson, Global Reporting Initiative

CHAIRMAN—Welcome. Do you have any comments to make on the capacity in which you appear?

Ms Funnell-Milner—I appear here in two capacities. I am the chair of the GRI stakeholder council, and I have a separate submission under the name of my company, Corporate ResponseAbility. I have been the sustainability manager for Westpac and National Australia Bank over the last five years and have developed at least five reports for those companies.

CHAIRMAN—Thank you. I now invite you to make an opening statement.

Dr Henderson—Thank you very much. We will take our submissions as read, but I would like to highlight a couple of points from our GRI submission. I would also like to give the committee an update on where GRI is since we put that submission in, because this is a very fast-moving process. At GRI we believe that the connection between sustainability performance of companies and shareholder value is about where the connection between corporate governance and shareholder value was, say, 10 or 15 years ago. That connection was not fully recognised but now, post Enron, WorldCom and HIH here in Australia, that connection is well accepted. We believe that in five years time the connection between good sustainability performance of companies and long-term shareholder value will equally be just an accepted reality.

We say that for two reasons. First of all, companies are increasingly being constrained by issues which I will put under the rubric of issues relating to sustainable development. The constraints that companies are facing now—and your previous participant outlined some of them—are increasing. Those companies which meet those constraints will certainly have a competitive edge in the future. The second reason we say it is that it is a matter of—and I know you were talking about this in the previous presentation—risk management. We believe that risk management can be viewed like an iceberg. You have the visible part of a company's performance—the financial performance—above the waterline, but below the waterline is the non-financial performance which is equally relevant for a company's long-term sustainability. If issues such as corporate governance, health and safety impacts, environment, employee satisfaction, stakeholder relations et cetera are not recognised and addressed, they can severely damage a company's performance and reputation.

This week, quite relevantly, the Centre for Australian Ethical Research based in Canberra has released a report on the extent to which Australian companies have policies addressing the issue of bribery and corruption. They have found that 51 of the ASX 100 have stated policies which address bribery and corruption amongst their officials, which compares with 92 per cent in the UK, 80 per cent in the US and 91 per cent in Europe. With AWB, it is a very interesting report that has come out now, and I can table that if you would like to see it.

Senator WONG—That would be useful if we could receive that.

CHAIRMAN—It is so ordered.

Dr Henderson—I will go through just a little bit on the history of GRI. It was established in 1997. The first GRI sustainability reporting framework was released in 1999. I will go through this quickly, and I can come back to it if you want me to. In 2002 we did a substantial update of the guidelines. That was released at the Johannesburg summit. This is an update on my submission: as of last night there are 791 GRI reporters in 55 countries around the world. The GRI guidelines are translated into nine languages. We have since 2002 embarked on an extensive structured feedback process globally to ascertain issues that people were having with G2. We have responded to those issues and through the last 12 months have been developing what we call G3, the third iteration of the guidelines. We have done that through the standard process GRI goes through—that is, the multistakeholder process. This is the important part of the GRI process. The process is as important as the product, and we can go into that in detail if the senators are interested.

With G3, just in summary, we are aiming to cater much more for investors and the capital markets. Thus, there will be more information on company strategy and analysis, more information on management information and more attention given to performance indicators. This is responding to the feedback we got through the feedback process. We will also be developing G3 in a digital format using XBRL technology, which will make for report readers the information much more accessible, more consistent and more comparable. GRI has been extremely well accepted by the SRI, or socially responsible investment, industry because it assists them very dramatically with the research they do on companies. Mainstream investors have been a little slower to come to the GRI framework, but now we are getting a lot more interested through the larger institutional investors. They are becoming much more involved and are exploring the value and the materiality of non-financial or sustainability information in their risk analysis of companies et cetera.

Briefly, the draft G3 guidelines were released in January this year. We are now going through a public comment period. We are conducting global consultations with 30 meetings, which we are calling ‘sneak peaks’, in 26 countries around the world, we will have had face-to-face contact with 2,000 people plus there are all the submissions that will come in on G3. So it really is an extensive multistakeholder consultation process. The response we are getting to this process is that G3 is a significant step forward from G2. There are issues and interest on the issue of relevance and materiality. Assurance continues to be an issue that creates a lot of interest, as are the reporting levels that we will be proposing with G3. The process now is that at the end of the public consultation period the document will be revised. This will go through the governance process of our technical advisory committee; through the stakeholder council, of which Linda is chair; to the board in July; and we will have a major launch of G3 in Amsterdam in October 2006.

CHAIRMAN—Thank you, Dr Henderson. Ms Funnell-Milner?

Ms Funnell-Milner—I will not add anything at this stage.

CHAIRMAN—We will move to questions. We have had a number of submissions—including from our previous witness Mr Beerworth and from Dr Gary Johns—that have noted the problem of friction between some shareholders. In the case of Mr Beerworth’s submission, he referred to retirees in particular who rely on their investments for income and who do not approve of what they see as directors distributing through CSR or CR activities what is essentially their private property in the form of profits, which would otherwise be distributed as dividends. I am wondering: what is your experience of how often that sort of conflict arises? Is the conflict mainly between retail investors and companies or is it also an issue that institutional investors raise with companies?

Dr Henderson—Maybe I could start and then Linda can add to that. I think the issue you are referring to comes down to a definition of what we regard as CSR activities. If the investors see their company’s profits being spent on philanthropic issues, which is part of corporate social responsibility, then that may engender this sort of response. Of course, CSR is much broader than that, and what we are referring to in the sustainability performance actually relates to the long-term shareholder value, which institutional investors, particularly pension funds, are extremely interested in because it is long-term shareholder value that they are interested in, rather than the short-term quarterly returns, which these issues do not relate to so much. The tangible benefits of good sustainability performance are a much more long-term issue.

Ms Funnell-Milner—I would like to add to that on the issue of philanthropy because there was quite an outcry last year after the tsunami donations were in the marketplace. There was quite a debate in the media about whether or not this was appropriate behaviour by corporations. Certainly that was coming from private investors and members of the Australian Shareholders Association. The GRI asks companies to report on their philanthropic activity. This does make companies examine what they are doing, in quite a structured way. The most important journey that a company should go on in terms of its philanthropy and charitable giving is whether or not it is connected to its main business purpose.

For the first time, companies are actually looking at whether their charitable works are connected to their main business purpose, or should they be giving money to things that are more closely connected. GRI does require companies to look at that. Certainly, where companies are unable to demonstrate a close connection between those programs and their main business purpose, shareholders become a little concerned. I would just like to add that there are many millions of dollars spent on marketing budgets inside corporations, on sport and on a whole series of things, but for some reason shareholders may not be concerned about that type of expenditure. That is actually not disclosed through corporate responsibility under the GRI; that is quite a separate issue.

With both companies—Westpac and National Australia Bank—there were some concerns that we did need to be able to demonstrate that nexus between the business purpose and what philanthropy we were involved in. I think that that strengthens the company’s position with its shareholders, so I think it is good for companies to look at that.

CHAIRMAN—In the letter attached to his submission, Dr Johns also said:

It is my sincere belief that Corporate Social Responsibility is a discourse promoted by non-owner political interests wishing to use corporate wealth for their own ends. Some wealthy corporations promote CSR as a means of forestalling such political action, but also to enhance their appeal to employees and customers.

In the first instance, the Committee should give no comfort to non-owner interests by changing the responsibilities of directors, nor should it lend legislative weight to any scheme that measures CSR, because this serves to undermine directors' duties.

What is your response to that evidence?

Dr Henderson—I disagree with that statement. I think it comes down to a company's responsibility in the 21st being recognised—I believe—to be broader than just to the shareholders. There is an issue of their relationship with a broader range of stakeholders and the community in general, which relates to a company's reputation. Companies have to develop a social contract with the community within which they are operating. I believe that is how it is in the 21st century.

CHAIRMAN—Is that a consequence of the need to build their brand, maintain their image, so in fact it is related to their profitability?

Dr Henderson—Sure. That is what I mean. It is certainly related to its reputation, its branding, its image. It is your relationship with a broader range of stakeholders, to use that word, in the community than just the shareholders.

CHAIRMAN—So it is enlightened self-interest in that sense.

Dr Henderson—Absolutely.

CHAIRMAN—If that is the case, there is not a need to legislate in this area.

Dr Henderson—GRI's position on whether reporting should be mandatory or voluntary is that we do not take a position on that. I am just looking from the position of my organisation. We are a multi-stakeholder organisation which has a broad range of views on the issue of mandatory versus voluntary reporting, so the organisation remains neutral on the issue. Having said that, we believe that the GRI framework adds value to both situations. In a regulatory system it certainly adds a consistent framework against which all companies would be required to report. In a non-regulatory system it provides best practice which companies may aspire to in their reporting practice.

Ms Funnell-Milner—In my submission from Corporate ResponseAbility I did in actual fact say that I did not agree with legislation in this area. I do think that there are enough mechanisms—I went through three or four in my submission—to achieve the same outcome without being prescriptive, without having it in legislation, at this stage. I do agree that the current directors' duties do enable directors to take into consideration stakeholders other than shareholders.

CHAIRMAN—That was going to be my next question. So you think the current Corporations Law with regard to directors' duties is sufficiently permissive?

Ms Funnell-Milner—I do. That is my view from Corporate ResponseAbility.

CHAIRMAN—Dr Henderson, are you of the same view?

Dr Henderson—Yes. I think it is, yes.

Senator WONG—I want to start with GRI. I was not clear about the 2006 version for public comment. When are you looking to finalise that version?

Dr Henderson—The public comment period finishes at the end of March, then we go through the process of refining the document according to—

Senator WONG—I am asking for the end point.

Dr Henderson—I think I mentioned at the beginning that it will be launched in October 2006, in Amsterdam. We already have the launch date and the venue booked.

Senator WONG—I am sure you will make it, then!

Dr Henderson—Which puts pressure on us, I have to say.

Senator WONG—I am not sure that we have the 2006 version as evidence before the committee as yet.

Dr Henderson—I can provide that.

Senator WONG—We can get it off the web, but if we can formally receive that, Chairman, I think that will be useful. Can I move that way?

CHAIRMAN—So moved.

Senator WONG—One of the things that has been discussed in the 2006 discussion paper or version for public comment is the four tiers of reporting. It looks at how you bring a company into the process of reporting. Can you explain the logic behind that?

Dr Henderson—I had a telephone call only yesterday morning to do with that issue.

Senator WONG—Then we will have very up-to-date evidence.

Dr Henderson—It is a very pertinent issue at the moment. It is a work in progress. There is not a general agreement on the number of tiers and what would be the criteria for each tier, but in general GRI's initial view was that a company's first report would be a very early report addressing some of the most important indicators in the framework, and then a company would gradually add indicators, add substance to their report, until they get to the higher level. Whether that is three or four levels is still being debated. What actually are the criteria for each of those levels is also not finalised.

Senator WONG—I presume the logic behind that is to do with giving companies time to build their capacity around these issues.

Dr Henderson—Absolutely. Also, we are not just looking at the top 100 companies. We are particularly interested in the issues relating to reporting by small to medium sized enterprises.

Senator WONG—Which is actually one of the questions that I wanted to ask.

Dr Henderson—We have released what we call High 5, which is a guideline for small to medium sized enterprises. We are operating in a number of developing countries. Most of the companies involved would fall under the SME rubric, so it is very important that we have a process that is not daunting for those companies so that they can actually enter it at an early level and progress through it. I am sure Linda would have something to add.

Ms Funnell-Milner—I will speak from my experience of developing reports. I developed the first and second Westpac reports. I also developed the first three reports from the National Australia Bank. For every organisation as they enter reporting it is a big decision by the board, and there is a journey that companies typically go on that includes the identification of where that data currently sits in the organisation. It is my experience that more than 85 per cent of the key performance indicators are already being collected inside an organisation. This is not a new series of information at all, because any company who is managing those intangibles actually does have that data. This particular journey starts with senior management and the board actually being comfortable about what goes into the public domain. No company will do a full report in its first year. In fact, the reports of Westpac, the National Australia Bank and even BHP Billiton are now sophisticated, but that has occurred over a three- to five-year period. The tiered reporting recognises that the first step is often a small step by companies. That is actually recognised, and it assists companies, senior executives and the board to feel comfortable about what goes out into the marketplace.

Senator WONG—I wish to go back to the SME issue. I am not sure if I have heard of High 5 before.

Dr Henderson—I can certainly get a copy of that for you.

Senator WONG—It would be useful if you could provide that to the committee. So it essentially looks at reporting requirements for SMEs. Is that correct?

Dr Henderson—It interprets the GRI framework for a smaller company. This was for the G2 framework, and we will of course be addressing that issue for G3.

Ms Funnell-Milner—High 5 is a ‘how to’. Whereas the guideline itself is a ‘what’, the High 5 document is a ‘how to’ document. I have spent some time talking to Australian Business Ltd, who are a business association of SMEs. They are actually looking at how they can assist small to medium sized enterprises in Australia to come on the journey. They are using that document.

Senator WONG—Can we talk about what other transitional arrangements as to capacity building et cetera can be engaged in. I think the tiered process is a recognition of that, as is the

'how to' documentation. What else can be done to support companies that want to take that first step and make the first report and then progress up the tiers?

Ms Funnell-Milner—In G3 there is a series of other modules that are coming forward, including education and awareness programs, that will help companies do that.

Senator WONG—Who delivers that training?

Dr Henderson—This is part of the new business model for the Global Reporting Initiative where we have the guidelines on one side and then we have a number of services that will be available. What we propose is that there will be an accreditation system. This has not been finalised yet, so this is still a work in progress. As for the accreditation system, GRI has not got the capacity—because we are a very small organisation—to do the training but what we can do is use the GRI brand as an accreditation process for education while working in partnership with education entities around the world.

Ms Funnell-Milner—That does include universities, MBA programs et cetera.

Senator WONG—Has there been any discussion with the Australian government about facilitating accredited training being taken up in Australia?

Dr Henderson—We have not got down to that level of discussion but we have certainly had extensive discussions with the Department of the Environment and Heritage about facilitating Australian companies' move into sustainability reporting and the GRI framework.

Senator WONG—But clearly it is not just environmental issues, is it?

Dr Henderson—No.

Senator WONG—Looking at this briefly, there is a whole range of risk management indicators against which you are suggesting people report—social performance and so forth.

Dr Henderson—At a federal level the DEH has been taking a lead role in this. We have also had extensive conversations with Family and Community Services. I am not sure what their name is now; I think it has changed. The GRI also has a sector supplement for public sector reporting. Both those departments are GRI reporters. DEH has produced its second GRI report and Family and Community Services has also produced a report. We are talking to both areas of government about the social and the environmental factors, but it is more current with DEH.

Senator WONG—If you could, please take your NGO or private sector hat off and put a government hat on. One of the things we are interested in as a committee—I certainly am—is what government can do to support and encourage companies to go down this path. I do not think many people have considered that in a lot of detail. We tend to have a lot of submissions which look at regulatory reform and a lot of submissions that are anti regulatory reform. It seems to me that government could potentially have a role in capacity building, resources guidance and policy development—the things government is probably better at rather than some of the micromanagement. Training is obviously one area. Facilitating the accreditation and training within the public sector would be another option. Would that be right?

Dr Henderson—Absolutely.

Senator WONG—Do you have any other suggestions?

Ms Funnell-Milner—Going back maybe seven or eight years, the government was very influential through its development of the Community Business Partnership program. It assisted the business community to understand about community business partnerships, regardless of whether or not our shareholders thought that they should exist. It was very influential, and that type of initiative from government could be very helpful in this instance across the other sustainability areas. Philanthropy is only one very small part of corporate responsibility.

Senator WONG—In terms of behavioural change it actually seems to be the least effective.

Ms Funnell-Milner—The community business partnerships?

Senator WONG—No. If you are serious about trying to get companies to go down the path of sustainability or corporate responsibility—whatever phrase you want to use—encouraging them just to give money does not seek to change any of the core business activities in the way that I think the GRI seeks to.

Ms Funnell-Milner—Yes. I was just suggesting that what came out when the government did put together a forum at which those things could be discussed was an agreed language. People suddenly understood the concepts and started to behave in a certain way with regard to understanding those things from a business perspective. I do not want more emphasis put on community business partnerships. One of the reasons I think Australia has been a little slow is that there has been great confusion about these other sustainability areas and the fact that it is not about philanthropy. I am thinking of an initiative where some clarity is given around language.

I would like to give another example. The Australian Greenhouse Challenge Plus program gave substantial weight and a lot of education to business around energy efficiency et cetera. It is only now, some 15 or 16 years later, that we have the energy efficiency opportunities legislation. We know that when companies participate in these types of voluntary initiatives companies they are seen as a leader and it gives them some credibility and advantages in terms of managing these issues. Those things can assist in the development of thinking.

Senator WONG—When you say you would like a forum where we get some agreement or consistency of language, what are you actually talking about? If we do not use the rubric of the community business partnerships, do you have any particular suggestions about how one might go about that?

Ms Funnell-Milner—I will give some more thought to it. I have read many submissions that have come before this committee that talk about there being so many doubts about exactly what corporate social responsibility is. There is a lot of different language, and this is part of the blockage in people picking it up, because they think it is still ill defined. I think just getting clarity around that in the Australian business community would really help to move it. Corporate responsibility is about business.

Dr Henderson—I do have an NGO hat here, but in other forums I work for the New South Wales government, so I do know the responsibilities of government in this area. Training and capacity building aside, which is a big area that government could be involved in, industry in this area of reporting is looking for a level playing field. That is why some areas of industry are quite supportive of a regulatory approach: it does mean that there is a level playing field. Here in Australia there is not a great appetite for a regulatory approach. So we could look at other forms of incentives—this is just looking at reporting—for companies to report.

I draw the analogy from the pollution controls here in New South Wales. I am on the board of the EPA. Rather than taking a mandatory approach, there are incentives given to companies to lower their pollution through lowering of fees et cetera. We could perhaps use a similar sort of economic instrument to encourage companies to report. The obvious one is some sort of tax mechanism. I am not sure that Mr Costello would be too happy with that suggestion, but that is an obvious one. There are mechanisms which government could use to ease the burden on companies for reporting by rationalising. They already have to mandatorily report on a number of different areas related to this. If—through a consistent form of sustainability reporting—some of that burden of other sorts of reports that companies have to do could be rationalised through this system, I think that would certainly be something companies would welcome.

Senator WONG—One of the issues that has been raised is the cost of reporting. Ms Funnell-Milner, you raised in an answer earlier that many companies already have the information. I wonder if you could comment on that a bit more fulsomely.

Ms Funnell-Milner—As Judy has described, companies do already collect the data that comes forward in a corporate responsibility report or a triple bottom line report. They are already collecting data on, for instance, their human capital. They understand how much training and development they do and what the cost of that is to the organisation. They know their attrition rates, they know how many people they employ, they know their graduate recruitment programs—they are managing those. Those are the key performance indicators that GRI asks for. It is a matter of finding the pathway for that information to come to the people who are developing reports. That does take quite a bit of time, depending on how sophisticated your report is.

There are two main costs to producing a report. Both of these have a fair amount of flexibility in them. One is whether or not you go to a published 80-page document. Obviously there are publishing costs for that, and there are design elements. Increasingly, companies are producing summary reports that may hit the highlights, and the main report sits on their website as a PDF. That is increasingly becoming the way large companies go, because they understand that different stakeholders want different levels of clarity around certain criteria, around certain key performance indicators.

The second largest cost to an organisation is if they choose to have it externally audited. Again, the cost is determined by who they get to audit it, what percentage of the report is audited and whether it has to be audited in more than one country. Obviously, companies are in control of how they go about doing that. The issue of tiered reporting does recognise that there are a whole lot of companies, including small to medium enterprises, that will not go down the auditing trail and, therefore, that cost will not be there for them.

Senator WONG—The chairman asked you a bit about institutional investors. I think you mentioned the SRI sector has taken up the GRI. I do not like to use the word ‘mainstream’ but, for ease of reference, is there an increasing take-up by mainstream investors in terms of the utilisation of GRI reports?

Dr Henderson—I will start off and I know that Linda will add to what I say. As I mentioned in my opening statement, institutional investors are becoming much more engaged with the GRI process and particularly with G3, and we have realised that we need to make the information more accessible to mainstream analysts when they are doing their assessment of a company. That is why the digital format—an XBRL format—which we are proposing for G3 will assist institutional investors. They are very interested in the issue of materiality and what matters to the financial performance of a company—the relationship between the sustainability performance and the financial performance. I would like Linda to continue, because she has been working with a small subgroup on this.

Ms Funnell-Milner—Prior to the release of the current draft G3, there was an international working group of mainstream analysts who specifically sat down and developed a series of criteria that they would need to allow them to look seriously at these non-financial indicators. Those things have been fed into the G3. But the analysts are continuing to comment and will comment right up until the release of the new standard. As a group of stakeholders, they are more interested in obtaining data that they can use to compare companies. They want it to be simple. They do not want to have to fight their way through a 90-page document to find out what the numerics of the key indicators are. This is partly why the XBRL format will just give them the highlights of the data, so they can immediately compare, within an industry sector, across companies. They want more clarity around time periods, the depth and scope of those indicators, and materiality—all of the issues that people are concerned about. So the GRI has taken into consideration both buy- and sell-side requests on this.

Senator WONG—Is there a lag between Australian investors and your experience internationally?

Dr Henderson—Do you mean in companies reporting?

Senator WONG—No. I mean the investors and whether there is actually less regard to this more nascent approach taken?

Ms Funnell-Milner—I have found that, in places that are ahead of Australia—for instance, Europe, the UK and some parts of America—the analysts who work for a company are more interested in this data than those analysts who work for the Australian branch of that company. I guess that is a journey that all investor companies have to go on.

Senator WONG—In the long term, in terms of access to capital, do you think that if we do not move down the path to becoming part of a more consistent reporting regime there is a risk in the future that Australia will miss out on access to international capital?

Dr Henderson—Let me go back a step, and I will be brief. If you look at financial reporting at the moment in terms of international standards, after 70-something years we still have not got an international standard for reporting. In this age of globalisation, companies like BHP

Billiton—in Melbourne, London and Johannesburg—need a consistent format to report in which is applicable in all jurisdictions. I think that Australian companies that operate internationally are very interested in a framework that has global application. So I do think that Australia will be lagging behind if we do not embrace a standard that is applicable globally.

Ms Funnell-Milner—Clearly we can see that the ASX, which came on board with their 10 principles, followed a global trend. That is because investors are concerned about being able to make intelligent choices when they invest their money.

Senator WONG—We heard from the ASX this morning, and as you are probably aware—you may be involved; I have no idea—they are looking at various reporting options on sustainability. Criticisms that they indicated had been put to them about the GRI as negatives in terms of its adoption were that it might be too prescriptive, that it was premature to go down that path, that it would potentially restrict diversity and, of course, the cost of compliance. I wonder if you are able to respond to that.

Dr Henderson—I think it relates to the previous question. If the rest of the world is going down that path, Australia needs to get on that train. I think that the global companies that are based in Australia would want Australia to do that.

Senator WONG—What about the ‘too prescriptive and restricts diversity’ criticism? In other words, different sectors might have different views about what they should report on.

Dr Henderson—The G3 will have a relevance test, where companies can actually look at the range of indicators and decide which indicators are particularly relevant for that company. As well as that, we have the industry specific sector supplements, which are additional sector specific indicators. We have heard that concern, and through what we are calling the ‘relevance test’, a company will be able to decide which of those indicators are particularly relevant for that company, and they would need to explain why.

Ms Funnell-Milner—As with the ASX corporate governance principles, if you do not report on a GRI indicator it is an ‘if not, why not’. So in actual fact it is exactly the same as the ASX.

Senator WONG—Would you be suggesting to this committee that it should be an ‘if not, why not’ in relation to sustainability reporting?

Dr Henderson—That is what GRI is suggesting.

Senator WONG—Yes, but in terms of Australian listed companies.

Dr Henderson—Yes, I would. For instance, some of the labour and human rights indicators are based on ILO conventions, which Australia is not a signatory to. In that case, a company could use that and say, ‘We are not reporting on this because the jurisdiction within which we work is not a signatory to these conventions.’ That is just an example.

Senator WONG—That is if somebody signs up to the GRI. What I am asking is: in terms of an ASX guideline, do you have a view as to whether or not it should be an ‘if not, why not’ test for publicly listed companies?

Dr Henderson—I do.

Senator WONG—So you would be supportive of that.

Dr Henderson—Yes.

Mr BAKER—Dr Henderson, could you describe the relationship that your organisation has with the major peak bodies in Australia: G100, Business Council of Australia, ASX, chartered accountants and CPAs?

Dr Henderson—Starting with the last one, we certainly have had meetings with the CPA. We have requested a meeting with the ASX and we have not been able to get one. We have not had a meeting with the Business Council of Australia. The World Business Council for Sustainable Development is on the board of GRI. Specifically, here in Australia, we have not had a conversation with the Business Council of Australia.

Ms Funnell-Milner—On the Business Roundtable, some of the members from the Business Council of Australia are GRI reporters. So GRI does not have to directly go to these associations—for instance, the CPA. There are people on the roundtable who are GRI reporters or who are organisational stakeholders of GRI. When the AICD was developing its submission to this committee, I sat on the working group for that. The view of GRI does come to the table through the experience of people who are actually reporting inside Australia.

Mr BAKER—It is interesting because the Business Council of Australia was one of the peak bodies which was actually showing quite a deal of resistance and yet some of their members, as you just stated, are GRI reporting.

Ms Funnell-Milner—That is true.

CHAIRMAN—There is a resistance to mandatory reporting, but you are not advocating that either.

Ms Funnell-Milner—No.

Dr Henderson—There is the ‘if not, why not’ issue, but we are not advocating mandatory reporting.

Mr BAKER—They were showing resistance to any type of reporting.

Ms Funnell-Milner—Yes. Perhaps I should give the example of the Australian Bankers Association. Clearly, there are three of the top four Australian banks which are now leading the way in sustainability and sustainability reporting. It is only recently that the Australian Bankers Association has started to look at that. I was part of Westpac and they did the first financial services report in Australia. The reason was that Westpac clearly saw it as a competitive advantage. You would not go to your industry association to lead in an issue that you thought was a competitive advantage.

Mr BAKER—There is quite a large difference of opinion that we have heard in a number of hearings. When you say competitive market advantage, can you give some examples of what is actually happening in that situation in Australia and also what is happening overseas—you mentioned the UK and Europe—that is relevant to the Australian company situation?

Ms Funnell-Milner—I think in the UK what has happened with OFR has created a level playing field. Any competitive advantage of the early movers in the UK has now started to be levelled out. In Australia, for instance, BHP Billiton, Western Mining Corporation and Rio Tinto in the early eighties realised that disclosure and transparency on environmental issues were going to be a competitive advantage for them. Even though the Mining Industry Association in Australia was not completely convinced of the benefits of that, those companies stepped forward anyway. What they were able to demonstrate was that, by managing those risks, they were managing their business to the benefit of their shareholders. I think banking is the same. Westpac would say that they believe they have a competitive advantage because they have been listed as the No. 1 bank worldwide on the Dow Jones Sustainability Index for five years now and therefore that attracts a competitive advantage in terms of investors and the way in which they are perceived.

Dr Henderson—I think, in summary, our experience with business associations is that they are actually behind some of the leaders within their industry sectors. We are relating more to those that are stepping out in front. We find that the business associations in all sectors tend to be further behind than the leaders within their sector.

Mr BAKER—So it needs the carrot approach, not the stick approach?

Dr Henderson—A business association has to cater for the spectrum within their associations, so of course they are going to be dragged back by those that are less enthusiastic about moving along this pathway.

Ms Funnell-Milner—The World Business Council for Sustainable Development in Europe are clear leaders as far as an industry association goes. In New Zealand, they have a New Zealand Business Council for Sustainable Development, and the US have one as well. Where those particular sustainability issues are dealt with by a separate body, you can see the difference between the normal business association and that particular business association. In Australia they are connected.

Senator MURRAY—Ms Funnell-Milner, you have worked with companies such as Lend Lease, Westpac and NAB. Tell me, what is the time frame that they report against? Those CSR reports I have read take a snapshot of where they are now. They will often go back some years to rate their progress—for instance, in greater energy efficiency or things they have done—and will quite often put targets forward. But in writing those reports do the writers try to arrive at some forward estimates, not in a target sense but in the sense of a comprehensive view of how it will be; and, if so, how far forward do they go?

Ms Funnell-Milner—If you begin from the premise that a sustainability issue is about managing a business line issue, then it is analysed and projected in the normal way, like any business issue.

Senator MURRAY—Well, I am not satisfied with that answer, and I will tell you why. And that is not a criticism of you. In the public sector, typically we have forward estimates of three years. Now and again, you get a terrific initiative such as the Treasurer's *Intergenerational report* which tries to look forward three or four decades—which is smart thinking, because policy has to relate to what you are trying to achieve. The forward estimates are quite detailed, and governments are measured against them.

I think one of the problems with both financial and non-financial reporting is that they do not attend to forward estimates in any way, and that in fact reinforces that short-term view. If you look at the typical financial statement of a top-500 company they report very well on the current year, as they should, and sometimes they report back a number of years. Commonly they do not—they might go back just one year—but they almost never put down forward estimates. I am quite sure the board and management have those concepts in mind, but it is my view that they do not want to be bound by them or pinned down by them. They do not want to generate market expectations or a market obligation. I think that leads to short-termism.

People are trying to connect CSR non-financial reporting to financial reporting. Yet CSR, I think, is and should be risk management orientated and should try to be precise about where a company is going. Companies tend not to do that financially. They tend to talk about targets. Obviously, if they are mining companies, they will talk about reserves and how much they intend to mine, but you will not see them making specific remarks in the out years, as we would talk about it in our sector. That is why I was not satisfied with your answer. I have not heard much in the presentations to us from practitioners such as you, or business people or academics, that looks at that particular issue.

Ms Funnell-Milner—I do not disagree with what you are saying. When you look at companies who are early reporters, as opposed to sophisticated reporters, you start to see a trend as to their ability to forecast the future in some sense. But they are also very careful about competitive issues: how much are they prepared to put into the marketplace that they may perceive to be early thinking in an area that is going to give them a competitive advantage?

While the key performance indicators in a non-financial report are a rear-view mirror—they are telling us about the past—it is an outcomes document in the same way that a financial report is. In the qualitative key performance indicators, we start to see the direction of management in looking at what the opportunities for sustainability for the company are into the future. But I do not disagree; they certainly do not go 10 years out.

Senator MURRAY—I do not want to say to you that the committee will do this, but let us say that the committee did recommend and it was adopted that somebody like the ASX took a similar approach to developing rules in this area as they have in the corporate governance world. I think one of the things they would have to examine—and I stress that I have not yet seen it examined in the material before me; I might have missed it—is forward estimates. Perhaps, if you have not thought about it much and have some further thoughts, rather than jumping in off the top of your head, you could send us a supplementary submission. If that is all right and you are able to find the time to do it, I would find that quite interesting. I am looking for two things. Firstly, I am looking for connectivity between non-financial and financial reporting, which tends to happen in public sector reporting, because we do both performance audits and financial audits. Secondly, I am looking at the time frame for forward estimates. I think historical reporting, to

some extent, is a lot better in CSR than it is in financial statements, because very seldom will you see a company give you a five- or 10-year look backwards as to how they have gone.

Dr Henderson—This is a new area and a developing area, and it is an area that we need to develop. I think that what companies are doing is looking at the internal advantages, and they have not quantified them and given forward estimates yet. They are looking at the internal advantages of reporting as opposed to the external advantages, which are always promoted in terms of reputation—that is, in risk reduction, cost reduction, efficiency gains, employee retention et cetera. I agree with you; those things are not quantified in terms of a forward estimate, and that is a very interesting direction which needs to be followed up.

Senator MURRAY—I will say this, and if you respond with a further submission I would be delighted: I talk to you this way because I have an investor's mind-set. Whilst I find this year's results and previous years' results very interesting, I am actually interested in the future, and yet I do not get much of the future in terms of financial statements, forward estimates or in the CSR stuff.

Dr Henderson—With respect, our whole view of the advantages of good sustainability performance and reporting against that performance is in terms of the long-term value.

Senator MURRAY—I understand that that is your objective; I am talking about present reporting—the current reporting that is available to Australian investors. That is what I am talking about, not what your objective is.

Dr Henderson—Point taken.

CHAIRMAN—In your submission, Ms Funnell-Milner, you say:

The achievements of companies with business practices that reflect embedded CR thinking and management attitudes demonstrate enhanced profitability. Yet a common fear is that such considerations would make a company less profitable.

I understand that there are some studies that show enhanced profitability, but I also understand that a very recent study was undertaken in the United Kingdom by Professor Chris Brooks of the Cass Business School which showed that returns of the least socially responsible companies were 24 per cent higher than those of the most socially responsible. Firstly, what is your comment on that?

Ms Funnell-Milner—I would like to see the parameters around which he looked at those companies and whether it was the short term or the long term. We all know that in the short term, this year and next year, companies who are heavily involved in corruption or anything else can be making a great deal of profit, but whether or not in five years time they will even still be around is questionable.

There was an instance—and this is an example—where Credit Suisse had a fund which they called the 'sin stocks' fund, because they believed that investing in companies involved in gambling, tobacco and alcohol would make you more money than not investing in those companies. In fact, the fund is now closed, because it was proven not to be true.

CHAIRMAN—Following on from that, to perhaps get a better handle on this: are you aware of whether any companies themselves have done serious cost-benefit analyses of corporate responsibility, in the sense of saying, ‘This is the cost to us of corporate responsibility, whether it be our philanthropic donations or the cost of doing more for the environment than we are required to by the basic environmental laws or more for our employees than is required by labour laws or whatever,’ and trying to assess what, if any, is the additional revenue that they have generated as a consequence of that?

Ms Funnell-Milner—My experience is that there are companies which are trying to do that, and certainly there are some studies overseas where they are trying to do that. We can definitely look at the cost of not managing these intangible risks, and there are some great examples—for instance, HIH. If you are not managing—

CHAIRMAN—HIH was more a case of straight-out fraud than of lack of corporate responsibility, wasn’t it?

Ms Funnell-Milner—Fraud is a cultural issue that—

CHAIRMAN—But fraud is illegal in any case.

Ms Funnell-Milner—Yes. I will give you another example. If you are a construction company and you are not managing occupational health and safety appropriately then there will be a cost for that. Your workers compensation will be more et cetera. In fact, the first stage that companies go through when looking at sustainability issues is: what are the cost savings they can make through eliminating waste within their organisations? If you have poor occupational health and safety systems then you are in fact adding a waste measure onto your insurance premiums, so managing that issue is about managing waste. So the first phase is: how much money can we save by being more energy-efficient, by being smarter about the water that we use, by using grey water? Not often enough do companies actually say: ‘Here is the minimum cost efficiency that we’re going to get out of this.’

I will also give another example, without mentioning any particular companies—though we have had probably four or five over the last few years. Where they have not been managing sustainability issues, it has cost them millions of dollars. And the issue of not managing ethics inside an organisation has been proven to cost companies millions. There are enforceable undertakings; there are major projects inside; boards collapse; they have to get new employees; their senior executives go—that has a huge cost inside an organisation, quite apart from reputation. And ethics is not an issue that can be triggered by materiality, so you actually do not know whether or not ethics is a material issue inside your organisation. There are some great examples right now. If you are delisted from the stock exchange, if you have a trading halt, they are all costs to an organisation which is not managing sustainability.

Dr Henderson—I will just add one point. There are a number of studies that can show lots of things. There are just two studies that we know of concerning the value relevance of sustainability reporting with respect to GRI. One study was done by Global Investor Communications and Lintstock, which compared GRI reporters against the S&P 1200 nonreporters. They showed that, in terms of the share price volatility, the GRI reporters showed marginally lower share price volatility. It was questionable whether that was significant or not,

but it was significant that the GRI reporters on average had a significantly higher profit margin with a marginally higher revenue growth than the nonreporters. So there are lots of studies that can show lots of things.

Senator WONG—Can I stop you there, Dr Henderson. I disagree with the view the chair is putting, so I will make that clear, but—

CHAIRMAN—I am asking a question; I am not putting a view.

Senator WONG—Implicitly putting, perhaps. It has been put to us that the reason a GRI reporter or a company that does report against sustainability does better is that it is a chicken-and-egg argument in the sense that only the profitable companies will do that in any event. In the context of the evidence you just gave about that study, do you want to comment on that?

Dr Henderson—It is the relationship between adherence to a framework of sustainability reporting and good management within the company. Of course there is a relationship between those things. Good managers want to measure what they are trying to manage and then they can report on those measures. I think there is a relationship there; I agree it is chicken-and-egg. I would just like to quote one other report that came from Business for Social Responsibility on reporting as a process. They researched companies using sustainability reports as a vehicle for communicating with employees. They said a number of companies had said that stakeholders with the most interest in social and environmental performance were their own employees. Employee retention was higher in those companies that demonstrated their adherence to corporate social responsibility principles, because they were proud to work for those companies.

Senator WONG—We have had a lot of evidence about that.

CHAIRMAN—As there are no further questions, thank you, Dr Henderson and Ms Funnell-Milner, for your appearance before the committee and your assistance with our inquiry.

[11.56 am]

COX, Ms Eva Maria, Senior Lecturer and Program Director, Faculty of Humanities and Social Sciences, University of Technology Sydney

CHAIRMAN—Welcome. We have your submission, which we have numbered 26. Are there any alterations or additions you wish to make to the written submission?

Ms Cox—No.

CHAIRMAN—We will move to your opening statement and then ask some questions.

Ms Cox—I did not very specifically address your terms of reference when I put the submission in, so I thought it might be worth while chasing through some of the points in the submission. Since I put the submission in, I have been involved in other activities which have fed back into that. I also serve on the UTS Council, the governing body, so I have had a bit more experience of being a director of a very large corporate entity. That is an interesting process because you get to sit on a board and watch how it works, particularly since that we are being told now to be more businesslike. One of the points I would like to make, having listened to the last stuff here, is that I am not here to say that my interest in corporate ethics or corporate social responsibility extends from the fact that I want corporations to make more money; I have always argued that corporations should be ethical because they should be ethical—not because it adds to their bottom line. I think it raises a very broad, general issue about what the role of corporations is.

If you assume that we created corporations and corporate law in order to protect the risks to individuals—and, if you go back and look through history, we did—by creating this fake entity which is supposed to mean the corporation is vulnerable to legal redress instead of individuals, it raises the interesting question about what sort of social and other responsibilities one should assume that this particular corporate identity has. One of the arguments I put, which does not make me particularly popular with some of the people who are making a living out of selling their services in the corporate social responsibility area—and there is a whole new industry out there—is that the object of this ought to be to say to corporations about their intrinsic rewards for acting ethically, ‘The fact that in many cases it happens to add to your bottom line should be a secondary consideration.’ I do not like the argument that if it does not add to the bottom line—and I think this relates to the chair’s last comments—you should not be ethical.

CHAIRMAN—Certainly not.

Ms Cox—Sorry?

CHAIRMAN—Are you suggesting that is what I said?

Ms Cox—No, I said that your question about whether or not corporate social responsibility has increased the bottom line is often used in the debates in this area with the implicit assumption that if it does not add to your bottom line you should not be doing it. I am not saying you said that, but I am saying that that is quite often the implicit assumption: you sell it on the basis that it will improve your bottom line. If you are selling it on that basis you are assuming

that if it does not improve your bottom line you can continue to be unethical. I think the distinction between ethics and legalities is often lost. I have had many a conversation with people on this issue, and when I say, 'Are you acting ethically?' they say, 'It is within the law.' If you say, 'That wasn't the question I asked,' they look at you very confusedly, because they actually do not understand that there is a difference between being ethical and sticking within the law. That is an important distinction that needs to be brought out for corporations, because very often they think that is the limit of what they have got to do.

If you go through the terms of reference, you see there are a whole lot of different views about the roles of corporations. I was just skimming through the Business Council of Australia's version of things—and some of the comments you were making about the attitudes of some of the business groups—which is, as far as they are concerned, that businesses are very concerned about their shareholder value. That is a legitimate thing, and I will get to that in a moment. But it is important for governments to say, in terms of their regulation, what they expect of corporations. Obviously you do that by high levels of regulation and changes in accountability processes. A lot of the changes in the governance processes that have gone on have been an attempt to block some of the holes in that. But it is an interesting process that you are going through at the moment, of trying to think through whether there are other responsibilities.

On point (c) of the terms of reference, I would like to use my own experience of a few voluntary boards as well as the UTS council, which is also voluntary. It is interesting how often that issue gets raised: people say, 'We have a responsibility for making sure that the university or whatever is working within financial constraints, and therefore we're not going to talk about this.' I get this quite often at the university when we try to raise issues about broader reasons for why we should do something. They say things like, 'We've got to do this because of the financial constraints we're under.' So the fear that directors have of breaching their responsibilities to manage the financial things within the construction and things like that sometimes interferes with their capacity to even talk about things outside that. It gets choked off at the board level.

I find sitting there and watching board processes very interesting, because I cannot imagine how boards run large organisations when the amount of time you actually have to talk about broader issues, and not just to approve the management decisions, is very limited. I think we have about nine meetings a year that each last for about 2½ hours. It is an interesting question, how you run a thing as big as UTS in that sort of time frame. Many commercial boards do not meet for much longer than that, and it raises some quite interesting questions about how much you as a director can take responsibility for the decision making. Some of the things we are seeing in the AWB inquiry and other such inquiries illustrate some of the difficulties—quite genuine difficulties in some cases—that directors might have in understanding what goes on within the structures of the management.

I would like to raise point (d), which I raised in my submission to some degree. I think it would be very interesting to look at the Corporations Law and how we actually set up the criteria for the accountability process. Shareholders come very high in the Australian system, but other systems are wider than that. The only other two examples I know are the Japanese and German corporations laws. They are different from the Anglophone systems, which all seem to have the same sort of model. I gather some other European ones actually put things like the environment,

workers and the community higher than the shareholders. I have not noticed that the corporations registered there have gone belly up.

I think the committee should think about whether or not the Corporations Law should be changed to acknowledge the other stakeholders, because far too many corporations slide back onto the fact that they have to deal with the shareholder value on a very short-term basis. You can argue that long-term shareholder value actually requires a broader view, but unfortunately that is a fairly confusing aspect of the current law: what is actually meant by shareholder value? Does it mean you have to push the shares up within the 12-month period, or does it mean that the organisation should be around in five years time? You will get both arguments from business, and they often lead back to the point that Senator Murray was making about long-term issues. One of the reasons that you have very short-term assumptions within the corporations is that they are very often working just on the basis of their current share prices or, at best, their annual reporting process to the annual general meetings. I think those were the main points.

My concern about leaving this entirely to a voluntary system is that the good corporations do it and the bad corporations do not. In a sense, good corporations run themselves better than bad corporations anyhow. It is that interesting question of whether or not, given the damage that is done by bad corporations, you want something that at least gives them a bit of a kick along to take into account some of the things that they otherwise would not take into account.

One of the other points—and it is an interesting one, because it is probably the role of government—is the cost elsewhere in the community that the government picks up when corporations do the wrong thing. It might not be the wrong thing legally, but when they are doing something that might be socially less responsible and it becomes an issue that gets picked up—maybe by social security payments, maybe by other things, maybe in other sorts of areas by people leaving and then not having jobs and so on—I think it is necessary to count the social and sometimes economic costs outside the particular areas that they do things.

The only other points I would like to emphasise are two points I bring up in my submission that I would be really happy to be quizzed on. I was just reading the Business Council of Australia's contribution. I think we ought to be very clear that donations or payments to the community are not social responsibility. Either it is cause related marketing or, if you are donating time to the community, it might really be management training. I have sat around and listened to managers talking with great enthusiasm about how much their staff members have learned by being sent out to the community. Conversely, I have heard some very bitter community groups complaining about being rung up and told to find work for 20 'suits' on Monday week, wondering what the hell they will do with them when they turn up for two days and asking, 'Do you think they can handle a paintbrush?' There is an assumption by business that sending their workers out for two or three days a year on that sort of basis, and not integrating it into what they are doing, is for the good of the community. It really is for the good of the corporation that sends them out there. It often wears community groups down. They do that because they become dependent on the goodwill of the corporations, to get a financial donation out of them. It is distorting the role of the community organisations by making them respond to other sorts of pressures beyond their primary responsibility.

As far as I am concerned, corporate social responsibility is doing your core business in a socially responsible way. Once you broaden it past that you start getting into some very murky

ground, because you really are dealing with marketing or corporate training. Any reporting system you bring up has to do that. Quite frankly the government has to carry part of the blame, because some of the stuff that is being pushed in terms of corporate donations blurs that and uses terms like ‘philanthropy’. It is not philanthropy. Philanthropy is giving for the love of giving; it is not getting your name in the paper for a \$30,000 donation and smiling sweetly at the local populace. You probably get more than \$30,000 worth of publicity out of it. I know I sound quite tough on this, but I get really quite terse about the fact that there are some very cheap varieties of greenwashing in the social sense—I do not know what that is; ‘pinkwashing’?—that actually look at how that relationship goes. We have got to be fairly clear that this is, as often as not, to the benefit of the corporation.

Some groups—and I point to IAG and The Body Shop that I have done some work with—actually incorporate their donations as part of their primary business. They see it as part of their core business. IAG only gives money to those things which will reduce risks for the insurance area. I think that is legitimate. Just chucking money at a community group because it is a good photo opportunity is not.

That distinction needs to be made much more clearly. Probably not many people make it because most NGOs will not bite the hand that feeds them. I am one of the people from the NGO sector that constantly bite the NGOs—which might also be evident in this, because I think the NGO sector also ought to be involved in reporting on what they do, and they do not. I have had this argument with ACOSS and with a collection of other organisations. Every organisation, whether for profit or not for profit, can benefit by thinking through what it is doing, who benefits, who loses and whether there are aspects of what they do that actually harms people who are not in a position to respond or to protect themselves. That should be one of the core responsibilities of any form of corporation, whether public, for profit or not for profit. Obviously it works differently according to whether you are a public institution, a for-profit institution or a not-for-profit institution. You can vary the criteria that you are dealing with, but basically they should know who they benefit and who they may not benefit and be able to make decisions accordingly.

CHAIRMAN—Thanks very much. Your remarks regarding not-for-profits in a sense mirror what Mr McLellan, the chairman of Habitat for Humanity, was telling us yesterday about the state of that organisation when he first became involved and the difficulty he had in getting them to accept what he regarded as businesslike standards of corporate governance, responsibility and the like.

Ms Cox—There are some interesting questions around that. One of the problems is that not-for-profits have been told they have to accept corporate standards of governance but at the same time there are corporations that are trying to mimic some of the not-for-profit stuff in terms of being good to corporate citizens. I would say that the not-for-profit area should have been offering leadership on what good corporate citizenship was about. Instead of that, they think they are doing good because they are set up to do good, but they do not actually examine what they are doing. I think they could probably add something—this was one of the points I made recently, and not very popularly, at an ACOSS congress. I said that the not-for-profit section should actually be providing some leadership in deciding what good corporate ethics could be. Some of the big not-for-profits—I will name one I had a public fight with at a corporate social responsibility thing, which was Mission Australia—are very lax in terms of what they do in their

own internal management. They prate ethics on their websites, and even publicly at conferences, but they run themselves like a corporation, a fairly hard-nosed corporation, and I think that they lose out on the capacity for being other things.

CHAIRMAN—Your submission focuses very much on corporate ethics. In your remarks today you have talked more about corporate responsibility. Do you see those terms as interchangeable or is there a difference between corporate ethics and corporate responsibility?

Ms Cox—If you are been responsible you should be being ethical; if you are being ethical you should be being responsible. I think they are linked. Corporate social responsibility should be based on the idea that you are trying to do the right thing. When I talk to people about what I mean by that, I say that there should be within an organisation an expectation that doing the right thing in terms of the corporation matches doing the right thing in terms of the stakeholders. So, in a sense, if ‘the way we do things round here’—which you very often hear as a part of organisational culture, and many of us can quote organisations where that happens—means burying mistakes, not raising issues, failing to point out when things are going wrong, going along with things you feel really uncomfortable about because you are scared to speak up, then we have a problem. You might be able to fill in a corporate social responsibility GRI but you might actually be behaving very badly.

I think corporate culture has to be part of things. One of the problems I have with some of the measures that come up in the GRI and other systems is that they do not measure corporate cultures. They measure measurable outputs. I am a sociologist. I do a lot of work around research methods. One of the problems is that you keep trying to find the measure and, in this area, because you are trying to balance it against financial accountability, you are trying to find hard data that matches the financial data. But, very often, when you are talking about what happens in an organisation that works really well, you are talking about soft data. You are talking about the relationships between people, levels of trust, capacity to do things without having to get everything specified down to the nth degree et cetera, and that is one of the issues of the fact that they are connected. So they are not identical but they are certainly closely connected.

CHAIRMAN—They are things that you cannot really legislate, aren’t they? The relationships between people within a corporation, the levels of trust—they are beyond legislation.

Ms Cox—It is beyond legislation but you can open up the possibility that people take into consideration the outcomes of what they do. That is where the legislation comes in: if you are doing things which cause harm or potentially cause harm in the community; if you do not take into account whether or not you cause harm to a particular environment or social structure; if you are unaware of it and make decisions without looking at things; or if you are prepared to make decisions without really understanding it.

The definition of corporate ethics I have used in some of the material I have written is that you are making the best decision possible on the best information you can find. That is an interesting point if you think of the AWB situation. It means that there is a responsibility on you to look for the information that is not necessarily being offered and take into account the benefits and losses—and perhaps particularly take into account those groups that are least able to defend themselves against the problems. And you do that within the context of the type of organisation you are, so you would be doing it differently if you were a commercial organisation, an NGO, a

service deliverer or a producer. If you use that as a deciding factor, then you can actually say it is unethical to go ahead making decisions without understanding whom you are going to harm. That seems to me to be a fairly straightforward decision. It does not mean you do not make the decision, but it means you have to at least understand the basis on which you are making it.

CHAIRMAN—Any questions? Senator Murray?

Senator MURRAY—The definition you gave in your discourse is about the best I have heard for CSR: you said that, essentially, if you are going to keep on the right track, you should be ensuring you conduct your core business in a socially responsible way. One of the reasons I like that is that I do not think CSR as a concept should only apply to corporations. It should apply to any organisation, though obviously it is most pertinent to large organisations. But, typically, if a large church, a large union, a large NGO or a profession conducts their core business in a socially responsible way you get very positive economic outcomes as well as social and environmental outcomes. Did you mean it in that broad sense or did you mean it only for corporations?

Ms Cox—I meant it in the broad sense. I have been particularly interested in looking at all types of organisations. I send my students out to look at small NGOs as part of their undergraduate course and report back on how far they set up their aims, look at what they are doing and have any consciousness of doing it. So I am very conscious of the fact that it does not necessarily happen at that level either. I am very interested in some of the big charities, as I mentioned before, partly because I think they are taking a lot government and private sector money and have sometimes lost their sense of what they are there for in the first place. They are constantly financially accountable in those particular directions, which I think can destroy their capacity to take into account what they were set up for.

But I would not exempt the commercial sector from that, particularly since the lines are getting very blurred. If you look at areas like child care, for instance, which is one of my particular interests, where you have a huge corporate player that boasts on its website that it is trying to reduce its staff costs down from 60 per cent to 50 per cent, you start thinking that maybe there are some questions around the ethics of that—the conflict between making a profit and delivering good child-care services. The question is of how you find those balances and of the role of government in funding them. I think there are some really interesting questions around the fact that there are more and more businesses taking on government contracts, whether it be building tunnels, running services or what have you. Therefore, the idea that they should all behave ethically stretches right across all sectors.

Senator MURRAY—CSR, like ethics, has an interesting view. There is a viewpoint common to the two—and of course they intermingle anyway—that you cannot legislate for it. What they do rather than legislate for it is measure it. We all agree that you cannot legislate for ethics, but I would argue that there are some kinds of ethics that you can measure. What is your view of the measurement of ethics and the resultant reporting of it?

Ms Cox—I think that is a difficult one because, as I said before, there is a bias to measuring the stuff that is measurable. It is a problem that runs through the entire social sciences. I am putting on my academic hat. Very often, the things that people measure—and you get the same stuff with contracts in the government for service delivery—are outputs and not outcomes,

because outputs are easier. You can measure how often you do something and what you actually do, but it is often seen as being too hard to measure what the effect is. I think you can do it. As a social scientist, I think there are ways and means in which we can do that. But it does require a mind shift to recognise that soft data is probably as significant as hard data. Because we draw most of our models of what we call data and accountability from the mathematical and financial area, we have not actually realised that maybe something like measuring increased trust in an area—and you can do that in certain ways—is probably important. If you measure the level of trust between service providers and the people who get the service, you would probably get a far better measure of the likelihood of the service being effective than you would if you measure how many times they meet. Yet at the moment we do not do that sort of measurement because it is seen as soft and not hard data.

Senator MURRAY—Yet companies do measure reputation all of the time as well as customer satisfaction and that sort of thing. My view is that there is a complex response which would include an ethical perception.

Ms Cox—Yes. I was involved in writing some of those questionnaires in work I did with the Body Shop. We started doing that. When we did the Body Shop stuff—this was a few years ago—one of the interesting questions in that was: ‘I am proud to tell people I work for the Body Shop.’ That was a staff question. In the first year we did it we got an 82 per cent positive response. Three years later, despite the fact that there was a split—this is Body Shop Australia—between the two owners which was quite public and nasty and various other problems had occurred, it went up to 92 per cent. I thought that was very interesting because it made an enormous comment on the level of openness and transparency at quite a difficult time and the level of trust that was built up amongst the workers. They were still prepared to trust the management of the shop despite the fact that there had been some quite public and nasty things that had happened. So I think there are ways. Odd questions like that actually illustrate very clearly a whole lot of things better than how many meetings you had about a particular issue.

Senator MURRAY—There is a crossover between values and ethics. Quite often if you say to people that they should take an ethical viewpoint they think of you as taking a moralistic and elitist view of things, whereas, if you say to them, ‘You should be offering a fair go,’ which is an ethical and a values statement, they immediately understand. It seems to me that many of the things that both our political establishment and Australians as a whole laud, such as a fair go and mateship, are essentially ethical concepts—that is, you should look after your fellow man.

Ms Cox—I will send you a paper I wrote on mateship for a Monash history conference. I will not argue that one with you at the moment.

Senator MURRAY—But you can see where I am going to with this. Given your presentation and submission on ethics and its intersection with values, the question is whether CSR can in a few practical areas in fact measure and report on ethical achievement.

Ms Cox—My worry about values is that I think ‘values’ is a much more contested term. Sometimes, to some degree, morals are, because they are seen as belonging to a particular group. The word ‘morals’ comes from the mores and actual customs of a group. In the same way, you can get people having arguments constantly about what ‘values’ are. As to ethics, although I know that this is a bit of a contested thing, I tend to see it as trying to do the right thing. It is

abstracted away from a particular cultural context. It is more appropriately used as being about what is right and wrong in a broader sense than just a cultural one. I know that it is not always used in that way. Some people, including some academics, use ethics and morals interchangeably. That is why I often tend to use the phrase 'doing the right thing' when I am talking popularly. I think 'doing the right thing' means not just doing the right thing by me or by my group.

Senator MURRAY—Yes, that is the concept I am using.

Ms Cox—It takes on broader things. I think what is important in this area is to try and say, 'We're talking about doing the right thing in a way which is broader than what suits me and what is good for my group.' That is one of the problems you sometimes get around concepts like morals and values—they are often ascribed to particular groups and tied to religion or other sorts of things, so you get some absolutely bitter debates around terms like values and so on which I have not heard quite as much around ethics.

Senator MURRAY—Sometimes in this discussion we get down to real practicalities, and I will give you a practical example. In Perth the Swan River, with its tributaries, matters a great deal to the health of the city, and I think something like 30 per cent of Perth—it might be less now—is unsewered, with septic tanks and so on. They have trucks that clean these things out and, to save costs of going to the proper site and discharging the waste, they have been known to pop it into the storm drain, straight into the river. To me that is not just illegal; it is profoundly unethical. It is really not doing the right thing. It has a direct environmental and social consequence. To me, CSR should try and inculcate the values. It is not just wrong in law; it is profoundly wrong in other ways.

Ms Cox—My concern is that we should not spend too much time focusing on the 450 different measures of CSR which you have probably had presented to you in five million different ways. While it is important to find some measures—and I think some of the GRI and other things at least have some sort of international backing, and there is the ASX version, the Standards Australia version and the other versions—it is important to incorporate within this, even into the Corporations Act, some sort of objective which says we think that corporations ought to act ethically, that they ought to try and do the right thing. Then people can work out exactly what it means as to how you actually do that. I think it is the importance of emphasising exactly the point that you were trying to make: that it is not just about obeying black-letter law. One of the things I say to organisations is that codes of ethics do not work because people read through the code of ethics and it does not say, 'You can't do that.'

Senator MURRAY—You are suggesting genuine principles based law.

Ms Cox—Yes.

Senator MURRAY—People often talk about principles based law, but 'Thou shalt behave ethically' is a good principle to have as well.

Ms Cox—At least it gets you into a debate about what is ethical, because if you have a code up there you have already decided what is ethical. If something is outside the code, somebody

rushes off and does that and says, 'But it didn't say I couldn't!' You hear that argument all the time—people playing that sort of game.

Senator MURRAY—Thank you.

Senator WONG—We are running a bit short of time and there are a lot of things I would like to ask you, but perhaps I will just focus on a couple. You talked about measurement of trust and you and Senator Murray have been having an interesting discussion about ethics. I am wondering, given we agree we cannot legislate for ethical behaviour—we can legislate against identified unethical behaviour, but that is as far as it goes—do you think, as a sociologist, there is anything that your discipline can offer to companies that are seeking to create a more ethical culture?

Ms Cox—I have been playing around with a questionnaire on ethical cultures, and I have offered it to people for free, which is probably a mistake. If I told them I would charge for it they probably would all have rushed it, which is an interesting question. It came out of some of the work I did with the Body Shop. It goes back—and this came out to some degree with the previous speakers—to trying to talk to corporations about trustworthiness. I want to use the word 'trustworthiness' rather than 'trust', and I have played around with this as a researcher. When you ask your students to go out and try and ask questions on trust, people do not quite get it when you say 'trust'. Trust is contingent. You trust your mechanic to fix the car but you would not give them your money to invest—I hope.

As for trustworthiness, if you start talking about the fact that an organisation is trustworthy, it usually means you expect them to do the right thing not only by you but by others as well. It is a broader sense. I think that is an important concept. I know sometimes it gets misused, but it is an important concept because what you are looking at is the idea that, if you think an organisation is trustworthy, or management is trustworthy or a particular practitioner or whatever is trustworthy—

Senator WONG—We trust them with a broad range of behaviours, essentially.

Ms Cox—there is also an issue around resilience. It means that, if they do something wrong, you assume they have probably made a mistake and not that they have done it deliberately. There is an interesting quote by a woman called Margaret Levi, who is an academic in the USA, in which she says, 'Trust reduces transaction costs.' I think that is a really interesting one, because you can find out how well an organisation is working by finding out the level of regulation it has within its own structures. If you find an organisation that has a rule book this thick you have a low-trust organisation, because nobody trusts anybody to do anything and everything has to be written down. So we have indicators we can look at to decide whether there are levels of trust.

There are some very good reasons to sell the idea of trustworthiness as something that makes organisations work well, and in a sense acting ethically is likely to create trustworthiness. This goes back to what Linda and Judy were saying that an organisation that has the sort of culture where people tend to trust management, tend to believe they do the right thing and tend to accept things, they have a greater capacity to change when they need to change. You can get a huge resistance to change. I can talk about UTS, which I always use as my example. People get anxious about change, because there is not a level of trust in the management.

So you have all sorts of benefits that can bring themselves out by creating more value for the organisation. It also makes it a better place to work. You are more likely to keep your staff and you are more likely to be able to make the right sorts of decisions, which is what I was trying to talk about before: people will give you the information instead of hiding it from you, because they might get into trouble for producing stuff that people do not want. So there are many ways in which looking at the culture of an organisation in that broad sense can actually be to the benefit of the organisation. Some of it will come out in the bottom line. That is why I am talking about cultures as producing good corporate social responsibility rather than producing just the indicators.

Senator WONG—What I want to focus on is not so much the articulation of why that is a good thing but how you might make an impact. You did work with the Body Shop. If you as a sociologist were asked to work with an organisation to increase its trustworthiness, essentially, how would you go about that?

Ms Cox—The first thing you would probably do is ask their stakeholders—which is the accountability model, the British one—what they think of the organisation. The first thing you want to find out is what level of acceptance they have of what the organisation does. Do they think it acts fairly in the way it markets its products? Do they think the products are appropriately described? Do they think the services are well delivered? Do they trust the people who are doing it? Do they have appropriate expectations? If you do that sort of stakeholder survey, it is a very good indicator of whether the organisation has problems or whether particular parts of the organisation have problems. A lot of organisations do that in terms of what are called ‘climate’ surveys. There is a whole lot of stuff around that. They do not focus it particularly on the ethical, but that would not take much thinking.

One of the things I say to people, because one of my other hats is running around being a ratbag feminist, is that maybe we have run out of steam on issues, such as talking about EEO in terms of achieving certain statistical benchmarks. But ethical corporations do not discriminate. So you can fold a lot of the issues. There is a lot of material that corporations already collect—if you look at their EEO stuff, if you look at what they do under occupational health and safety, if you look at what they do under their corporate image, if you look at customer satisfaction surveys and things like that.

You do not have to start from scratch. It would not take very much for somebody with a sociological or research background to dink those various things so that you could get a sense of: ‘Do people find us trustworthy? Do they think we’re doing the right thing? Is it important to us?’ Some fly-by-night companies would think, ‘We don’t care, we’re not going to be here in a couple of years.’

In a sense, there is already a lot that is collected that could be refocused onto CSR at very little cost. So the idea that this is a big-cost exercise that you have to start from scratch ignores the amount of stuff that is collected. You can get things like separation surveys that you do when people leave. There are all sorts of different things that you already have somewhere in the system—if you could extract them. That is one of the jobs that we did at the Body Shop, which admittedly was a relatively small organisation. But you are not starting from scratch; it is not hard to look—

Senator WONG—I would not have thought so.

Ms Cox—A lot of that is quite good data.

Senator WONG—You have mentioned the Body Shop. It is a private company, isn't it?

Ms Cox—Yes.

Senator WONG—Do you see examples of Australian public registered companies that you regard as at least tackling or attempting to instil an ethical culture?

Ms Cox—To give them their due—and Linda was involved in that—I think Westpac has made a fairly good effort to do so. It was one of the first ones in. I would not say that everyone who works at Westpac thinks it is an ethical organisation, but at least at the top level they have tried to do it. One of the interesting questions is about when you have top-down stuff, and they are doing it. There are public companies that come up constantly. They will turn up as 'employer of choice' and then they will turn up in the CSR lot and they will turn up often as doing well in other ways too. So I think there are quite a lot of companies that are beginning to see themselves as being able to do this. I would not say that they were all doing it. BP, for example, does very well in the environmental stuff. Some of the other people do well in the environmental stuff but do not do so well in the social areas.

There is a whole mix of different ways in which they are doing it. I think what is happening in the corporate sector is that smart companies have realised that this is important. Dumb companies are still trailing around saying, 'It's not important and we really shouldn't do it,' and protesting that it is ruining their shareholder value. So, in a sense, it is happening on that sort of basis. My issue is that the dumb companies are likely to cause an awful lot of damage before they fall over. One of the reasons they will not fall over is that, to go back to the economic term, their moral hazard has often been underpinned by the fact that government bails them out when they stuff up, in some cases. That ruins their risk taking. I think there is an interesting question around that stuff, if you are going to be purely economic about it.

The other question that I have raised in my submission and that I want to raise here again, because I think it is part of it, is that NGOs and other organisations really should be part of the same system. If you actually had them all doing some form of corporate social reporting or if they had some obligation within the structure of the Corporations Act to take a socially responsible view of their operations and be able to be held accountable for it then I think you could actually get some much better performances out of organisations in that sort of sense, because there are a lot of situations where they really do have to think through that issue of who they are harming. I think the stakeholder model has a lot to do with it, but I would tend to add to the stakeholder models, because to take responsibility for your customers, your workers and your suppliers is quite an interesting process. It does force corporations to think about the people they deal with. But I think that into it needs to be added something called society or community, the common good, as well so that at some particular point in time you can say, 'Okay, these are your own stakeholders, but are there things that you are doing which is creating harm to the broader community'—which gets back to the question of which bottom line you are counting—'that has to be paid for by people outside the corporation?' Even in economic terms that makes sense. There ought to be a situation where you can assess. Maybe that is as far as legislation

goes: to say that organisations have to report on what effect they have on all their stakeholders as part of a process, without getting into the finer points of whose particular measure is going to be the most appropriate.

Senator WONG—Thank you very much.

CHAIRMAN—There being no further questions, Ms Cox, thank you very much for your appearance before our committee and for your contribution to our inquiry.

Ms Cox—Thank you for the opportunity to appear.

Proceedings suspended from 12.39 pm to 1.19 pm

MacMAHON, Mr Rohan, Business Group Member, Amnesty International Australia

SMITH, Ms Rebecca, Advocacy Coordinator, Amnesty International Australia

NOLAN, Ms Justine Mary, Associate, Australian Human Rights Centre, University of New South Wales

CHAIRMAN—We have before us your respective submissions, which we have numbered 20 and 90. Are there any alterations or additions that you wish to make to your written submissions?

Ms Smith—Not at this stage.

CHAIRMAN—Okay. I invite you to make your opening statements, at the conclusion of which I am sure we will have some questions.

Ms Smith—Firstly, Amnesty International Australia thanks the committee for the opportunity to provide an oral submission today on this important subject. As you would be aware, our mandate is to protect and promote human rights. So it is that perspective that we are bringing to the debate about corporate social responsibility today. While CSR is obviously a concept which is considerably broader than Amnesty's mandate—it includes that a business meets or exceeds its ethical, legal, commercial and public expectations society has on a business—we believe that companies that meet the human rights standards which we set out in our submission will in turn meet public expectations.

We propose that the Corporations Act be amended to specify that directors must exercise reasonable diligence to ensure human rights are not breached as a result of companies' operations or that their suppliers or outsourcers do not breach the human rights outlined at page 11 of our submission, which were taken from the UN norms document—*Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights*. We propose that companies, as part of their normal annual auditing processes, complete and table a simple statement to ASIC noting that, in the opinion of their authorised auditors, they have complied with each of the human rights from the UN norms document, as set out in our submission. We see this approach as a somewhat more simple and limited reporting mechanism than full triple bottom line reporting and we see it as not unduly onerous on business. I will now hand over to my colleague Rohan.

Mr MacMahon—I would also like to thank the committee for the opportunity to talk with you today. The Amnesty International Business Group is a group of volunteers, mostly within the corporate sector, who are working as members of Amnesty International to talk about issues of corporate responsibility and corporate governance. As part of that, I have been asked to disclose that I work at Telstra. Although I do work at Telstra, my comments today are entirely on behalf of Amnesty International—not on behalf of Telstra.

In support of Rebecca's remarks, the point of the Amnesty International submission is that we believe it provides legal certainty, which we think is what a number of bodies within the business sector have been seeking. We believe the submission reinforces the fact that corporate

social responsibility is in the long-term interests of all corporations and indeed all organs of society. That is borne out in other submissions before you, such as the submission from the Business Council of Australia.

The point of our submission is that not all companies clearly understand that, as a matter of management of risk, it is appropriate to balance the voluntary approach which you see in self-regulatory mechanisms and the voluntary behaviour of a number of notable Australian companies with a modest codification of corporate social responsibility standards within the Corporations Act. We believe that the appropriate specific mechanisms to do that are represented within the UN norms, as Rebecca mentioned. That is essentially the summary of our submission. Thank you.

Ms Nolan—On behalf of the Australian Human Rights Centre, I thank you for this opportunity. My submission deals with the focus on moving corporate responsibility from the voluntary to the mandatory, still assuming that some guidance needs to be given to directors of companies when publicly reporting on corporate responsibility issues and, at the same time, leaving them a minimum amount of discretion. My submission focused on the voluntary efforts—how far they have come to date and the fact that voluntary efforts can be shown to be the foundation for more mandatory regulatory requirements in reporting. This has been shown in some jurisdictions which I have covered in the submission—specifically, the UK, France, South Africa and, in very minimum requirements, Australia under the Corporations Law.

The focus of the submission from the Human Rights Centre deals with the value and effectiveness of corporate reporting and specifically considers those issues which might be considered material to a company in that they must be disclosed. It specifically considers to whom, what and when such issues should be disclosed. In guidance, it looks at emerging regulatory requirements from the countries that I mentioned. There is one update from the submission I would mention. The submission refers to the UK's operating and financial review and the requirement for quoted companies to provide that narrative. In November or December 2005, the UK government announced that it was abandoning this, which was considered a u-turn. It is a decision that has been criticised by a number of NGOs and business leaders. The chancellor's decision is currently the subject of legal challenge.

The submission primarily focuses on the fact that mandating the disclosure of social and environmental issues is a necessary step in integrating corporate responsibility into a company's core business strategies. The existence of a requirement for companies to disclose relevant social and environmental issues will not by itself prevent acts of corporate irresponsibility, but we believe that it may act as a deterrent in certain circumstances. However, we suggest that clear guidance must be provided to companies on what and when such issues should be disclosed. Otherwise, we run the risk of engendering a movement that merely encourages the production of token reports that lack consistency, comparability and credibility between companies.

We believe that the transparency associated with corporate reporting will lead to greater accountability, and without accountability such as that companies will have no responsibility for change. We stress that reporting alone is not a panacea but is one increasingly valuable tool for ensuring corporate ownership of the broader impacts of business operations on the community.

CHAIRMAN—Amnesty’s submission and the Human Rights Centre’s submission focus pretty narrowly on the human rights issues rather than the broader issues of corporate responsibility, and that is understandable, given your particular interest. Are you proposing some amendments to the Corporations Act or simply to the reporting requirements?

Mr MacMahon—What Amnesty is proposing is an extension to the directors’ duties section of the Corporations Act, specifically to note that directors should, subject to a reasonableness test, state that they comply with UN norms for human rights standards. On page 11, our submission outlines what those statements are. It is worth noting that those particular human rights are not in any way challenging to the vast majority of Australian businesses. They represent standards like the right to equal opportunities and non-discriminatory treatment in the workplace, the right to a fair standard of consumer protection for one’s customers and so on. We believe that those represent an appropriate, modest and clear set of statements backed by international law.

CHAIRMAN—Are you concerned principally with the activities of corporations within Australia and their obligations in relation to human rights in Australia or their obligations when operating offshore or both?

Mr MacMahon—In Amnesty’s case, it is both. We are concerned about activities within Australia and within Australian companies with operations overseas.

Ms Nolan—Ours is the same.

CHAIRMAN—Given that in Australia the human rights issues that you have addressed in your submission are largely protected by other legislation, why do you see a need to amend the Corporations Act and add to the protections that already exist in legislation?

Ms Nolan—In our case, we are not specifically looking at directors’ duties but the reporting requirements. It is not clear that companies have to report on all these issues now. We are trying to simplify the process. We want there to be a clear set of indicators and a one-stop measure so that if someone is trying to find this information they are not going to 20 different sources but can just go to the company’s annual report.

Mr MacMahon—Amnesty would agree with that, but I would also add that a number of businesses have sought the kind of certainty that we are talking about. Ms Meredith Hellicar from James Hardie, for example, mentioned that she was concerned that directors’ duties as they currently stand would allow the opposite, where it would be open to be construed that shareholders might take action against directors precisely because they had taken some of these factors into account.

CHAIRMAN—A lot of our evidence has been to the contrary, though. It would be almost reasonable to say that in terms of public presentation her argument is probably the only one that has been presented by a corporation that says that the law is not sufficiently permissive to allow directors to take account of stakeholders other than shareholders. That is by the by, though. Obviously, human rights are a component of corporate responsibility. Accepting that that is your particular focus, within that context do you see a need to have a broader commitment to corporate responsibility in the Corporations Act than just in the area of human rights?

Ms Nolan—When you refer to human rights, are you talking about human rights that Amnesty has set out in the UN norms?

CHAIRMAN—Yes.

Ms Nolan—I think the language gets clouded at the moment, particularly in Australian usage. Environmental issues tend to be given priority because they are easier to encapsulate. Other things tend to fall under ‘social’, and I think ‘social’ needs to be more clearly defined to explicitly include certain rights and not be left as a broad category.

Mr MacMahon—It is worth noting that the UN norms themselves make explicit reference to environmental protection as a category of human rights. Specifically, the way in which companies carry out activities should be in accordance with national local environmental laws. It is effectively a restatement at the Australian level that a company should be expected to follow the applicable national laws of the country in which they operate.

CHAIRMAN—So you want a more specific requirement in the Corporations Law than simply an amendment saying that directors should take account of the interests of stakeholders other than shareholders? You want more specific direction towards human rights?

Mr MacMahon—In my opinion, something more specific is required. Certainly just a description that says ‘stakeholders’ leaves it open to the questions: which stakeholders, to what extent and how? We think that an approach based on the best international instrument available, which is the UN norms, is the best move.

Senator WONG—Can we go back to the UN norms issue. I am not sure to what extent you are looking at alternatives. Are there other ways you think government can endorse and promote compliance with the norms and the activities of companies, particularly in the transnational context, rather than simply putting it in the Corporations Law?

Mr MacMahon—Certainly Amnesty’s submission is definitely in favour of continued take-up by Australian companies of voluntary mechanisms which take a number of different forms. Things like third party indexing measures like the corporate responsibility index or Reputex are a helpful move forward. We also see the company’s own self-reporting activities which might be over and above participation in an index, the likes of which you see from many a leading Australian company. Westpac or BHP Billiton might be examples. They are very helpful mechanisms. I suggest to you that the gist of Amnesty’s submission is not around the voluntary activities of companies that are already taking those measures but around those that are not. I refer you to page 8 of our submission. We have attempted to describe the fact that some companies are already doing reasonably well.

Senator WONG—I understand what you are saying, but, frankly, I am trying to give you the opportunity to give us an alternative. You are probably aware that there would be a significant degree of opposition to amending the Corporations Law in the manner you describe, so I am asking whether there are other legislative mechanisms or other governmental mechanisms that you would look at. If you have no view about it, that is fine; I do not have a problem with that.

Mr MacMahon—Certainly. I think that Amnesty would support an extension of, for example, the Australian Stock Exchange guidelines to become—to use a word—perhaps ‘mandated’ for, potentially, the top 100 companies or the top 200 companies. Another mechanism might be an extension of the corporate responsibility index to cover the same list of leading companies. So things that are voluntary could become encouraged, if you like; they could even be mandated.

Senator WONG—What is the status of the UN norms insofar as the ASX is concerned—that is, in the current guidelines?

Ms Nolan—They do not make any reference to them, because the UN norms is a 2003 document. It is still a draft document. The ASX guidelines basically give general credence for people to consider relevant instruments et cetera, so you could include it broadly in that. The UN norms is clearly still a draft document. The Special Representative of the Secretary-General came out with his report yesterday, I think—he is the representative of business and human rights—and he discusses the norms in it. He specifically feels that the norms contain useful elements in that they provide indicators—for example, what could be reported on by companies. But it is not a definitive document; it is still being worked on. He questions the legal veracity of the norms in terms of their direct relevance to companies in that it is still a matter of debate whether it should be a state or corporate obligation. He specifically says that the matters raised in it—the rights they raise—are things that could be used as a base for, for example, companies reporting or for states mandating reporting.

Senator WONG—Is the primary focus on companies operating internationally offshore? What is your primary concern?

Ms Nolan—Ours is offshore, in part because of what the senator said—there are laws in Australia that are not sufficiently clear in some ways or they are coming from 1,000 different sources. But we feel that there is a bigger vacuum for companies operating offshore.

Mr MacMahon—Amnesty would agree with that. The current legislation is piecemeal—state and federal and so on. Primarily, our focus would be offshore.

Senator WONG—The piecemeal argument, though, is not necessarily a reason to put more into the Corporations Law. There might be an argument to codify a bit more coherently the various aspects of state and federal legislation and harmonise the legal position on people’s rights for the country.

Mr MacMahon—Certainly, that is true.

Senator WONG—Can I briefly turn to the SMEs. You did touch on this when you talked about the highest risk. We have had some evidence about the difficulty both in cost and capacity for small and medium enterprises to engage with sustainability or corporate responsibility issues. If we fold the observance of human rights into that rubric, the view might be: how do you get the small to medium enterprise sector to engage with these issues? I do not know if you have any comments about that.

Mr MacMahon—I certainly believe that is a very big issue. There are more SMEs out there than there are large companies, obviously, and they do not have the resources or skills to deal

with some of these issues. I think it is important to try to keep the bureaucratic overload down and not add unnecessary overheads to businesses. We would support efforts by government which might be promotional for CSR activities broadly but for human rights activities specifically. That could be in the context of the indexing measures that we referred to before. It could also be in the context of things like the Prime Minister's community partnerships scheme—things that are already making some progress on that front. From a reporting point of view, that is to me why the Corporations Act seems like the simplest measure. It is something that companies are familiar with, even if they are small. To that extent, it tries to keep the burden to a minimum.

Ms Nolan—I think it also supports the argument for greater clarity in what should be reported on in that you do not need to have small to medium enterprises wondering what the hell they should be reporting on in the first place. It can take a year for them to figure it out before they get around to reporting. There is some guidance. I think that the measures have been far from perfect in France, South Africa and the UK in recent years. I think we can learn from the mistakes they have made. They have also had some necessary flexibility built in between the larger quoted companies and SMEs.

Senator WONG—What were some of those mistakes?

Ms Nolan—In France, the new economics regulation that came out left it originally very unclear as to exactly what the indicators were. Originally, it was also applying to a very broad range of companies. It also was not clear whether it was just companies operating in France or offshore. So they basically had an overload of companies. Some companies were reporting everything and some were reporting nothing. Again, when you are looking at the argument for the Corporations Law, it is the main source that companies go to. If you could have a condensed report of, say, a company's annual report, it makes it clearer and less ambiguous for them.

Senator WONG—Have you engaged with the GRI at all?

Ms Nolan—Yes.

Senator WONG—I noticed in what I think is called the G3—which is the current draft looking at the revision of GRI—there is a reference to a section that deals with human rights. Do you have any comment to make about how useful that is or any criticism of that?

Ms Nolan—The GRI has traditionally tried to cover the world in terms of reporting, and I think it has been asking too much of companies. The question of reporting also has to be one of who you are reporting to; who is going to read it. I do not believe that the average consumer is going to pick up a 1,000-page report from a company and look at their basis on rights. The GRI, as it is currently constituted, is very detailed on the indicators. The review it is undergoing now is trying to condense it to the essential indicators. I think it will take some time. That is where I think they need to have some consistency with the relevant rights coming out of the norms as well.

Senator WONG—I guess that is where I am focusing.

Ms Nolan—Yes. Their human rights indicators are starting to parallel with the norms. I do not think they are there yet, but all of these voluntary mechanisms will merge more into one and the GRI shows some promise of doing that. I still think it is asking too much of SMEs.

Senator WONG—There is a bit of a paradox in the evidence that is coming out. On the one hand you say that there is too much evidence and on the other hand you are actually asking for greater reporting against human rights. We have an environmental group coming before us and they will ask for greater reporting against environmental sustainability. Community groups which have other social issues, obviously, would want greater reporting in relation to that. I guess that is why I am asking whether or not you think that the GRI discussion of human rights or the parameters around that could be sufficient.

Ms Nolan—I guess what I am saying is that the GRIs traditionally had a lot less focus on human rights and environmental factors. I think they are coming late to the table with it. I have seen a previous draft to the one you are referring to and I think it was still too expansive. They need to basically be in line with the UN norms and the indicators they are asking for.

Senator MURRAY—I address my question to Amnesty International because you are an international organisation with a very high profile. Does Amnesty do triple bottom line reporting or CSR? Do you produce either of those forms of reports?

Mr MacMahon—I am aware that we have some statements of compliance with certain measures like fair wear and fair trade and those sorts of things. I am not aware that we have a formal reporting that goes to the extent that we would like to see on CSR issues.

Senator MURRAY—As you know, the Corporations Law covers not-for-profit organisations, which I think both of your organisations are—or more particularly Amnesty International; I think, Ms Nolan, your organisation is more university based—as well as organisations that are incorporated. If what is required of any organisation is that its core business is conducted in a socially responsible way, to purloin the words of Eva Cox, any organisation should do its best in that area. Of course, some are much better equipped than others—for example, a large church organisation, a charity organisation, an activist body such as yours, a profession or a union. There are numerous examples of bodies that are not incorporated that have a very large economic, social and environmental footprint. But it strikes me as odd that many of the advocates that come to us and talk about what corporations should do are not doing it themselves. It is a ‘take the plank out of your own eye first’ type of approach.

Mr MacMahon—I would agree that there is an opportunity to improve that. The submission from Amnesty draws its body from Amnesty’s mandate, which is based on things like the Universal Declaration of Human Rights. That states clearly that every organ of society is obliged to uphold human rights. That applies to our organisation as much as it does to any other. I guess many NGOs would face the very same challenge that corporations face, which is that we would like to be doing something but it is not quite clear exactly what it is we should be doing.

Senator MURRAY—Let me be specific so that you understand my own prejudices and bias. I am not a supporter of constitutionally based rights because I think that becomes very difficult, but I am a big supporter of a charter of rights. I think that the sorts of things you are arguing for fall within that. As you know, in Australia there is only one example and that is in the ACT.

Therefore, I am a supporter of the broader approach taken up by CSR because as soon as you start doing checklists or 'must includes', you get fairly lengthy amendments and it becomes highly contestable. I am quite responsive to the present approach.

I must declare I am a member of Amnesty, and I believe in its role, so I approach you with a positive bias. Nevertheless, I have often found that churches that proclaim their love for humanity will not pay out compensation for some poor soul who has been abused somewhere. A union may behave unfairly to its employees or a legal practice may behave profoundly unethically and unjustly. You can see where I am going with this. I would ask you to take a question on notice. Perhaps you could ask your corporate people—and I presume you have them somewhere—just what they do about CSR and triple bottom line. Triple bottom line is economic, environmental and social and I think commonly in CSR the economic is taken for granted and corporations are asked to accept social and environmental responsibility. But the flipside is for those organisations of a social and environmental nature to take economic responsibilities because in my view you want all organisations to attend to all three. That is the framework of my question on notice. Would you mind doing that?

Ms Smith—Senator, that is not a problem. It is something that is on our priority list at the moment, so we would be happy to provide the committee with further information.

Senator MURRAY—The important thing for you to recognise and perhaps for you to comment on is this. This committee has been asked to examine the CSR matter and, if it comes up with recommendations, those recommendations will apply in the NGO and not-for-profit sector as much as in the for-profit sector where those organisations are incorporated. If that is the case, you have to ask: why shouldn't it apply at the lower or different level for small business that is not incorporated, for professions and so on? Do you take that wide view or do you restrict yourself to the principle that ill is in the corporations and that that is where the focus should be?

Mr MacMahon—I think from Amnesty's perspective the focus of our submission has been on the corporate sector specifically, but our mandate is clear that all organs of society are where we should be trying to affect human rights outcomes.

Senator MURRAY—The other question which affects us as legislators is often where matters should be housed. I have already raised the issue of the charter of rights versus dropping these matters elsewhere. Typically, the Criminal Code tries to wrap up all criminal offences, and you do not then repeat them in numerous sources of numerous places. Bribery and corruption is in the Criminal Code; you do not repeat it in the Corporations Law. A major human right is equal opportunity—that is, principally gender based but also age based and disability based. Do you not feel that the human rights aspect is adequately covered by the equal opportunity legislation and that to put it into Corporations Law would be repeating something which has got jurisprudence as well as established process, with institutions that manage it and so on?

Mr MacMahon—I mentioned the point about operations outside Australia, where I do not believe that local, state based legislation would apply. I guess the gist of our submission is around the need for a legislative solution that brings together what are currently disparate elements across different state and federal acts and a number of different acts.

Senator MURRAY—Perhaps, Ms Nolan, you would respond both to that previous question and to this question. One thing we are asked to do with respect to the international conduct of corporations is to put matters into the Corporations Law which really are designed to just apply to those conducting business offshore, to ensure that they behave as ethical corporate citizens, basically. Again, my view—and in fact my party has a private bill on this matter—is that that should be captured in a separate piece of legislation, as, for instance, the child sex and sex tourism thing is not general or specific to anyone who is travelling overseas. Do you react well to that?

Ms Nolan—As to your first point, I think that Australia's antidiscrimination provisions are perhaps our finest protections of human rights, that there is not much argument about that and that they tend to be fairly comprehensive. But, as Rohan said, they are restricted to Australian jurisdiction and that does leave a vacuum for offshore operations, which we have talked about. As for the argument as to whether the alternative to the Corporations Law should be in a separate piece of legislation, like your private bill, yes, that would be great. In terms of looking at what is the most likely thing to go ahead, Senator Wong has mentioned that there is considerable opposition to changing the Corporations Law. There is perhaps even more opposition to a private bill like that in the near future, so in some ways we are looking at what offers the most immediate change. In our submission we focused purely on reporting. We thought the Corporations Law was the home for those types of amendments that are encouraging greater reporting.

Senator MURRAY—Your submission does indeed focus on reporting but it does not deal much with measurement. Reporting is one cost but that is a relatively low cost, I would suspect, compared to measurement although perhaps not with respect to human rights. But when you get into environmental reporting, to actually measure emissions and then measure negative outputs from factories and so on you need sophisticated equipment and all that sort of thing, although I accept that does not necessarily apply to the human rights area. Is it your view that the GRI process will produce the standards and measurements that are necessary, so all you want to do is argue that the principle be accepted?

Ms Nolan—In our submission we refer to measurements as being more like indicators. That is an area that requires a lot more clarity in human rights. In some ways it has been a lot clearer in environmental issues because it has a longer history and other jurisdictions have gone further, and Australia has also required clearer reporting on environmental emissions et cetera. Human rights, in terms of what should be reported on and how things should be measured, is still very much a question of debate. That is why the norms on corporations' responsibilities have created such controversy. They have proposed as a first step that these are the indicators that need to be measured, and there has been dispute on many sides over that. I do not think that debate has been resolved. This inquiry is one of those bodies that have an opportunity to look at it and say, 'Perhaps we should look at something like the GRI or the norms as our starting point.' I think that some guidance has to be given to companies and that we should not just say, 'Report on human rights.' I would argue that you report on those indicators that are raised in the norms.

Senator MURRAY—One of the views that the committee might have sympathy for—and we have discussed this with witnesses and witnesses have put this to us—is that when you get as much of the measurement issues, the indicator issues and the standards issues as right as you can then you can talk about putting them into law, because it is in the development of standards, the

ironing out of differences and the ending of controversy that you get a significant result. Also, this committee has a great deal of experience of the 41—whatever the number is—accounting standards, and each one might be a couple of hundred pages long. So you would not put that into law; you would merely give it the force of law when it has been institutionally developed through proper consultation. So my question to you—and this is really what I am putting to you—is: would you perhaps accept setting up a process whereby the government would assist in the development of standards and a better understanding of these things so that, rather than charging straight into a legislative requirement and a reporting requirement, it would assist the process that is already under way?

Ms Nolan—I think there is a lot of value in that. Obviously, it comes down to details such as: does it have an end to it? Are we going to focus on this for five years and then consider the next steps, or are the terms of the consultation for an indefinite period to get to specific standards? Is there going to be a trial period? Is there any recommendation for specific items in terms of which company should take it up—for example, the largest companies or the listed companies et cetera? There is a lot of value in what you say, but it comes back to a need for some specific guidance on what those standards include, who they apply to and how long they are going to be enforceable.

Mr MacMahon—Amnesty would agree with that. We would like to see the government take a leadership position on corporate responsibility at a general level and encourage the auditing and accounting industry to help the corporate sector come up with the right measurement tools. The norms, as have been mentioned, are relatively new. They are still at the draft stage. Exactly how they would be interpreted, if they were eventually given the full force of law, is something that you would expect to be backed by a genuine measurement capability within the accounting sector. They could be the companies that we consider to be accounting companies today or they could be some of the newer third-party measurement organisations that are coming out now.

Senator MURRAY—Going full circle back to my first question, would you suggest that the standards, methods of measurement and accepted indicators that are developed should apply to NGOs—not just incorporated but unincorporated NGOs—and that the NGOs themselves should participate in the process of developing those standards and so on and not stand outside of that process?

Mr MacMahon—Certainly.

Ms Nolan—Absolutely. For the standards to be credible, they have to have representatives from the different sectors involved in their development.

Senator MURRAY—Not in a sense of being there to ask the corporations to make sure that the corporations get in but in the sense of recognising that they can apply to them too.

Ms Nolan—Sure.

CHAIRMAN—I have one final question. You are concerned about Australian corporations operating offshore. Is it your contention that in their offshore operations they should comply with Australian law or the law of the country in which they are operating?

Mr MacMahon—From Amnesty’s perspective, whatever modification we might make in our proposal to the Corporations Act, essentially we need to make sure that the UN norms are followed. In the case of environmental laws, for example, that would mean following the local law of the country that they are operating in. In the case of areas like equal opportunity and non-discriminatory treatment, that would mean a pretty generic legislative requirement would apply even if it were not required in a local geography.

CHAIRMAN—Thanks to each of you for your appearance before our committee and for your assistance with our inquiry.

[1.58 pm]

MATHER, Mr Erik, Head, BT Governance Advisory Service

CHAIRMAN—Welcome. We have before us your submission, which we have numbered 19. Are there any alterations or additions you wish to make to the written submission?

Mr Mather—No alterations.

CHAIRMAN—In that case, I invite you to make an opening statement, at the conclusion of which we will have some questions.

Mr Mather—Thank you very much for the opportunity to appear before you this afternoon. From our perspective, corporate responsibility is concerned with environmental, social and corporate governance. We are not aware of any existing legal impediments to the consideration of environmental, social and corporate governance by companies. Environmental, social and corporate governance relates to cost and risk management. Cost and risk management is in the interests of the company; therefore, the duty to the company by directors implies a positive duty to be concerned with environmental, social and corporate governance.

In our experience, environmental, social and corporate governance considerations either lack appropriate consideration or, when they are considered, lack transparency in the interface between companies and markets, and, in both issues of governance substance and governance form, share owners' interests are not as well served as they might be. The remedy to this is not regulation. Supportive policy, however, would assist improved understanding of environmental, social and corporate governance and the innovation of responses at the corporate level.

We suggest a top-down and bottom-up approach to remedy this. From a top-down perspective, there could be a positive duty to disclose how environmental, social and corporate governance is dealt with, including the opportunity for companies to state that it is not relevant or appropriate in their particular circumstances. I think that is understood as being 'if not, why not' in the current regime for listed corporations. From a bottom-up perspective, the opportunity is to actively support an industry developed approach to reporting of environmental, social and corporate governance as being corporate responsibility. With that, I conclude my opening remarks.

CHAIRMAN—As you have said, you believe that the current Corporations Law is sufficiently permissive to allow directors to consider interests other than those of shareholders but that it makes good corporate sense to do that in the context of the shareholders' interests.

Mr Mather—We find it difficult to understand why a corporation would not take these issues into account. A corporation is impacted by many different forces in the community, and what has occurred, particularly over the last decade, is that the internet, the transfer of information and the ability to exercise vigilance over corporations in a variety of circumstances are all threats to a corporation. Therefore, a corporate should be vigilant about those. Our experience is that the

issues are perhaps not factored in an appropriate time frame, meaning that we have a mismatch in reconciling the long-term interests of the company and its short-term behaviours.

CHAIRMAN—You say in your submission:

... some companies lack guidance on what information should be reported to long term investors.

Is there a particular category of generally long-term investors? Are they more likely to be what we might call mum-and-dad investors as against institutional investors? Can you identify who long-term investors are?

Mr Mather—We would say that superannuation funds are long-term investors, and the greatest tool available to superannuation investment strategy is diversification. That tool is well exercised by Australian investors. The downside to exercising the diversification tool is that you are so well diversified that you are buying all the risk of every single company in the market, and that is where part of the problem may lie in the sense that there is a mismatch for those shareholders of superannuation funds if one considers long-term risk. Often, issues of corporate responsibility are matters that evolve in years or perhaps tens of years rather than even tens of months. If any entity is likely to be holding stock in a company in 10 or 15 years time when a corporate responsibility risk may manifest—and we have recently seen that in the case of asbestosis—it is more likely than any other class of shares to be a superannuation fund, because superannuation is invested for retirement benefits, often with a 40-year time horizon. That is the class of investor.

CHAIRMAN—Typically, who would you categorise as short-term investors?

Mr Mather—Short-term investors could be hedge funds which are seeking to arbitrage a moment in time. Don Argus recently gave a speech to the Australian Institute of Company Directors where he talked about the minute investor. These are investors who are really trading for an arbitrage and exploiting an opportunity. They probably have a totally different perspective on corporate responsibility from somebody who is a long-term holder because that investor is less likely to be holding stock through the period when a corporate responsibility risk might manifest itself.

CHAIRMAN—One of the discussions that we have had through these hearings is on the problem of, for want of a better term, ‘short-termism’—

Mr Mather—Yes.

CHAIRMAN—where directors and management take a short-term view of a company’s interest rather than the longer term view. Does that indicate that this group of short-term investors to whom you refer have more influence over the company than the superannuation funds, or is the issue of short-termism and decision making as against the categories of investors quite unrelated?

Mr Mather—No. It has been suggested by some companies to my business unit that that is exactly the case. In fact, the head of investor relations for a top 50 company at the Company Secretaries Association conference in November last year did make a statement that corporate

Australia is being run by an Excel spreadsheet. The connotation of that is that, unless the behaviour of the company can be factored into a dividend discount model and into a particular cell in a piece of software on a computer, basically it becomes irrelevant. Anecdotally, there does seem to be some evidence that that is impacting on long-term returns for companies. Every time these risks manifest themselves, because they do not fall into the spreadsheet approach to investing, you are invited as policymakers to impose regulation. Have I not made myself clear in relation to that? Would you like me to run through that again?

CHAIRMAN—No, that aspect is clear. But, given that you would expect institutions like superannuation funds to be larger shareholders than perhaps some of those shorter term investors, does this indicate a lack of interest on the part of the longer term investors in corporate governance and in their willingness to use their influence as shareholders over the board and over the company? If so, what can we do about that?

Mr Mather—One would have to say that the fixation with proxy voting over other forms of active engagement leaves open the conclusion that investors are not doing as much as they might in relation to governance issues, including corporate responsibility. I refer to Justice Neville Owen, who in chapter 6 of the HIH royal commission report, in his section in relation to corporate governance, said something along the lines of, ‘If shareholders as owners do not convey their views and expectations to managements and directors, then those managements and directors will act on guidance from those interests whom they are supposed to serve.’ To paraphrase what Justice Neville Owen said, I think he said that investors have an enlightened self-interest to communicate with companies in relation to risks.

The point that I am making is that superannuation funds or long-term investors in particular have a duty to diversify to manage their risk and, in doing so, are perhaps not fully aware of the risks that they are exposing themselves to by being so well diversified, because you have agency principal issues. Let us say that I am a superannuation fund investing \$5 billion in the Australian share market in the top 200 or 300 companies, which is increasingly the case with consolidation. In terms of diversifying my manager style, I will appoint five, six or seven different fund managers; I will have a growth manager who is selecting companies based on their future earnings per share potential; I will have a value manager who is an investment manager who is buying companies that typically have a high dividend yield and a low price-to-earnings ratio; and I will have a quantitative manager who just uses a computer to choose the stocks et cetera. Each fund manager may be buying only 20, 30 or 40 stocks in order to execute their mandate, but when you aggregate everything back up at the super fund level the reality is that, if the super fund has done its job properly, they own most of the top 200 companies. An analysis of portfolio shows that that is largely the case. This is where this concept of permanent share ownership arises.

I invite the committee to consider the issue of whether or not permanent share ownership and that positive aspect of diversification bring with them a duty to exercise ownership behaviours which include active dialogue with companies. In today’s environment, if you were a large superannuation fund and, for example, if you were unhappy with the banking sector, your risk management process would be very unlikely to allow you to have zero exposure to the banking sector, given that it comprises 25 per cent or thereabouts of the conventional benchmark.

CHAIRMAN—If this is one of the ways in which we can tackle corporate responsibility more effectively—and certainly sustainability—how do we encourage them to interact with those companies in a more effective way to achieve that?

Mr Mather—We are suggesting a top-down, bottom-up approach. From the top down I think it is a signalling opportunity. I want to underscore that we have presented the view that regulation will not solve this. That means providing the right signals that it is appropriate and expected that long-term investors do take a longer term interest in relation to the corporation. From the bottom-up perspective, though, all shareholders could well say that they are not well served by the current level of disclosure and reporting by companies, because if they were to try and exercise vigilance on those issues, the amount of reporting would not allow them to. I draw your attention to the second page of our submission to your inquiry. Section (a) says:

The extent to which organisational decision-makers have an existing regard for the interests ...

At the bottom of that page, our review in 2004 of reporting by companies found as follows:

More than half of—

the top 200 companies—

did not ... disclose information on their processes to protect against violations of consumer privacy.

The third point there states:

Nearly half ... of ... companies did not publicly disclose policies protecting whistleblowers.

Yet we know from experience that in the resources sector a no-blame policy in relation to health and safety has seen a massive improvement in health and safety and has facilitated innovation in relation to those areas. I do not want to be construed as suggesting that these are two indicators that are the key aspects of corporate responsibility, but I want to give the committee a flavour for the fact that some of the things that do impact on shareholder value—and we are seeing ethics and some of those issues right now materially impacting on the valuation of companies—are not well discussed in the case of corporations. We need to have a two-pronged approach. Yes, we need to tell all investors that they need to be more alert to these issues. But, secondly, we need to ensure that when they are alert there are the appropriate signals so that they can exercise what Justice Neville Owen clearly indicated was a fiduciary duty, in our view, to exercise vigilance.

CHAIRMAN—You have indicated that, typically, the long-term investor is the superannuation fund. Is there a need perhaps to encourage other categories of investor to be longer term investors? If that is the case, would the capital gains tax mechanism be one means of doing that? In other words, rather than having the current concession we have for capital gains tax, you could have a system whereby the capital gains tax was on a sliding scale downwards, based on the length of time you held your shares.

Mr Mather—That is a thought that we have not given specific consideration to. However, it does have the potential to align interests more strongly in terms of the tax regime. So that is one potential policy response available. I do have to say, though, that from an institutional

perspective an institution is already holding stock for a long time anyway, regardless of the capital gains tax implications, because of risk diversification.

To give you another example, if I am a large institution responsible for a \$1 billion or \$2 billion portfolio, if I am to deliver a return which is benchmarked to a conventional benchmark, such as the ASX 200 or 300 index, and BHP makes up eight per cent of that index, for all intents and purposes holding four per cent of BHP stock in my portfolio is akin to having a very strong sell recommendation on the company. In other words, no matter how much I might want to sell the company—and I do not want to make a comment about BHP positively or negatively—if I want to have a strong sell on the company, I cannot afford the risk of having zero exposure, so I will hold that floor. There is a de facto floor and ceiling on institutional holdings. Nobody wants to talk about this, because it is rather boring to talk about, but it is the reality.

And I think this is why we are having this discussion. It is exactly that whole mind-set and the mismatch between time horizons that give rise to the approach: ‘We can simply trade the governance of the company. We can pre-empt the issues.’ Fund managers are intelligent people and they quite rightly believe that they will not be holding the stock when a risk manifests itself. Yet we have seen in a number of instances—and I dare say that is part of the reason for the constitution of this committee—that institutions and others have been holding stock when those risks have occurred.

I think you have already got the point that I am trying to make: the longer the time over which we measure investment performance, the more the interests of the shareholder and corporate responsibility will converge as one. But, if you measure these issues in time horizons of three, six or nine months, you are less likely to find that occurring. If you look at the case of the share price of James Hardie after they announced the decision that the board made, the share market supported that very strongly; the share price rallied very strongly immediately in response to that decision. So, measured over a certain period, the directors of that particular company had very much safeguarded the interests of shareholders. If you measured it over a longer period, you might come up with a very different conclusion. That is really the point that we are trying to make.

Going forward, we are likely to see more interest in trading managed funds, including superannuation, so it is important that we try to head off the rise and rise of short-termism, through more disclosure and encouraging the idea that these issues are relevant investment issues. That signal is not being adequately conveyed to companies—witness my anecdote about the public statement by a head of corporate relations that corporate Australia is run by an Excel spreadsheet and also the statement, by the same individual, that they are confident that companies are not making decisions that are in the interests of the company over a 10- and 20-year time horizon, because they will not be rewarded in the market.

Now, we cannot interfere in markets but we can go a long way towards improving the understanding of investors in relation to what really goes on within a corporation. And believing that the current reporting of P&L is an appropriate diagnostic as to a company’s future prospects is clearly insufficient—it is necessary but not sufficient.

CHAIRMAN—Is the short-term nature of senior executive employment contracts also a factor in the short-termism issue? And, leading on from that, are you aware of any corporations that link corporate responsibility performance to remuneration packages; if so, how?

Mr Mather—Yes, there are some companies. In particular, there is one building materials company that I can think of whose chief executive suffers a seven per cent diminution in their performance bonus for a death in the workplace, and that is cumulative. So, in that instance—and this is an adverse example—if 13 people died, you would get no bonus. In terms of other companies, I am aware of one company where the chief executive's performance bonus is measured against, in part, international ratings in relation to global responsibility; I think in that case it is the Dow Jones sustainability index. I think it would be fair to say that these are the exception rather than the rule. The typical performance bonus is based on the 12- or perhaps 36-month total shareholder return or the earnings per share, or a 50 per cent weight to each of those measures. So the assumption would be that corporate responsibility is going to be manifested in the share price during that period.

Senator WONG—We have talked a fair bit about short-termism and you have identified a number of drivers, primarily the way the market views information and what the market rewards. Can you talk a bit more about those drivers of short-termism, because I think then we can start to think about what can be done about them.

Mr Mather—One of the drivers towards short termism must be the education process which analysts have gone through. We can look at the last 10 or 15 years of accountants and others being educated in the university system. I am an example of that. When I was doing an accounting degree at the University of New South Wales, sustainability was not in the lexicon at all. Many of my peers are now investing in companies, and, in defence of investment professionals, sustainability is not a tool which has ever been in existence. The capital asset pricing model and the efficient market hypothesis are key drivers of how markets are viewed, and the issues of sustainability and corporate responsibility being a risk are new factors. The point that I am making is that investment professionals have not historically necessarily had the tools.

Senator WONG—Has there been any shift in that?

Mr Mather—There have been some shifts. A lot of the work that is being performed in this regard is being driven by the United Nations Environment Program.

Senator WONG—I meant in terms of the education of analysts.

Mr Mather—Yes. For example, two years ago I gave a speech to the final year students at the accounting faculty of the University of New South Wales. Those students were reading the same current material from the *Harvard Business Review* and other material that I and my team use as part of our vocation.

Senator WONG—So there has been a shift.

Mr Mather—There has been a shift, but that is not coming through yet in terms of the manifestation of investment processes. Some work is occurring, but I could not say in relation to

all universities the extent to which this is a core rather than an optional process. I think the other thing that we have to be mindful of is that the way investment management is lauded and rewarded is another contributor. Many times I have criticised the media for having the 10 best and 10 worst equity managers measured over a one-month period or three-month period.

To put that in perspective, measuring the one-month return on a managed fund in the equity space, investing in Australian shares, is like measuring an 87-metre segment of the Commonwealth Games marathon in Melbourne. It is very much analogous, the reason being that a marathon is 42 kilometres and superannuation has a 40-year time horizon. It is a useful analogy. We would not measure a marathon in that way, so why are we so fixated on using that kind of measurement? It is a real issue. Investment managers with the best intentions in relation to corporate responsibility know that their livelihood and their performance bonus are dependent upon how they perform over at least a 12-month period.

Having said that, BT Financial Group, for example, has changed it so that at least 60 per cent of the analysts' rewards are weighted towards three-year periods. I could not speak for other funds managers. The point I want to make is that there is some shift in that regard. But I could not give you evidence in relation to where the industry stands. There would be others better placed.

Senator WONG—They are some drivers of short termism. Is there anything else you have not alluded to that you would like to?

Mr Mather—The issue that the committee might want to draw its attention to is that of superannuation. We now have a choice regime for superannuation whereby, including internet transactions, you are likely to see more, not fewer, transactions in relation to managed funds. The Senior Economist of BT Financial Group, Tracey McNaughton, has recently completed a 34-year study, which started in the seventies, of BT retail managed funds involving 850,000 investors and I think six million transactions per day, to study investors' behaviours in managed funds. The evidence has shown that some investors, particularly as they reach the age of 50 or thereabouts and particularly men, are more likely to make suboptimal investment decisions. There is a separate paper available—

Senator WONG—What happens when they are 50 that makes them throw caution to the wind?

Senator MURRAY—Come outside and I will explain it to you!

Senator WONG—Thank you very much.

Senator MURRAY—It is probably to do with the male menopause.

Mr Mather—There is more work to be done in that area, but anecdotally the experience is that your superannuation fund investments or other investments sit there until you get to the age where you see retirement on the horizon and you start thinking about how to manage them. Typically at that time investment decisions tend to become more active. The thesis that McNaughton and others have put forward is that, unfortunately, men are more overconfident in their decisions and suffer from that as a class of investor.

As I say, there is more work being done. If you take that study and apply that to the regime that we are now looking at, where we are encouraging individuals to be more active with their superannuation, there is a real risk that the individual is more likely to understand three-, six- or 12-month type investment performances. Unless encouraged at the policy level, it is a lot harder to keep one's eye on the five- and 10-year type of investment horizon in that competitive environment.

CHAIRMAN—Could that study be made available to the committee?

Mr Mather—Yes, it is a document we can make available.

Senator MURRAY—You could send it electronically, if you have it.

Mr Mather—Yes.

Senator WONG—First, are there any other drivers of short termism you want to comment on that you have not already raised?

Mr Mather—As drivers I think they are the key issues. The manifestation of all those considerations in our view is that corporate Australia is also not being given a sufficient quantity of the right signal in relation to corporate responsibility.

Senator WONG—You talked about, in the absence of policy mechanisms essentially, the fact that the horizon under which corporate Australia is going to be forced to work—or with this great incentive for them to work—is naturally shorter than you might suggest is appropriate. I suppose I would start with this: what sort of policy action can be taken to try to encourage a longer term approach? There is the extraction of value for that. That is the key issue. I think what you are saying is that the Excel spreadsheet comment essentially says, 'What is the point of us looking at long-term value and managing our long-term sustainability risks if the market really is not valuing it?'

Mr Mather—I think the Reserve Bank has demonstrated the strength of signalling as opposed to, necessarily, regulation in influencing markets. So that is a precedent. Therefore, for your committee there is the opportunity to make very clear to corporate Australia, in relation to the legitimacy of these concerns. The imperative of appropriate consideration is, I believe, the primary tool that you have. The option then would be to encourage industry—I have reviewed the many other submissions that you have received—to walk the talk, as it were, in relation to the offer to innovate and be vibrant in providing a response in this area. After that, you may well find yourselves in a position some time down the track, if nothing occurs, perhaps wanting to regulate, which is the concern that has been expressed widely. There is a nice alignment of interests. There is an incentive, if you were to telegraph that, that industry innovate and provide a market driven solution in order to head off the need for a regulatory response, if the committee were to conclude that there is insufficient work being done in this area.

Senator WONG—When you say signalling you mean signalling the possibility of future requirements in the absence of business responding? Is that what you meant when you were referring to signalling?

Mr Mather—I mean signalling on two fronts. Firstly, signalling very clearly that these issues are legitimate issues and that it is appropriate to take them into account. Whilst I am aware of submissions that refer to the fact that company directors might need a safe haven in order to take ethics and other issues into account, we do not support that proposition. As I said in my opening remarks, there is an implied positive duty to take these things into account for the simple reason that they impact the value of the company over time. That message is not understood.

Senator WONG—There is a distinction between how we would want to think about what are the best interests of the company on what the plain reading of the section discloses and what the case law has said about that. I think that in some ways the argument is at two levels. I agree with you. I would have thought that, just at a very practical level, if you wanted to talk about the best interests of the company that surely would encompass at least the management of the sorts of risks you outlined in your opening submission. But I think there is an alternative view from the lawyers, essentially, about what the case law actually says. It is a different argument but I think we get caught up in that a bit.

Mr Mather—I am not aware of a situation where a company has detracted value, on any basis, by taking into account ethics and the views of community and others. Industry leaders such as Don Argus have gone out very publicly and commented about the importance of these issues in terms of the shareholder value. But, whatever the lawyers may want to argue, from the market's perspective it does impact risk and therefore it should be taken into account. We must signal very clearly that it is not inappropriate to take these things into account. There is also the opportunity to invite the innovation that, from my understanding, the business community and others want to embrace in this area in order to avoid regulation. I think that is one aspect.

There is a lot of talk going on at the moment, in relation to industry groups, in regard to corporate responsibility. In fact, from a meal-ticket perspective, there is no better meal ticket than organising conferences in this particular area! That is a problem in itself, because it results in fragmentation and a cottage-industry approach. We would invite you to consider the constitution of a task force which brings together the various groups who are having these conversations under one roof to oversee the development of an appropriate, market-led—and I want to underscore 'market-led'—response to these issues, but one which brings it together as one comprehensive response, as opposed to the many different conversations that are occurring at the moment that do not seem to be getting the traction that we might wish.

Senator WONG—How would you deal with that? That is, essentially, my next question: what do you say government can do? How would you deal with the different sector perspectives in such a task force? Do you understand what I mean?

Mr Mather—When you say 'sectors'—

Senator WONG—The extractive industries will have a very different view from the service industries about what their risks are and how they should manage them—let alone what the companies within that might think.

Mr Mather—I think that in terms of disclosure and behaviours, the sort of 'if not, why not' regime is appropriate and, to be most effective, companies should disclose in these areas as is appropriate to their exposure to risk. We are not suggesting that companies should not be

allowed the opportunity to make clear that they are not exposed to corporate responsibility risks and therefore that is the end of the matter.

In the case of a listed investment company—which is a company that exists simply to invest in other companies—you could think of them as being in a class, in regard to disclosure, which might legitimately say, ‘We have no exposure to these issues.’ I am not putting that forward as a fact—I am putting that as an example relative to an extractive industries entity.

There are a number of areas, though, of corporate responsibility that are valid, in terms of the behaviour of the company in relation to its attractiveness to labour or its human capital and in relation to its access to resources. There may be no need for access to resources but the industry group could come up with classes of risk and companies could disclose whether or not they are exposed to those.

Senator WONG—Are you talking about a government and business task force—drawn from government and members of the business community?

Mr Mather—That is correct.

Senator WONG—The work that I think you are involved in, Mr Mather, in terms of the ASX corporate governance guidelines and the consideration of Senator Campbell’s reference—is that essentially doing what you are suggesting, or are you looking at a broader rubric?

Mr Mather—I believe the opportunity continues to have a broader perspective on these issues. The ASX corporate responsibility working group, for example, is not considering issues in relation to how companies might report the sorts of interests that, for example, some of the accounting and auditing professionals might want to contribute to in relation to providing a more comprehensive response.

Certainly, a number of the relevant bodies, such as the Institute of Company Directors and the Business Council of Australia, are sitting at that table. Whilst it is a diverse group—and a good and productive group—it might be more broadly constituted. Also, remember that it is actually a small subcommittee of the overall corporate governance council. This is an area where there is an opportunity from a policy perspective for a greater signalling of leadership in our view—bringing those groups together.

Senator WONG—Can I just go back to your view as to where Australia is, compared to other countries, in terms of long-term risk—which I think is the language you used to describe it—or sustainability of corporate responsibility, as others describe it.

Mr Mather—In relation to being able to examine the exposure of Australian companies to risk, we lag behind the rest of the globe quite substantially. KPMG have done work in this area, with a report commissioned, I believe, by the Department of the Environment and Heritage, which showed that Australia ranked about 14th of 16 OECD countries. In terms of providing information—

Senator WONG—Is that in terms of environmental risk?

Mr Mather—That is in terms of social and environmental reporting. That is not about the exposure of the business activity; it is about communicating with markets about how governance is exercised in relation to those risks.

Senator WONG—So Australia was 14th out of 16?

Mr Mather—My recollection is that it was 14th out of 16. We could locate that report and send it through to you.

Senator WONG—That could be useful.

Mr Mather—Certainly there is no dispute that Australia lags in disclosure in this area. That impacts Australian companies in relation to their trade with countries and areas that do have a more advanced regime of behaviour in this area. For example, if you are seeking to transact in the UK or the European Union, this becomes a relevant issue. Many corporations would be able to give you evidence on how it impacts their business.

Senator WONG—Is that one of the drivers behind the take-up of GRI reporting or something similar by Australian companies operating in those jurisdictions?

Mr Mather—I think that is part of it. Also, from our observation, there are some companies that recognise that there are risks associated with corporate responsibility and that having a robust evidencing of how those risks are managed is in the company's enlightened self-interest. If you look at the number or classes of companies that report in that way, the unfortunate reality is that many of those companies have had a most adverse experience themselves and it is a reaction to that experience that results in the reporting. There are many examples of companies, and I am happy to share with you that that is one of the drivers for them. From our perspective, from a markets perspective, the value creation in trust in financial markets and the value creation in stability of investment performance are gained by pre-empting these issues and ensuring disclosure so that investors can pre-empt these issues rather than just react to them.

Senator WONG—You essentially argue for a stepped approach—I do not know if that is how you would describe it. On page 5 you are essentially saying, 'Expand the matters against which you report or the risks that you report your management of under principle 7.' Is that an interim step in the absence of a more comprehensive, standardised framework?

Mr Mather—Yes, it is our view that Australian companies are not yet ready for a completely standardised framework, because of the concentration of the Australian market and the various levels of understanding that companies have in this regard. So, therefore, to some extent, it is a matter of simply ensuring what already exists under principle 7 of the corporate governance guidelines:

The risk profile should be a description of the material risks facing the company. Material risks include financial and non-financial matters.

It is widely recognised that Australian companies provide very little disclosure in relation to non-financial risks. Asking companies to report to a particular framework might be unhelpful at this juncture because companies in some instances do not actually understand what their non-

financial risks are. Therefore, the stepped process of encouraging them to address their mind to that issue first and then asking them to report to a framework might be a better approach, particularly if there is some public development of some sort of a framework led by industry that might assist companies in terms of being ready to report on some of those sorts of issues.

Senator WONG—I have two final areas to ask you about. One is super trustees. You made the point—and I am going to press you on it a bit—that we ought to consider whether essentially permanent share ownership by superannuation funds should bring with it certain responsibilities. What were you getting at?

Mr Mather—Some years ago my business unit was approached by superannuation funds—so this is their idea, not ours—in order to recognise this risk and that they have an interest in engaging companies in relation to heading off risk, because the value is in preventing risk, not in responding after the event or trying to game the system in terms of trading risk if you can head that off. There seems to be a lack of understanding that large institutional portfolios tend to be measured by individual investment mandates, as opposed to a whole-of-portfolio approach. Superannuation trustees have an opportunity to take a more active focus on the long-term behaviour of companies.

One would have to say, from a governance perspective, that the focus is far too heavily weighted towards executive remuneration relative to the various other forms of risk that can manifest in terms of impacting the share price. If you think of the raft of issues that impact on a company's performance, and the fact that companies are now providing some 27 pages of remuneration disclosure and, in some cases, zero pages of disclosure in relation to non-financial risk, it invites the question as to whether or not the balance is appropriate. There is no class of investor who might be more interested in the appropriateness of that balance than a superannuation fund.

Senator WONG—Should government have a role in impacting on that? If so, what can it do?

Mr Mather—If the committee were to form a view in this area, we would invite you to make sure that that view is very well understood and to give the market the opportunity to respond, knowing that if a response is inappropriate at some future point in time then you may wish to strengthen the way in which you deal with the issue.

Senator WONG—What could you get super fund trustees to do?

Mr Mather—Trustees should be having a dialogue with companies in relation to the various risks that they have. They should be asking those companies to report to—

Senator WONG—Via their managers, presumably.

Mr Mather—Via their managers so, therefore, intuitively you would be writing it into your investment mandate that these issues shall be reflected in the way that the mandate is constructed. I am not aware that investment mandates are currently constructed on anything other than basis points performance measured over certain time periods.

Senator WONG—One of the points that was made to us is that there was a suggestion that the sole purpose test might create a bit of difficulty for trustees in a similar way to the way directors' duties is argued by some to create a difficulty. Do you have a view about that?

Mr Mather—I believe that there may be some substance that the understanding of the sole purpose test may have an impact. Having said that, I think that it is not to the stage where, from our perspective, we are talking about directing companies to invest in certain classes of business—for example, to move away from fossil fuels to renewables.

Senator WONG—You are saying you have to engage to manage risk. Isn't that essentially—

Mr Mather—That is all they are saying. Therefore, from our perspective, we do not see that the argument holds water in relation to the sole purpose test. But I agree that there are many who believe that it may be holding them back and I think that is a question of education as opposed to fact.

Senator WONG—Are there any other government initiatives that you want to talk to us about?

Mr Mather—They are the main areas. There is certainly the opportunity to signal and to have a comprehensive approach to this area, if the committee believes that it is a valid concern, and that would be a better approach than the fragmented approach that is occurring, not necessarily with sufficient consultation. There is industry consultation going on at various levels, but you are in a position where it is perhaps difficult for you to be aware of the extent to which that consultation is occurring amongst the various stakeholders. By constituting that group, you could make sure that you have appropriate oversight and that your policy objectives are being matched by what industry might be developing.

Senator MURRAY—I want to stay with the institutions, the investment funds. I was interested in you quoting Justice Owen. You said that he had said that institutions have a fiduciary duty to exercise vigilance. I have long argued that case, because I have an essential view that superannuation funds and investing institutions hold shares in escrow, in trust, for the beneficial shareholder. Attached to that view is a view that they do not exercise, or do not fulfil, that trust in a number of important respects. That does not mean that is universally true. I have noted that organisations try to ensure that corporate governance rules are laid down, and they press for them to be abided by and so on. But you had said earlier that you did not think that regulatory mechanisms should be applied. I might agree with that proposition with respect to corporations. I do not agree with that proposition with respect to the investing institutions, because they are not doing their duty.

I would ask you what your reaction is to a few mechanisms which one might consider. The first is mandated voting. You remarked on proxy voting. I think it is impractical at this stage to require institutions to vote on all resolutions, but I do think that they should be mandated to vote on what I regard as the three most important: constitutional issues, election of directors and the remuneration of directors, because it is a very big issue.

The second thing I think it is possible to consider with regulation of the investing community is that the investment funds should be required to report as to what they have done to

pressurise—interact with, manage, consult; use any word you like—to ensure that proper risk management processes, particularly with regard to the CSR area, are being undertaken by those companies in which they invest. That would mean, of course, that they would have to develop a view across their portfolios and they would have a common approach, which I think would have the effect of ensuring that companies react appropriately. In that process you allow them to develop, against the international trends, the kinds of mechanisms they use. Those two measures, I think, would quite significantly improve corporations' take-up rate of these issues, because the investing community would be requiring it. How do you react to those propositions?

Mr Mather—In relation to mandated voting, we would propose—and I think there might be agreement here with your proposition—that many of the issues put forward for voting are routine. It has been put to me that there are large institutional investors investing portfolios of above \$1 billion, and in one instance there were 1,712 resolutions that they were required to vote on and to report on. The concern there is more in relation to reporting and the value of disclosing the extent of each of those resolutions and how each of those resolutions had been voted on.

Senator MURRAY—Which is why I have isolated the three most important.

Mr Mather—Yes. That is one arm of governance that is open to consideration. I would provide a counterview that, whilst those issues are relevant, particularly from a corporate governance perspective, the issues relating to corporate responsibility that manifest in risk almost invariably will never reach the proxy voting sheet or the annual general meeting of a company, because of the nature of the sorts of risks that give rise to corporate responsibility.

Senator MURRAY—I accept that. What I am talking about is a greater engagement in terms of a fiduciary duty. You have to then take into account a number of issues. Of course, the corporate governance area has been developed precisely because of concerns. You have the mandatory voting area, you are talking about a further area of required reporting on CSR and you might have others you could offer.

Mr Mather—Are you happy to move away from the mandatory voting on proxy voting?

Senator MURRAY—As long as you agree with me, I am happy to!

Mr Mather—I do agree with the spirit of what you are expressing. I have to say that my view—and this is my view—is that I am concerned that proxy voting dominates the corporate governance landscape because, from an institutional perspective, proxy voting on contentious issues is shutting the stable door after the horse has bolted. What I mean by that is that, if there is a concern in relation to the directors' remuneration, that issue should be raised prior to the AGM because, by the time it gets to being proposed by the directors, the directors have nailed their colours to the mast. It is very unlikely that a director is going to want to remove those colours, other than in a very public and embarrassing way.

Senator MURRAY—Can I give you a counterproposition? If mandatory voting on remuneration were required, I think what would happen is that companies would go to the institutions beforehand and say, 'This is the package we are proposing.' In other words, it would be pre-vetted and it would not be after the horse has bolted. The problem at the moment is that, because it is not mandated—it is voluntary—there are still occasions when the first time the

institutions might look at it and they might decide to vote or not is once the proposition is presented publicly.

Mr Mather—In relation to that aspect, I agree. You will be heartened to know that certainly a number of company chairmen are now doing the rounds and consulting beforehand.

Senator MURRAY—Yes, I have seen that.

Mr Mather—It will not be a surprise to you, of course, that those company chairs who are taking these issues around are invariably those who have thought about the issue and for which there is no contention. Where there is contention or there is a lack of thought, it is less likely that that is going to be correlated with consultation. The point that I wanted to make is that, in the balance of governance in most markets, the weight accorded to proxy voting does seem to be disproportionate compared to the issue of engaging and acting as a share owner.

Senator WONG—Sorry, can I interrupt for a moment? You have used similar phrases three times now: you have described the dominance of proxy voting, the obsession with proxy voting et cetera. Whose obsession?

Mr Mather—The obsession of investors and the various interest groups that are pushing investors.

Senator WONG—Overreliance on it as a mechanism for change?

Mr Mather—That is correct. The risk is that it becomes so dominant that it is viewed as a necessary and sufficient arm of governance as opposed to a necessary but not sufficient arm of governance, which is where I believe we would agree with your proposition. I will turn to that now in relation to disclosure regarding engagement. Certainly it might be open to having a voluntary disclosure requirement in the sense of ‘if not, why not’, to disclose what engagement activities have occurred or why it was not necessary.

Senator MURRAY—By the investment institution.

Mr Mather—Yes, but when you say ‘the investment institution’ are you talking about the fund manager or the beneficial owner?

Senator MURRAY—You get both super funds which are constituted as such and investment vehicles. What I am suggesting is that both classes hold shares in escrow. What I am suggesting is that they would be required—it would not be voluntary—to report as to what efforts they have put in to ensure that CSR, in the risk sense of that, is being observed and pursued in those companies that they invest in. You would probably need to set a significant market share. The reason I put it like that is that, if you are going to drive a market response, if it is driven by the investing community, I think it is likely to have a hastening effect.

Mr Mather—Where would you see that incidence of reporting being imposed—because before I was describing the institutional investment market as being the superannuation fund at the head of the table, as it were, which might have six, seven or up to 15 service providers conducting that investment mandate for them?

Senator MURRAY—Whoever has the material or primary responsibility. If the delegation of the authority to a fund manager is, ‘This is the investment mandate; now you go off and realise that,’ then I would suggest that it lies with the fund manager. But I am not trying to design it now, because I think that gets into a different discussion. I am interested in the proposition that I am putting to you, because the proposition principally put to us is that, if we are going to change regulation, we must change it with respect to corporations. I think the alternative proposition is that you put that regulation with respect to the investors and only those investors who hold shares in trust.

Mr Mather—The fund managers are in a position whereby they are given a mandate, and that is a contract. They are to behave in relation to the mandate that they are given, and if they are contracted to do something they must do it. If it is not in the mandate, then it is unlikely to be done. You do not normally perform additional duties that are outside of the contract, and the measurement of investment performance in mandates is typically in relation to percentage out performance against an agreed benchmark. Therefore, from a fund manager’s perspective, the issues of corporate responsibility and governance will be manifested by trading in and out of companies based on the fund manager’s view in relation to those issues.

Senator MURRAY—Are we talking past each other here? I am not sure you understand—

Mr Mather—I am not sure how the fund manager is going to manifest that, because typically a report—

Senator MURRAY—But you are getting involved in the mechanics.

Senator WONG—He is a practical man.

Senator MURRAY—I am a practical man too. But earlier you said that one of a number of principal opportunities to change corporate behaviour is if those who manage the investments engage more with the corporations with respect to longer term risk. I am paraphrasing my understanding of what you said. If you are going to do that and you cannot get the investment community to do that—some are doing it but not all—then the opportunity is for government to say to the investment community at large, ‘This is what we require you to do.’ It goes beyond what they are doing now. It is a new obligation, which some are probably carrying out already. The question you are asking in answering is: at what level would the reporting rest? That can be resolved later. The question I want to ask you is: do you think that, if government regulated the investment community to require a CSR, particularly with respect to the risk area—because not all CSR relates to risk—that that would be effective? If you do not think it would be effective, tell me, but I do not really want to hear about ratios and this and that.

Mr Mather—Then the short answer is that, given that companies have a disclosure obligation under the corporate governance principles to report on an ‘if not, why not’ basis in relation to mainly corporate governance issues—and we could argue that that includes corporate social responsibility issues—then it is hard to see that there would be an argument that investors should not also provide some counterbalancing disclosure in relation to how they have manifested that. Is that what you are suggesting?

Senator MURRAY—I am suggesting that you would not apply that regulation to companies at all; you would apply it to the investors. In fact, I am asking the question—I am not suggesting it at all.

Mr Mather—I do not believe that you can alone impose it on investors, the reason being: which class of investor? You are only talking about institutional investors.

Senator MURRAY—I am talking about those who hold shares in trust.

Mr Mather—Yes, but if companies are not disclosing where they stand on some of these issues then it is very hard to be informed. What I am saying is that I think you need both. You cannot have one incidence of imposition on the investor in order to achieve what you are describing.

Senator WONG—Because they will not have the tools—is that your evidence?

Mr Mather—You will not be informed. If I am an investor and I have this reporting obligation in relation to what I have done because I hold shares in trust for others, how am I to inform myself in relation to the behaviour or attributes of the companies in which I am investing if there is not a source of that information?

Senator MURRAY—Let me give you a simple example because I am not at all sure that you have understood me. If a superannuation fund says, ‘We will not invest in any company that does not have a stated policy on its website and in its formal, agreed processes concerning bribery and corruption,’ I think that, within a transitional period, they would all have it. That is dictated by the investor. If you are seeking for key corporate social responsibility mechanisms to be instituted in a market situation in a relatively unregulated situation, that is the sort of mechanism you apply. To an extent, that is what has been done with corporate governance. You started right at the beginning by saying, ‘No regulation.’ If you applied that regulation to investment institutions and said, ‘It’s your job to ensure that CSR applies in key areas,’ particularly those attached to risk, and you do not give them any direction whatever but just tell them that that is an imposition they have to go for—or you give them some direction, I presume, with guidelines and so on—would that be effective?

Mr Mather—I am having difficulty answering that question in the affirmative because the fund manager who is awarded a mandate to invest in certain parts of the market—for example, ASX 200 shares—is going to believe that they are looking for those issues as price signals and will trade those stocks.

Senator MURRAY—But they don’t. You are in the business and you know that they don’t. The number of performance audits, risk audits and insurance audits and the number of proper, long-term appraisals that go on are quite limited.

Mr Mather—I am differentiating between the various fund managers who are investing. Various fund managers, typically from an institutional perspective, are investing in a slice of the market. They will have a particular style where they buy certain classes of companies because that is their investment philosophy.

Senator MURRAY—Against a very narrow range of criteria.

Mr Mather—Yes.

Senator MURRAY—And primarily on a short-term basis.

Mr Mather—And the super funds are selecting a variety of those funds manager approaches and aggregating those in order to have a diversified approach to investing in the market.

Senator MURRAY—That is still on a short-term basis and on narrow criteria. You find me a super fund that actually genuinely takes a 40-year risk assessment and I will be absolutely shocked and amazed. I actually do not think it is possible to do that, by the way.

Mr Mather—The issue that has been put to me by one superannuation fund investment officer is that they would be willing to do that, but if they did give an investment manager a 10-year mandate to invest, the concern would be that the manager would not necessarily be appropriately incentivised. They could put their feet up and would not have to worry because they were locked in for 10 years. So there is a bit of an agency principle issue in regard to that time horizon as well. You become a captive client if you award too long a mandate. In terms of your question in relation to disclosure, in broad principle there is an opportunity to encourage some sort of a disclosure regime. But the idea of mandating—saying that you must disclose because you must behave in a particular way—is I think where we would say that that might not be helpful in terms of innovation in the market.

CHAIRMAN—I put one proposition to you as a final question. It was the proposition put to us by Dr Gary Johns. In his submission, he wrote:

It is my sincere belief that Corporate Social Responsibility is a discourse promoted by non-owner political interests wishing to use corporate wealth for their own ends. Some wealthy corporations promote CSR as a means of forestalling such political action, but also to enhance their appeal to employees and customers.

In the first instance, the Committee should give no comfort to non-owner interests by changing the responsibilities of directors, nor should it lend legislative weight to any scheme that measures CSR, because this serves to undermine directors' duties. As for corporations that use CSR as competitive tool, there is no reason to intervene.

What is your response to that statement from a witness we had here yesterday?

Mr Mather—It is an interesting statement. It is difficult to see that, where corporate responsibility issues give rise to risks—and they do—it is not appropriate that a director should give their mind to that issue. In relation to the specific example of labour, interestingly enough we are, on any measure, entering an era of constrained labour—we are looking to employ older workers et cetera. Therefore, the notion that corporate responsibility connotes flexibility which is negotiated at the individual workplace to make sure that that workplace is attractive to that class of labour seems to make all the sense in the world if you want to make money. It is very difficult to see that a director who is wanting to make money in the long-term interests of the company is in breach of their duty.

CHAIRMAN—Thank you, Mr Mather, that has been very helpful.

Mr Mather—Thank you.

[3.09 pm]

SIDOTI, Mr Eric, Consultant, Compact Consulting

VAN BEEK, Mr Harris, Consultant, Compact Consulting

CHAIRMAN—Welcome. The committee has before it your submission, which we have numbered 12. Are there any alterations or additions you wish to make to the written submission?

Mr van Beek—No.

CHAIRMAN—I now invite you to make an opening statement, at the conclusion of which I am sure we will have some questions.

Mr van Beek—Thank you for giving us the opportunity to contribute to this important inquiry. To provide some context for our comments, we want to take a few moments to explain our experience. Most of Eric's working life has been involved with public policy and the practical implications of such policies. This has frequently involved building alliances between various components of society. His work with the Catholic Justice and Peace Commission in the mid-eighties focused on examining the key issues facing Australia at that time, many of which, though different in form, remain current. In a range of roles with Amnesty International in Australia and internationally, he led the establishment of alliances to focus on changing social attitude and behaviours. During his time with Amnesty's international secretariat, Eric had prime responsibility for Amnesty's work on human rights, economic and corporate relations. This required, amongst other things, establishing AI's policies and relations with the World Bank and the development of international policies and actions with respect to transnational corporations. His subsequent work has also required him to establish working relations with businesses. Since the early 1990s, Eric, through his work as a consultant with the Dusseldorp Skills Forum, has had a recognised influence in Australian schooling and training. This has included a direct interest in the relationship between education, business and the community.

I too have worked for Amnesty International for many years, including as the National Director of Amnesty International for 13 years. For six years from 1996 to 2001, I was the chief executive officer of a Commonwealth funded agency known as the Australian Student Traineeship Foundation and subsequently as the Enterprise and Career Education Foundation, which had a role to build local partnerships between schools and businesses to create opportunities for young people to have workplace learning opportunities during their senior years at school. Forging stronger links between the needs of business and education and young people's aspirations has been critical to this undertaking. During my time at the Enterprise and Career Education Foundation, student participation grew from 2,000 to nearly 100,000 throughout Australia. Business participation grew from a few hundred to over 50,000.

Largely in the 1970s and eighties, Australian businesses moved away from providing entry-level training and much of the other pre-existing, on-the-job structured learning. My role was to partly change corporate behaviour so that businesses would again play an integral role in Australia's skill development and workplace participation. In 2000, I arranged a high-level

delegation to Europe to research the various approaches to encourage business participation in the training needs of societies while at the same time meeting the immediate business needs of individual enterprises.

Both of us have extensive and influential experience in the development of public policy. However, for this inquiry, of more significance is our understanding of the complexities and practicalities of leading social and cultural change, including amongst businesses. In appearing today, we wish to emphasise the following key matters: what are our Australian society's expectations of corporations? Do corporations currently meet those expectations? If not, what can be done about it?

I turn to the first: expectations of corporations. In Australia, there is no clear statement of the expectations of corporations. For example, the Corporations Act does not have a preamble setting out the context for the act or the purpose of Australia establishing the privilege of corporate status. As a consequence, consideration of appropriate corporate behaviours is severely hampered by the lack of a common Australian understanding of the nature of the corporation. We appear to ignore the fact that corporations only exist by virtue of statute and that they are granted particular privileges to achieve social goals. As a society, we are not clear about what those privileges are, and, more significantly, we have not articulated the social goals to be achieved. The second consequence is that the identification of effective approaches and related mechanisms is challenging in the absence of such clarity. In the absence of such considerations, it is very difficult to establish just what changes in corporate behaviour our society is trying to achieve under the rubric of corporate social responsibility.

Are Australian society's expectations of corporations currently met? While it is not possible to provide a definitive answer, there are ample indications that Australians are not happy with corporate behaviour: the extent of anger regarding the social impact of the closure of banks' local branches; the cabinet decision to prevent Shell's takeover of Woodside because Shell was not seen as an appropriate Australian investor; concerns associated with the behaviour of companies in private-public partnerships, such as Sydney's Cross City Tunnel and the management of immigration detention facilities; concerns regarding the levels of remuneration of senior executives, as was highlighted a moment ago by Erik Mather; and concerns about the behaviours of companies such as One.Tel, BHP, AWB and James Hardie, which are well known and documented. Also, there are concerns about the impact of large shopping malls on small businesses and communities.

Research such as that by KPMG which highlighted that Australian companies do not adequately account for environmental change, and the reports by Erik Mather's group that he referred to before, indicate that there is a failure to adequately account for long-term factors that will impact on investment. From our own recent experience there is widespread concern about the failure of business to play an active and committed role in addressing Australia's chronic skill shortages.

It is also worth reflecting on the future. There are a number of very major issues that are inevitably going to affect Australia, and they will impact on the way in which Australia expects business to behave. One is around the demographic changes which will reduce the taxation base in a society with a high level of social service needs, such as health and aged care. There is the cost of maintaining and upgrading basic infrastructure in such a large continent. As governments

outsource services, there are issues raised about accountability, the quality of services and the strategic purpose. There are the short-term investment issues that you were exploring with Erik Mather immediately before our appearance. There are the implications of the concept of mutual obligation for companies. For example, are corporate behaviours resulting in greater costs for society? Finally, there is the obligation—whether or not articulated—that companies in Australia ensure that we do not become a dysfunctional society in a beautiful economy. Australia can only benefit from an acknowledgment of such matters and a concerted effort to address them.

I would like to now quickly turn to what we suggest can be done about this. We do not pretend to have the definitive answers but we seek to present to you a number of issues, and we suggest that the basic elements in our approach are these. Firstly, there is a need to establish clarity regarding the place of corporations and our expectations of them. Secondly, we need to initiate measures to lead the desired changes in corporate behaviour. Thirdly, we need to identify appropriate roles for key bodies to achieve such far-reaching change. Finally, we need agreement on the processes to monitor and evaluate the change. On clarity of intent: we detailed in our submission a proposal that there would be a corporate charter—that is, that the Corporations Act would be amended to include that the parliament adopt a corporate charter clarifying the definition of the nature of the corporation—and that further such a charter would be required to be included in the constitution or replaceable rules of each company upon acceptance of limited liability. We believe that that is achievable through an amendment to the Corporations Act.

Secondly, we would suggest that there need to be measures around leadership to achieve the desired changes. We propose measures which include leadership by the government and the parliaments, and the work of this committee is a very important step in that direction. We also suggest that the government be much more proactive in its own activities through utilising its purchasing power to influence corporate behaviour and that the government facilitate and resource the engagement of key stakeholders to work together to shape future directions.

We also suggest that there be relevant research and projects undertaken and initiated to address issues of agreed priority in collaboration with non-government parties and that there be an environment established in which these issues are governed by long-term interests in the nation, rather than the short-term ones that were also alluded to by the previous presenter.

Thirdly, we would suggest that benchmarks and preferred reporting requirements should be established for certain categories of companies. We say ‘preferred’ rather than ‘required’ reporting. In particular, we would suggest that this apply to the extraction industries and those companies which have a broad impact on the wellbeing of society, such as: the producers and retailers of food; companies which invest with a view to securing long-term returns, such as superannuation funds; those which have an impact on financial markets, such as the ASX; companies whose behaviour is likely to impact on the stock exchange; companies which have a large presence in and undertake activities which have a major impact on the community in which they operate, such as mining in remote locations and companies which build large shopping malls in urban areas; companies which have a role which impacts on broader corporate behaviour, such as banking through its own investment and borrowing; and, finally, companies which provide services which had previously been provided or managed by governments, such as telecommunications, transport, energy and prisons.

The fourth area of action we suggest is that there is a need to identify appropriate roles for key bodies to achieve change. These include the roles for federal and state governments, business and industry bodies, employer and employer representative bodies, and bodies such as the ASX, the ACCC and APRA. Whether or not the roles of such players are described as leadership, there would be benefit in examining and recommending appropriate roles for such agencies in relation to the promotion of monitoring of corporate social responsibility. Finally, there is a need to agree on processes to monitor and evaluate the change. We thank you for the opportunity to speak to you.

CHAIRMAN—I will open the questioning by quoting from page 2 of your submission, where you say:

Corporations only exist by virtue of statute.

That is fair enough. Then you say:

They are granted particular privileges to achieve social goals.

They are certainly granted the privilege of limited liability. I am not aware of any particular privileges that corporations are granted beyond that that are not granted to businesses generally. Then you say:

As creatures of our laws corporations may be moulded to any shape or for any purpose our society may deem most conducive for the common good.

One issue that has been explored quite extensively in these hearings and one of the underlying rationales that is provided for why corporations should be giving more attention to corporate responsibility is the need to manage long-term risk. I suspect that, if we take an attitude that corporations may be moulded to any shape or for any purpose our society may deem most conducive by deem of the law, most investors would regard that as a very high-risk option and corporations would find it very difficult to find investors. What is your response to that?

Mr van Beek—We explored the origins of the corporate entity in England and Europe, as well as the earlier provisions in the US for the establishment of corporate entities. It was granted by their societies for a very particular purpose and, in some cases, for a very limited period of time. It reflects that it is a very great privilege to have corporate status and that it is granted because the society believes it is in its own interest to have such entities in existence. So the social good is the underpinning of granting such status. Our concern is that there is no clarity around why corporate status exists in the current Australian Corporations Act or other pieces of Australian legislation. It is open to very many interpretations of why there is a Corporations Act and what the purpose of corporate status is.

Mr Sidoti—We clearly appreciate where you are coming from with the question, but there is a sense in which the type of certainty that enables corporations and investors to be confident in what they are doing requires clarity at all levels. It seems to us that part of the dilemma is in fact the absence of clarity, which creates the sort of investment environment in which the risks are exacerbated. Erik Mather, for example, classified at least three forms of risk in his submission, one of them being litigation. If we look at what has happened over the last few years, litigation is

mounting. It is our suspicion that it is likely to expand considerably over time as various sectors in society, including shareholders, resort increasingly to the courts to resolve issues that may be in dispute. So, we are suggesting looking at a way in which the clarity that governs the expectations of our society—and clearly establishes the expectations for corporations themselves—is codified appropriately by the legislature.

CHAIRMAN—Equally, Mr Mather was not advocating further legislative intervention.

Mr Sidoti—No. I have not read all the submissions to this inquiry, although I have read a number, but generally speaking there consistently seems to be a message about no further intervention and a reliance on voluntary behaviour by corporations or an emphasis on the reporting mechanisms which govern accountability. We are suggesting something which goes somewhat beyond that and we are doing that because the incremental nature of the growth in corporate responsibility and the issues that grow around it are such that, unless the legislative architecture can take us into the future, we are likely to see increasing complexity in individual arrangements and amendments to the tax act, Corporations Act and other legislative arrangements as well as a plethora of individual corporate reporting arrangements which do not allow for the sort of comparability and ease to enable investors and others to make decisions. So, in some senses, we agree with the risk components of what Erik Mather's organisation is talking about but we think those risks need to be contextualised within the architecture, and that really goes to the heart of the Corporations Law.

CHAIRMAN—Most who have come before this committee—perhaps with the exception of those who raised the argument put by the James Hardie directors, which seems to be the exception rather than the general view—have argued that the current Corporations Law with regard to directors' duties is sufficiently permissive for directors to have regard for interests other than shareholders. Isn't it then the role of shareholders in particular, or those who want to guard against the risk profile—which, in the end, as we heard from our previous witness, would ideally be the longer term shareholders—to demand of their directors that they provide an appropriate reporting mechanism that suits their needs rather than having this imposed by legislative fiat?

Mr Sidoti—The sorts of impositions we are talking about relate to the expectations, not the detail of operation, which I think is an important distinction. The second reflection we would make here is that there are limitations to an exclusive reliance on shareholders themselves to determine corporate behaviour, and quite clearly there are other factors at play. The interests of shareholders and whether they take a short-term or long-term perspective is going to affect what they regard is acceptable in terms of their investments.

Part of the recommendation, as we alluded to in our opening statement, is that we see that there is an importance to—and I think others have stressed the need for it—education of corporate parties but there is also a question of a mature nurturing of shareholder expectation as well. Part of that is informed by the information they receive but it is also informed by having some sort of clear articulation of, or debate about, what our expectations are.

CHAIRMAN—I seek your response to a view put to us yesterday by Dr Gary Johns, which perhaps characterises coming from the other end of the spectrum from your point of view. In the letter that accompanied his submission Dr Johns said:

It is my sincere belief that Corporate Social Responsibility is a discourse promoted by non-owner political interests wishing to use corporate wealth for their own ends. Some wealthy corporations promote CSR as a means of forestalling such political action, but also to enhance their appeal to employees and customers.

In the first instance, the Committee should give no comfort to non-owner interests by changing the responsibilities of directors, nor should it lend legislative weight to any scheme that measures CSR, because this serves to undermine directors' duties. As for corporations that use CSR as competitive tool, there is no reason to intervene.

I invite your response to that statement.

Mr Sidoti—Dr Johns's view, I have to say, strikes me as being somewhat ossified in the sense of the definition of ownership. Part of what underlies our approach is that we are talking about corporations operating in a democratic national environment and, therefore, ownership relates to the people. Ownership of corporations is taking a limited view of the role that corporations play in our society. In his writings Dr Johns tends, across the board, to take a very narrow and limited view of the role that civil society plays in our national inheritance and in the democratic nature of the country. I think it is not appropriate to constrain this debate by limiting it to a very narrow view of what ownership means and implies.

CHAIRMAN—How do you define 'civil society'?

Mr Sidoti—Broadly, we would suggest that there are a number of players interacting in the formation of our political and social environment. That would include organised civil society in terms of non-government organisations and community organisations—it could be anything from a sporting organisation through to the other ways that people come together to relate at a community level. That group or organisation feeds into the mood as well as into the politics of the nation in a whole range of ways.

I think we see it playing out constantly and I would imagine that you as politicians would have experienced it yourselves. The community tends to organise and informally respond to a range of issues before it, as it quite appropriately should do. The degree of organisation in civil society and the support that it receives are affected to a greater or lesser extent by the legislative and other environments at play. We can relate it back to what is happening in many of the areas that you are dealing with—for example, public liability. It is fairly critical that the insurance environment is such that it enables small community organisations to exist with the security that they can do so without volunteers and community people being exposed to exorbitant risk.

When you look at corporate social responsibility in that context—for an insurance company to consider its role—part of our argument is that it is critical for corporations, insurance companies or others to consider the impact of their direct activities on the community. In the case of insurance that means making public liability viable, rather than just concentrating social responsibility activity on what it may do through a corporate foundation or through donations or contributions to community activity. So our part in the debate is to suggest that this is not a fringe issue. This is about embedding behaviour into the mainstream, core business activities of corporations in this country.

Mr van Beek—I might also say that part of our submission goes to the heart of statements by the Prime Minister and the Treasurer in the last few days in response to yesterday's

announcement by Qantas. When Qantas said that they were going to sack people, the Treasurer said yesterday afternoon that you would think that an Australian company could find it in itself to employ Australians. Whether or not that is a legitimate expectation, it is very hard to find the basis for that statement. Most of us feel that it is probably a pretty reasonable thing. When you go to the Corporations Act or anything that defines what we think about acting as a corporate entity in Australia, there is no basis for the Treasurer's statement. As an Australian and a person who would like to see Australians employed, I feel it is a very valid statement.

We are in a way saying that, if we only have the debate about whether there should be more reporting and whether directors have limitations, we are actually not having the real discussion we should be having. As key players in our social fabric, what is the legitimate set of expectations that we have in granting corporate status? If that is not clear then we should have a statement that makes it pretty clear. That is not the same as limiting the behaviour of companies. We grant this status because we want them to have that status, but, in granting that, whilst we do not say that you must employ people, there are a number of expectations that are pretty widely shared. If they are not clear at the moment then we should have a public discourse around that to clarify it. That is our submission.

It is not so much about whether there should be more reporting or more legislative change. This is a very fundamental debate about the future of our society. In a number of societies we have seen, behaviour towards corporations has been quite negative and damaging. We are saying that this is a very important opportunity to have a proactive and positive approach to defining that for our future.

CHAIRMAN—Let us take the example you have just given—the announcement by Qantas and the response from the Prime Minister and Treasurer. Surely you would not suggest that we go as far as writing into the Corporations Law or any law that an Australian company may only employ Australians in Australia? You might have the expectation that they would try to employ Australians where they could. Isn't this a matter of where it is appropriate to draw the line and what the appropriate degree of regulation is?

Mr Sidoti—You are right—we would not expect that it would be written into a charter or into the Corporations Law that there is a requirement to employ Australians. But, in establishing expectations, the sort of issue that we believe would be in such a charter would be a recognition of the fact that the corporations do exist at the discretion of the society, mandated by the parliament and under legislation. Therefore, because of that discretion that is accorded to them by the Australian society, they are answerable in some senses to the Australian community. Whether that is through the courts or the legislature, it is still to the Australian community.

I think we keep coming back to this notion of what part the corporation plays in the democratic society. Also, in doing so, there are expectations about the impact that a corporation which has been granted that discretion to operate in Australia will have. It has an effect not just on the economy but also on the environment and Australian society. To that extent, they become the parameters within which those sorts of decisions and arguments take place. I can give you a different example—

Senator MURRAY—Before you go on, can I clarify something just so that I understand. You are putting up the proposition of a charter. Commonly in law and across many laws we have

objects which try to fulfil the same kind of intention. It is not an extraordinary proposition that you put forward. It is an interesting proposition. But objects, in my experience—and I do not know if either of you are aware otherwise—never have penalties attached to them. They merely provide, as you put it, the architecture or the infrastructure or the housing into which the statute goes. You are not intending, are you, that the charter be justiciable or have penalties attached to it?

Mr Sidoti—No.

Mr van Beek—I will use this morning as an example. I am still involved with school industry initiatives, and I spent much of the morning with a business that sort of is committed to providing training opportunities. Australia faces a major skill shortage. Thirty years ago it was expected—although nowhere was it stated—that all major businesses, government departments and local governments would provide entry-level training. We had such a fundamental shift that we now have very great difficulty getting businesses to play an active role in providing entry-level training. Somehow the school system or somebody else is meant to provide that.

The relationship between the different components of society at the moment would suggest that we need to have a debate about how we can encourage different corporate behaviours—and we are not talking about going back 30 years. Our submission is really not about how to have penalties. But if we seriously want some changes, such as in that area of training and entry-level training opportunities, then what are the mechanisms that might be available for us and on what basis would you make those changes? The starting point is some sort of articulation of what Australia's expectations are in the form of objects or a charter. So it is not about penalties; it is about what tools might we usefully use to drive some change.

Senator MURRAY—This is quite an interesting proposition you are putting to us, because nearly all the submissions have said: change the law—which, of course, attaches penalties and the potential for it to be adjudicated at law—or do not change it. However, far less contentious, in my view, would be to set an expectation in law through objects and charters. It is quite an interesting halfway house between those two.

Mr Sidoti—Part of that is not that it should be empty rhetoric. As we know, to establish such principles and objectives in legislation actually has an impact—not only in terms of guiding behaviour but also in terms of informing judicial decision making.

Senator WONG—It can substantially alter how a provision is interpreted. It potentially does have significant legal ramifications.

Mr van Beek—Our concern would be that if you only had legislative change or reporting requirements, you drive two sorts of behaviour. Legislative change results in minimalist, compliant behaviour. Reporting often translates into glossy spin-doctoring. If we are seriously trying to drive some corporate behaviour change we need a mix of things, and penalties will not of themselves do that.

Senator MURRAY—Staying with that issue, my ears really did prick up this morning when one of the witnesses, Eva Cox, gave such a pithy encapsulation of CSR. Essentially she says that CSR means that the core business of a business is conducted in a socially responsible way. An

encapsulation of that in objects, even on its own, would alter the perspective of Corporations Law interpretation—in the broad principled sense, not in the narrow duty sense.

Mr Sidoti—That is right. I think it is fair to say, Senator, that you are on our wavelength. It is not coming from a position of saying that corporations are inherently evil, by any stretch of the imagination. Our work has actually been largely with corporations that are anything but evil. They are positive contributors to our society. For those corporations there is surely no danger in recognising that in legislation, in terms of principle. The only ones who need to have anything to fear from such a position are surely those who feel that they are somehow acting outside of a responsible manner.

Senator MURRAY—The other thing you raised which is of interest is the preferred reporting idea. One of the problems we are faced with whenever people suggest to us that we change the law is that we are conscious that it is going to apply to people it need not apply to—with compliance costs and all the irritation attached to it—or that, in being designed, it is so generalised as to not have an effect on the worse offenders—the people you are trying to impact.

It seems to me a preferred reporting regime could be spelled out in legislation, with the responsibility for deciding that that is brought into play, either permanently or for a period, laid upon somebody like ASIC or the ASX. The worst example, in my view, of negative corporate behaviour is with tobacco. The preferred reporting regime might be imposed by ASX on tobacco companies to ensure that people who invested were fully acquainted with every sort of risk and how things were to be managed. Is that how you meant the preferred reporting regime should operate—at a discretionary level by a regulator such as ASX or ASIC? Or did you mean that that regime should be established by government and be spelled out in either regulation or legislation?

Mr van Beek—Again, we are looking at one component of a range of activities to try to encourage changes to corporate behaviour. If you look at the Global Reporting Initiative—I think you have had a presentation to you—my sense of their contribution is that they have become in a way the clearing house for the range of expectations, some of which are reasonable, some of which are not. New issues emerge, inevitably. Environmental issues were not big on our radar screen 30 years ago, with a requirement or an expectation that no-one would damage our environment. There are other smaller issues which may have more volume than warrant serious attention. So there is a need to have some vehicle for saying, ‘These are legitimate issues against which, ideally, corporations would report, because they have these sorts of ramifications for our society, environment or economy.’ The intention was to say, ‘If we establish some expectations in the charter or the objects, then we should also be looking at some guidance to companies—whether or not it is legislatively required—that these are the kind of things that our society expects them to report against in the following sorts of ways.’ It is about standards setting rather than necessarily imposing.

Senator MURRAY—Let me be a little clearer in what I am asking you. In my head is this concept: CSR is under way, it is in its developmental phase and there are people trying to set standards. That is being done both internationally and nationally. The reporting and measurement mechanisms are all under way. The proposition put to us is probably too early to formalise and to require it mandated in any way. But perhaps it might be necessary to mandate it on the discretionary basis—which sounds like an extraordinary concept—for the worst

offenders. I took an industry which is easy to badmouth, because 19,000 people are killed every year with their products—the tobacco industry. But you do not say in legislation, ‘We are going to pick on the tobacco industry.’ You say, ‘This is the preferred reporting required, and ASIC and ASX can trigger it at their discretion.’ That was my reaction to what you were saying.

Mr van Beek—Can I just talk about one of the challenges for us. I was at a conference once where somebody was saying that British American Tobacco has a very good corporate social responsibility report. It does not deal with whether or not it is a product that a society should accept. So they fit with everything but—

Senator MURRAY—They probably do not need to, because we know it.

Mr van Beek—But there is a definitional problem, in a way, in saying they might employ people appropriately and all sorts of things, but the fundamental that you are concerned about does not necessarily get covered by that.

Senator MURRAY—Yes, the risks—and I am focused on risk. For me, when you get into mandating anything in corporate law you must attend to risk. It must be the must-do stuff, not the nice-to-do stuff.

Mr Sidoti—To answer your question about what drove us, I sense there is sufficient experience to know that good public policy depends on its workability. The workability of reporting, which others have alluded to, depends upon being able to take the plethora of reporting arrangements that are in place at the moment and to recognise that in fact some well-meaning corporations are not fully equipped, either through their own level of awareness or their infrastructure, to respond appropriately to a mandated reporting requirement as of point zero. As with a whole range of other major public policy initiatives, you have to put in place transitional arrangements. You have to build towards the applicability. That may be, in some instances, the stepped arrangement that Erik Mather spoke about. What we are suggesting is that if you start to establish preferred directions you are not simply allowing it to be voluntary, you are pushing it along, you are providing incentive and you are actually moving progressively towards a point where the level of reporting is of a sufficient standard to allow the accountability we need.

Senator WONG—You have canvassed with Senator Murray most of the stuff I was going to ask about. Essentially, I think you are right in that the discussion we have been having through this inquiry has probably been a proxy discussion about what the role of the corporation is and therefore what its obligations should be and how you effect that. Coming back to the charter, are you proposing that it be legislative? If so, how—adopt it into the Corporations Law?

Mr van Beek—We are not—

Senator WONG—You do not have that level of detail?

Mr van Beek—We do not have that level of expertise, but it was our understanding that it could be through an amendment to the Corporations Act and that there could also be a requirement in that legislation that companies that accept limited liability incorporate that charter or object in their own constitutions.

Mr Sidoti—But it does have to be legislative in the sense that, as we were discussing previously, if you are going to establish the expectations of principles and objectives, it has to be embodied in the legislation to give it the sort of effect that we are talking about. The form of words we have not proposed. The broad outline of what that expectation would be we have suggested in the submission.

Senator WONG—Mr van Beek, can I go back to your example about training. I suppose the doubters might say that a decision as a sector or as a class of employers progressively over a period of 30 years to reduce as a sector—not necessarily individual companies—their contribution to the public good of training is not related to how they construe the role of a company in society. Some might say it is a practical decision about efficiency, cost and investment.

Mr van Beek—I am sure they do, but it has had national ramifications.

Senator WONG—Absolutely. I think where I am trying to go is to the question of why having any discussion about the role of the corporation in society will impact upon that kind of decision.

Mr van Beek—I think because the charter is not only about defining corporate behaviour but about the way we in public policy see an appropriate role for businesses. That, in the longer term, will translate into other public policy responses. As we put in the submission, there are things on the immediate horizon such as what this will mean for corporate taxation when we have infrastructure costs and the burgeoning costs of health care et cetera—those sorts of things. That is not to say this is a secret agenda, but at the moment it is not clear how we see the company. It means that we do not necessarily build it into public policy appropriately. Our contention would be that it not only impacts on companies but on public policy as well.

Senator WONG—Arguably, your charter itself is a proxy discussion—

Mr van Beek—It is, yes.

Senator WONG—about what the proper role of the state is, what the proper role of civil society is, what the role of the corporate sector and business is and what the proper role of the individual is. You could probably segment it differently.

Mr van Beek—Definitely; and we are saying that that is a debate that necessarily will be had and we might as well engage in that proactively, knowing that it is emerging in a whole range of ways.

Senator WONG—You could argue that it is a debate that is already being had but it is not being had—if you know what I mean. Decisions are being made all the time in a whole range of policy areas which alter the relative position of responsibility, including funding, of a whole range of activities—training, health services, defence, detention. There are a whole range of decisions being made but they are being made without that discussion necessarily, as a priori decisions.

Mr Sidoti—That is exactly right. Essentially we are arguing that it is going to happen by default, in an unconscious way, leading to all sorts of unclear and therefore inefficient consequences and, possibly, poor social consequences. Or we can bite the bullet and consciously engender the debate in a way which leads to a quite appropriate legislative response.

Senator WONG—Thank you.

CHAIRMAN—There being no further questions, thank you, Mr Sidoti and Mr van Beek, for appearing before the committee and for your assistance with our inquiries.

[3.56 pm]

DEEGAN, Professor Craig, Judge, ACCA Sustainability Reporting Awards, Association of Chartered Certified Accountants

FRANCIS, Mr Richard Daniel, Head, Australia and New Zealand, Association of Chartered Certified Accountants

CHAIRMAN—Welcome. Do you have any comment about the capacity in which you appear?

Prof. Deegan—I am the professor of accounting at RMIT.

CHAIRMAN—We have before us your submission, which we have numbered 32. Professor Deegan has a separate submission, which is numbered 96. Are there any alterations or additions you wish to make to the written submission?

Mr Francis—Yes, I would just like to mention an update to our reference to corporate law reform in the UK, where the submission mentions that the introduction of the Operating and Financial Review is under way. That has been withdrawn recently and unexpectedly.

CHAIRMAN—That is noted. I invite you to make opening statements, at the conclusion of which I am sure will have some questions.

Mr Francis—I would like to make a statement on that particular point, to provide some background. While ACCA has been active in promoting corporate social responsibility and we have had our awards for environmental and sustainability reporting since 1991, we also felt that in practical terms the proposals of the Operating and Financial Review were a good way to encourage a greater level of reporting. While it would not be at the same level as triple bottom line reporting, we put in quite a lot of effort in support of the introduction of that review and generally were supportive of narrative reporting as an encouragement to supplement historical financial reporting, and to encourage listed companies to report on future impacts which took into account social and environmental issues.

We were therefore disappointed that the proposal in the UK for the OFR was withdrawn and replaced by an EU mandate for a less rigorous business review statement. ACCA have submitted a paper to the government in the UK, basically describing what we feel are the differences between the business review and the operating and financial statement. Another point we made was that the Operating and Financial Review would have offered a contribution to the development of an international accounting standard, which is being proposed by IASB over the coming years. So, as an opening statement, I would just like to mention our involvement in that particular area, as well as in our sustainability reporting awards.

Prof. Deegan—The main thing I have looked at in my submission is more the reporting side. Since all the submissions have been in what has become apparent—I know you would be fully aware of this—is the dichotomy of views that are out there. It is obviously up to the committee

to work out who is right and who is wrong, but you have the corporates, industry bodies and accounting bodies and then you have the social and environmental employee groups at totally different ends of the spectrum on a variety of things. Clearly what has come out is a preregulation/antiregulation stance, which you would all be aware of. So the sort of thing I would like to get emphasised is that there is very much the view that what is in the Corporations Law at the moment from the industry side is sufficient and therefore, through enlightened self-interest, everything will just turn out okay.

I would like to emphasise that there is not a lot of evidence to actually support that. There is this notion that there is going to be a trickle-down effect and—left to the markets, left to an unregulated environment—everyone will be better off in the long run. I thought it was quite interesting that a number of the submissions actually refer to the works of Milton Friedman, which I found a little bit scary, and again this idea that things will trickle down nicely and everyone will benefit. I have gone through this in the last couple of weeks, trying to find some evidence to suggest this trickle-down effect actually works, and there is nothing to really support it. Again, there is not a lot of support for the idea that, through a lack of regulation in the area, everything will go to the most efficient uses and the whole of society will benefit, but that is clearly the position being adopted by industry.

What does concern me a bit at the moment, from looking at the submissions—I have actually written a paper on all the submissions already—is just this derived effect. If you go through the consideration of stakeholders other than shareholders it is all just a derived effect, so it is a derivative effect. If we do attend to the interests of stakeholders—and this is the corporate perspective at the moment—it is really only to the extent that it is in the interests of the company. And, given the way the whole debate is going with sustainability, I am not convinced we can still live with that sort of situation. There are a lot of key issues. I am not convinced we can maintain a situation where we can rely on this litmus test that the Business Council of Australia puts forward:

The litmus test for any activity or responsibility is whether the performance of that activity or responsibility can reasonably be seen to be contributing to the growth of shareholder value.

I am just not convinced that has worked in the past and perhaps we do need to bring something forward.

The other point I would like to make is that I saw a lot of the comments that are coming out about reporting—it is going to hinder innovation, it is going to stifle activity if we put in place this sort of reporting—in 1998-99 in the inquiry on section 299(1)(f). Exactly the same comments are coming out: that if we left section 299(1)(f) in the Corporations Law somehow that will stifle future reporting and it is best left to industry to work out innovative ways. The fact is that after that inquiry, even though we were told things were going to be stifled, reporting has got a lot better. The introduction of that law did not bring back the quality of reporting and I really see no reason why some form of introduction of laws on the reporting side might not improve things.

Why not leave it the way it is, voluntarily? I do a lot of research in this area. The point is that at the moment you have things like the global reporting initiative and companies are just cherry picking, yet they are coming out and saying, 'We're in compliance with the global reporting

initiative and isn't it great that we have adopted this voluntary code.' But the fact is there is a lot of cherry picking. Some companies still will not report; it is crisis driven. At the beginning of my submission there is so much evidence that reporting on the social and environmental side is really about responding to either key and powerful stakeholder concerns or to media attention and so forth. A lot of the reporting to date has been about corporate survival and really not about accountability and, again, I just wonder whether the accountability side should go.

In terms of the submission I made I think there is a lot more requirement for disclosure about governance structures. There have been calls for disclosure about how issues of climate change are impacting companies—there is still not a lot of that. We have done our judging today on our ACCA Sustainability Reporting Awards and a lot of this governance stuff is still not there. We have been waiting to see if, voluntarily, a lot of what we thought were important things would creep into the reports—they are just not coming in. That is the opening statement I would like to make. Again, in the report I have made a number of suggestions of the types of disclosures which I think might be appropriate.

CHAIRMAN—Thank you, Professor Deegan and Mr Francis. You mentioned—to paraphrase what you said—'the trickle-down effect'. We have heard a lot of evidence as to the extent to which companies are now giving attention to triple bottom line reporting and sustainability reporting and the like. Wouldn't you acknowledge that the level of reporting is much more substantial now than it was a decade ago?

Prof. Deegan—Sure, though I would probably argue that a lot of it is due to community demands for it. But, if you leave it to the community to tell us what should be disclosed or to put the pressure on companies, it is still not about accountability. If people do not know that there is a problem, they do not demand that the company tells us about it. Certainly the disclosure has increased. I have done heaps of research on this. If you go back to the early 1990s, you see that there was nothing. It has certainly increased but there has been a lot of pressure put on companies to do it. I would still argue that it is a reactive rather than a proactive or an accountability approach.

CHAIRMAN—Are you arguing that the directors should be more accountable to the broader community than to their own shareholders?

Prof. Deegan—Yes.

CHAIRMAN—Why?

Prof. Deegan—I guess it goes back to the notion of the requirements for change. You would have had all of this stuff thrown at you, but companies are the ones who have the resources to create change and you still have one dominant stakeholder group, shareholders—

CHAIRMAN—They are the ones who are most at risk.

Prof. Deegan—Financially? Yes, but there are a lot of impacts that companies are creating other than just the financial impacts. I do understand that that ultimately flows through to shareholder value, but it goes to whether the key quest of companies is put as being to increase shareholder value. If we accept that companies are coming out and saying, 'We are truly

embracing sustainability and responsibilities to a broader group of stakeholders,' but then in the next sentence they are telling us that their litmus test for any activity is whether it increases shareholder value, that is inconsistent.

CHAIRMAN—Would you accept that a corporation needs to attract capital to exist and to operate—

Prof. Deegan—Yes.

CHAIRMAN—Unless it does increase shareholder value it is not going to get that capital or the cost of capital is going to increase.

Prof. Deegan—People are still going to invest their money. If there were some form of common requirement regarding accountability and so forth across the board—

CHAIRMAN—They might choose to invest in real estate or in private businesses rather than corporations, if you put particular duties on corporations that do not apply to other investments.

Prof. Deegan—They might. As you would be aware—this is stuff that has probably been thrown at you—there are three common limbs of sustainability: economic, environmental and social. In this day and age, it is incredible that we have such a high focus and extensive regulation on one component of that, economic, and not on the social and the environmental. I think companies are accountable for what they are doing to the environment and what they are doing for society, but they are not being made to be accountable.

I notice that a number of the arguments in the submissions have said, 'That's fine, but the annual report isn't the place to put this sort of disclosure on the environment, society and stuff.' The annual report is the place because that is the document that gets the most readership and is the document that is regulated at the national level.

CHAIRMAN—But if you are talking about accountability and we take the environment for example, aren't they accountable in the sense that they are required to comply with environment laws? If you are looking at employees, you see that they are required to comply with labour laws. It is not as if there is no accountability with regard to those issues.

Prof. Deegan—No, but a lot of the reporting is at a state based level. I have tried to get a lot of this stuff, and I know that it is very difficult. You certainly do have things like the National Pollutant Inventory, which relates to a limited number of companies. Again, as you would know, environment disclosures are state based, and it is very difficult to get hold of that stuff.

Senator WONG—There are a few issues that I want to raise with you. The first is where we sit internationally on this. Erik Mather appeared earlier today and he talked about how Australia is lagging—I think he used that word, but I am paraphrasing—behind the rest of the world. I was looking at your submission, Mr Francis, which at least does the table of sustainability reports. One could argue about to what extent that actually indicates that we are doing something, but Australia is quite substantially behind at least Japan, the UK, the USA and Canada. Would you comment on where Australia is in relation to sustainability and corporate responsibility issues as compared to the rest of the world, given the experience of your international organisation?

Mr Francis—Our table shows Japan as having the highest percentage and the UK the second highest. It is interesting that the drivers of that are rather different. Concentrating, say, on the UK and Europe, we feel that the higher level of reporting is really due to a high level of stakeholder activism.

Senator WONG—In the UK?

Mr Francis—In the UK and Europe. There is more happening through stakeholder activity, pressure and expectation. I think that, if there is a stronger expectation in a particular region, then you will get more reporting coming out. Japan is a slightly different situation—it is perhaps more conformist and if one does it then everyone follows suit, so there are different drivers there. I do not know that much about the reasons in Japan, but it is interesting that the UK does have a higher level of awareness and higher standards of reporting.

Senator WONG—There is a figure here in brackets of 49 per cent. Is that for the previous year?

Mr Francis—Yes.

Senator WONG—Would you put down the very substantial jump in the UK on sustainability reporting to the activities that the government has undertaken to try and encourage a greater focus on these issues?

Mr Francis—I think the corporate law changes are really trying to produce an element of triple bottom line, but they are encouraging the rate of this form of reporting. There is some government encouragement. I think the government does get more involved in encouraging special interest groups to contribute, so it is partly a government driven area. I believe it has a lot to do with the culture and the benchmarking. In Australia and New Zealand, although we find the standard and level of reporting is still not very high, the water industry, for example, is getting to a stage where not only are there several good reporters but they could even start benchmarking against each other. We have seen that with the banking industry, where more banks are starting to produce reports now.

Senator WONG—I suppose what I was asking is whether the 21 per cent increase in the UK in the last year as opposed to a seven per cent increase in Australia might be due in part to the fact that there has been a fair bit of government activity in this space, both legislatively and also just in the articulation of views in the UK.

Mr Francis—Yes, I think it is related to government activity on articulation.

Senator WONG—We know that our reporting levels are lower. Do you think that Australian companies are perhaps behind a number of our competitor markets in considering sustainability issues?

Mr Francis—Yes. There is a lot of activity in Australia around the discussion of it, but since we introduced the awards here we have found that the actual number entering has not changed a great deal, even though the awards received quite a lot of publicity and have a good reputation. We got about 36 entries this year, about 33 last year and 27 when we started, so there is an

increase. We are seeing more diversity, and organisations that would find it quite difficult to report, such as retail organisations, are starting to do so. I think we are seeing more new reporters coming in but not necessarily a rapid growth.

Senator WONG—Can you remind me of the awards?

Mr Francis—The awards are for the best sustainability reporting and include categories for social and environmental reporting, but almost all the entries nowadays are sustainability reports and not specialist reports. The judging panel look at things like credibility and completeness and a number of different factors to be convinced of the quality of the reports.

Senator WONG—If we proceed from the position that we are behind a number of our competitor markets internationally in this and the take-up rate is perhaps not as quick as we would like, what are your views about what can be done? I will throw the question open to both of you. Bear in mind, and I think this was raised earlier, the view that is being put by some, who would probably be seen to be on the side of trying to push this along, that, if you mandate reporting at this point in the trajectory, you may stultify innovative responses and the cultural change which underpins reporting. Reporting is an end in itself, but one of its major benefits, one would hope, is to facilitate a cultural shift in the businesses.

Prof. Deegan—I am still not convinced on the argument that you will—again, this is something that has come up quite a bit—bring down the level of reporting. Some of the proposed disclosures I would have put in my submission in terms of governance structures and things like that would be base level type disclosures. It is not as if you are throwing a framework on organisations; it is just that a lot of the information, I would think, that could be disclosed would be things like existing governance structures, what you have and whether you use best policy everywhere when you are going offshore in terms of the environment and so on. It would be those sorts of general requirements. It is not as if you are asking people to put a cost on their environmental impacts everywhere. We do not have the technology to do that. It would be quite silly to push that sort of thing.

But when you are asking things about governance structures and so forth, you could ask: how are you attending to the risks associated with climate change; if you are in coal and that market in Japan is going to close down on you, what are you going to do about it; do you see it as a risk; what are you going to move into or how are you going to combat that risk; and so forth.

Senator WONG—Sure. I have a follow-up question. Mr Francis, did you want to respond as well now?

Mr Francis—I am not sure if it is quite the same thing, but the only thing I would like to note on the earlier point I made about the difference between a business review and the operation or financial review is that as a result of all the discussion in the UK a body of knowledge developed which could help companies to report. I think one of the difficulties for companies in starting to do sustainability reporting is that they need guidance on how to go about it. You have to have an environment which is not just statutory. A statutory requirement to report is not necessarily the capability to do so.

Senator WONG—In terms of a stage process, one of the views that has been put to us is that as an interim step we could get some guidance issued on, I think, principle 7 of the ASX guidelines to try and encourage or get companies to report more fully on how they are managing environmental and social risks as opposed to saying, ‘Here’s a framework—report against it.’ What do you think of that?

Prof. Deegan—On the ASX thing, and a lot of my recommendations relate to the Stock Exchange, there was a lot of scope through the corporate governance council to put in place some quite useful disclosures. If you look at how it was developed, you see that principle 10, which regards stakeholders, was a tack on. People who were involved in the development of that will tell you that came towards the end. If you go through the types of disclosures that they are requiring, you see that there really is not a lot there. Yes, you could beef up those disclosure requirements greatly. That is a great vehicle for requiring disclosures. You are hitting the top end of town; you are not hitting the smaller companies. You have differential reporting.

That was an opportunity lost. When that first came out of the guidance document, a lot of us were quite upset to see the lack of consideration given to social environmental issues. If you go out and talk even to shareholders or big institutional investors and so forth, they are now listing amongst some of the key issues they consider—even if they are just fixated on the money returned—social environmental risks, yet the Corporate Governance Council totally missed that in their guidance document. There are a couple of throwaway lines referring to social and environmental issues, but it is not embedded, and that is where they could have had a great impact. If you go and see what has happened in South Africa with the King report, which addresses the same sorts of issues, which, for me, is not a radical thing, you will see that they took into account that this is a big risk area. They actually incorporate some things within the King report, which is the South African equivalent of our Corporate Governance Council.

So it is not a radical thing. If you look at some of the surveys again—and I am sure this has come up in the submissions—that AMP Henderson and others did on climate change, you will see that that is one of the biggest risks facing companies, even for those who are fixated on financial return. There is nothing in the corporate governance document from the ASX on climate change. In this day and age, given what companies are saying and doing and what institutional investors are saying and doing, what is being said overseas in terms of the very big risk to business of climate change, why wasn’t it there?

Senator WONG—I do not want to traverse the past; I am sure that the ASX might have a view. They are obviously looking at the composition of the council you refer to in your submission and the resistance of which you are aware from a significant number of their stakeholders. I guess it is not surprising. Some might say that it is better than nothing that ‘legitimate stakeholders’ was actually put in, because I understand that that is a controversial issue for quite a lot of people. But a number of your suggestions about reporting could be done in the context of the existing guidelines.

Prof. Deegan—Absolutely.

ACTING CHAIR (Senator Wong)—I want to explore the issue referred to in your submission, Mr Francis, about the changes in UK pensions regulations. Senator Murray may want to talk about this too. One of the things we have been looking at is: how do we get the

investment sector to contribute towards a more long-term perspective? Can you tell us how successful this was, or are you not able to give that evidence?

Mr Francis—I can, but not in too much detail. I was talking to our technical director in London the other day and he specifically mentioned the pension sector as being something they had been very pleased with—that it had been taken up much better than expected. In particular, because of the long-term nature of pension funds, one of the difficulties in current reporting is short-term emphasis. The pension area has been an area that seems quite promising in development.

Senator MURRAY—I am sure the ASX have the figures, but they are not here to ask; perhaps you know. I am sure it is bigger by market cap rather than by numbers. Do you have any idea of how many of our listed corporations are also operating overseas and therefore would probably have to report in terms of overseas requirements?

Prof. Deegan—Obviously at the top end there would be a high proportion, but, no, I do not.

Senator MURRAY—One way in which you can approach this issue is by taking the view that, because of globalisation, because of our internationalisation of our own companies, all this is going to happen to us anyway, so we might as well take the best of what is being done overseas and apply it in our own law and not agonise over the basics, because otherwise it will end up being imposed.

Prof. Deegan—One of the big bodies that has an impact on annual reports and so forth is the International Accounting Standards Board, and they really do not have it on the agenda. A couple of things have come out. Even a year ago there was nothing, but about eight months ago something came out saying that the Australian Accounting Standards Board had it on the agenda. So I emailed the chair of the AASB, but he said: ‘No. That has been wrongly reported. We have not got it on the agenda whatsoever.’ Again, they are financial reporting standards, so you would probably ask: ‘Why would they be there anyway?’ But they are not on their agenda at all.

ACTING CHAIR—One of the reasons is that you want the membership changed.

Prof. Deegan—Totally. As you said, it is the same as the corporate governance council. There is no outside interest in terms of social, environmental or employee groups at all. It is a captured debate and it is quite frightening.

Mr Francis—We do make the point in our submission that we feel that if there is too much national emphasis it may not adequately take into account the international developments and focus on stakeholders.

Senator MURRAY—Today we had our attention drawn to a report produced by the Centre for Australian Ethical Research. On page 7 of that report they have a figure of the percentage of top companies from Australia, the UK, the US and Europe which prohibit both the giving and receiving of bribes.

Prof. Deegan—Is BHP on that list?

Senator MURRAY—I cannot find the relevant figures instantly but, for the purposes of *Hansard*, I will verbalise it. As you can see, the graph shows that the figure for Australian companies is around 51 per cent, whereas the average of those others would be of the order of 90 per cent. You have outlined in your submissions—as have others, I might say—that Australian business lags behind forward, progressive thinking in the area of reporting accountability, taking a broader view of their responsibility and so on. That report I have just quoted shows that yet again. Do we have a fundamental cultural problem in this country? Are our business milieu, training and the personalities in business so different from the leading companies in the countries that are referred to?

Prof. Deegan—Generally, I would not know, but I know that certainly we lag on the reporting side. It would be hard to accept that, I guess, because—

Senator MURRAY—I find it hard to accept, but I am continually told that—and I accept the evidence—our companies do not do what other leading progressive companies are doing overseas. They do not take the initiative in these areas. That is not universally true—of course it is not—but there is that kind of inference that heel-dragging goes on in our business community.

Prof. Deegan—Certainly on the accountability side. On the accountability side you would have to say yes. We have someone who is on the judging panel of the ACCA awards here but who has come from Europe, where she also judged awards. She says that, compared to what they are doing in Europe, we are so far behind here. People who I work with say the same thing. Up until recently it has basically been a voluntary reporting regime in the UK too, yet they are three to five years ahead of us all the time. Again, I do not know why the difference.

Senator MURRAY—My point is that with this sort of activity you are not trying to get people to do something because they have to but do not believe in it, because then it does not have the proper effects—although it has some effects. What you want to do is to have people committed and have behavioural change. I guess that, if we are to advance this debate, within our own recommendations we need to look at the behavioural change side, the attitudinal side—how you address the heel-dragging that has been going on.

Mr Francis—You could not, for example, say that the reason they are more advanced in Europe is simply that they started earlier. We have found over the last two or three years that the standard of reporting is not shifting very quickly in Australia. We are looking at reports and, every so often, one report will improve in quality but the overall standard is quite slow moving. I think there are not the drivers there. It is still reputation or risk based rather than based on principles of better disclosure, transparency or those sorts of areas.

Prof. Deegan—What I would say is that it does appear on anecdotal evidence that, every time the possibility of regulation arises in Australia, opposition to it does appear to be greater than in most other countries. As I was saying right at the outset, if you have the time to go back and look at the submissions to the 1998-99 inquiry about section 299(1)(f), it is the same stuff that is being wheeled out again. The quality did improve after 299(1)(f). It did not squash everything. So, if we have further disclosure requirements imposed, I cannot see that that is going to squash everything either.

ACTING CHAIR—Professor Deegan, Mr Francis, I think we are going to have to finish up because we are all flying out. Thank you very much for attending to give evidence today; that has been very useful.

Committee adjourned at 4.31 pm