Australian Council of Super Investors Inc.

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Mr Anthony Marinac
Acting Committee Secretary
Parliamentary Joint Committee on Corporations
and Financial Services
Suite SG.64 Parliament House
Canberra ACT 2600

Email: corporations.joint@aph.gov.au

Dear Mr Marinac,

Corporations Amendment Bill (No.2)

The Australian Council of Superannuation Investors ("ACSI") is a not for profit incorporated association formed in April 2001 to provide independent research and education services to superannuation fund trustees, in relation to the corporate governance practices of the listed entities in which they invest.

The superannuation funds that belong to ACSI collectively manage $110 billion in assets for over five and a half million Australian workers and retirees. Just over 46% of the $600 billion of total superannuation fund assets are invested in the Australian equity market. Therefore the performance of Australian companies is a major determinant in the levels of retirement income of millions of Australian workers and retirees.

Superannuation trustees are required to take into account a range of risk considerations in the investment decision-making process and are increasingly concerned with performance of listed corporations and their corporate governance practices.

General observations

ACSI welcomes the opportunity to make a submission to the Parliamentary Joint Committee on Corporations and Financial Services on the Corporations Amendment Bill (No.2) 2005.

ACSI supports the rationale and general direction of the proposals introduced by the Federal Government. We recognise that the proposals seek to introduce mechanisms to improve shareowner participation in companies. We also recognise that these amendments build upon improvements to the corporate governance regime already introduced through a range of CLERP 9 reforms.

We do however have concerns about two specific matters contained in these proposals and will endeavour to briefly focus on these items.

Calling of a general meeting by directors when requested by members-s249 D

ACSI understands the rationale for amending section 249 D of the Corporations Act, that currently allows a small number of shareholders to call a general meeting of a company.

We do not agree that special interest groups should be able to utilise provisions to call general meetings, and effectively exercise a power that is disproportionate to their overall economic interest in a company.

We are aware that convening general meetings results in significant expenses for the companies and ultimately shareholders.

There have been few occasions where these provisions have been utilised by narrowly based sectional interests. These occasions have generally related to a small number of companies, some of which, like the NRMA, are not publicly listed.

We nevertheless agree that the 100 member (shareholder test) provision in s249D could be subject to abuse, and should be modified to overcome the potential for abuse."

We are however concerned that the Federal Government proposal which seeks to remove the 100 member provision and maintains only a single 5% shareholding threshold, does not strike the necessary balance between corporate interests and the interests of shareholders, particularly smaller ones.

Take the example of a major financial services company currently listed as a S&P/ASX 100 company with 1,818,414,833 ordinary shares distributed amongst 252,072 shareholders. As at March 29, 2004 a share in this company was trading at $20.50. To achieve the 5% shareholding threshold test, a resolution to call a general meeting in this company would require the support of shareholders who hold 90,920,000 shares whose total value is just over $1,872,058,000.

52.43% of shareholders in this company currently own less than 1000 shares and represent 3.18% of overall shareholdings in the company, well below the 5% threshold being proposed by the Federal Government.

We are concerned that the 5% shareholding threshold will make it virtually impossible for small shareholders to utilise these mechanisms and would also challenge a number of institutional investors, to meet these requirements.

ACSI Proposal

ACSI calls on the Federal Government to refine the existing 100 member (shareholder test) rule to minimise the potential for abuse. This is preferable to removing a shareholder test threshold and thereby imposing a virtually impossible benchmark for most shareholders.

ACSI accepts the principle of the Companies and Securities Advisory Committee that "the Corporations law should differentiate between the threshold for shareholders to requisition a general meeting and the threshold for shareholders to propose a resolution at the next scheduled general meeting. The threshold should be much higher in the former than in the latter situation, given that the costs and administrative burdens for a company in holding extraordinary general meeting are much higher than those incurred by the company in adding items to the agenda and distributing additional draft resolutions and accompanying statements for meetings that have already been scheduled[1]".

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[1] Companies & Securities Advisory Committee, Shareholder Participation in the Modern Listed Public Company, Final report, June 2000, p.28.

We also support the view that such mechanisms should only be utilised in the most extreme circumstances in between annual general meetings.

ACSI supports a way forward which has been previously considered and takes into account the different sizes for companies.

We propose the introduction of a tougher minimum shareholder test that would result in an increased minimum number of shareholders who may call a meeting, underpinned by a requirement that these shareholders hold a minimum value of shares for a specified period of time.

With respect to the minimum shareholder test, we are aware that both the Federal Government and Opposition had previously considered a "compromise position" that would have resulted in a test based on the numerical square root of the total number of members of a public company.

In the example discussed above, in the financial services company, the shareholder threshold test under the "square root" threshold would be 502 shareholders. This is a reasonable numerical amount.

Each shareholder would need to have a minimum shareholding of say $1000 that must have been held by the shareholder for the preceding twelve months.

We believe that this proposal would address key concerns of the Federal Government as outlined in the Explanatory Memorandum.

The fact that different thresholds exist overseas, does not constitute a sufficient justification for totally overhauling existing Australian Corporations Act provisions on this issue.

If the ACSI proposal were to be accepted this would result in section 249 D providing two options:

- a 5% shareholding threshold test, or
- a shareholder test threshold based on the square root of the total number of shareholders, with each individual shareholder holding at least $1000 worth of shares for at least one year.

We are confident, that this overcomes the potential for abuse by small groups of shareholders and still provides a more reasonable, scaled, yet tougher requirement for shareholders to muster more significant levels of support amongst "bona fide" shareholders, who have genuine concerns in relation to a company and have sought, as a last resort to call a general meeting to address critical matters of concern.

Reduce the threshold allowing member resolutions and statements to be brought to Annual General Meetings already scheduled

ACSI supports the reduction in the threshold for member resolutions and statements being submitted to annual general meetings. The Federal Government has proposed these amendments in light of the proposals relating to s 249 D of the Corporations Act.

We do not believe these amendments overcome our primary concerns with regard to the introduction of significantly more onerous requirements that would apply under the amended s 249 D provisions, that could result in shareholders having to wait up to eleven months to raise a serious matter of concern at an AGM. This might be too late, particularly where a matter may be of a more time sensitive nature.

Electronic circulation of members' resolutions and members statements

ACSI supports these proposals that improve the facilitation of information via electronic means.

Cherry picking proxy votes

ACSI supports Federal Government proposals on this matter.

Disclosure of proxy voting

ACSI supports these proposals that aim to improve transparency with respect to proxy voting.

Disclosure of information filed overseas

Section 323DA of the Corporations Act states:

> (1) A company that discloses information to, or as required by:
>
> (a) the Securities and Exchange Commission of the United States of America; or
> (b) the New York Stock Exchange; or
> (c) a financial market in a foreign country if that financial market is prescribed by regulations made for the purposes of this paragraph;
>
> must disclose that information in English to each relevant market operator, if the company is listed on the next business day after doing so.
>
> (2) [REPEALED]
>
> (3) This section applies despite anything in the company's constitution.

Section 323DA was inserted into the Corporations Act by the Company Law Review Act 1998. It was not part of the original Company Law Review Bill (as drafted by the government). Instead, it was added to the Company Law Review Bill in a package of 'last minute' Senate amendments, as a result of Opposition and minor party proposals.

We refer to paragraph 2.45 of the Explanatory Memorandum to the Corporations Amendment Bill (No. 2) 2005 that gives the government's rationale for wanting to repeal section 323DA:

> 'The PJC recommended that the Corporations Act should not require companies to report such information. Two of the reasons given by the PJC were that the only additional information disclosed under the provision is non-material and that it is preferable for the Australian Stock Exchange (the ASX) and various accountancy bodies to provide for disclosure requirements of listed companies rather than the Corporations Act.'

The reference to PJC is to the report of the Parliamentary Joint Committee on Corporations and Financial Services, *Matters Arising from the Company Law Review Act 1998* (published 21 October 1999).

In that report, the PJC said it had received 31 submissions on whether section 323DA should be retained or repealed. The PJC said 11 submissions were in favour of retaining the provision and 20 argued for its repeal.

The PJC's report concluded that section 323DA should be repealed because it:

> 'was superfluous and included a number of potentially undesirable consequences. The Listing Rules of the ASX already require the disclosure of any information which would have a

material effect on the price or value of company securities. Any additional information disclosed to foreign exchanges would not be price sensitive and would not be material to the Australian market. Therefore there seems little reason for the provision. ... The PJSC does not accept that shareholders will be disadvantaged by removal of the provision, because, as noted above, the only additional information which the provision requires to be disclosed is non-material.'

The reference to the ASX Listing Rules is to the 'continuous disclosure' rule (LR 3.1). As a note to Listing Rule 3.1, the ASX states 'The following would require disclosure [under LR 3.1] if material under this rule: ... a copy of a document containing market sensitive information that the entity lodges with an overseas stock exchange or other regulator which is available to the public. The copy given to ASX must be in English.'

Only 'material' information needs to be disclosed under LR 3.1. Therefore, there is an argument that section 323DA mandates disclosure of non-material information.

ACSI would argue for the retention of section 323DA and that the basis for this is more of a practical rather than legal nature:

- In a practical (rather than legal) sense, the 'materiality' of information is in some respects *subjective*. That is, different investors will place a slightly different weight on different types of information. Sometimes, an investor will regard as significant a piece of information that, as a matter of law (and as a matter of Listing Rule 3.1), is not 'material'.

    - For example, consider a piece of information relating to the corporate governance structures and processes of a company, which the company's lawyers have advised is *not* information that 'a reasonable person would expect to have a material effect on the price or value' of the company's shares; and hence is not required to be disclosed under LR 3.1. Assume the SEC mandates disclosure of the information. And assume several Australian institutional and retail investors place considerable importance on the information due to their committed approach to corporate governance. Currently, they have ready access to the information simply by reviewing the list of ASX announcements – because of section 323DA. But if section 323DA were to be repealed, these investors would have to monitor not only ASX company announcements but also SEC disclosures.

    - An actual example is the SEC regulations which require publicly traded companies (including Australian companies with ADR programs) to disclose a brief description of the material terms of any employment agreement between the company and a new senior executive within 4 business days of the appointment (on Form 8-K), and then file a copy of the full contract itself as an 'exhibit' to the next periodic report (e.g. annual report or quarterly report).

    - Australian legal advice may well be that LR 3.1. does not require the full employment agreement to be disclosed.

    - Currently, however, the full employment agreement is required to be disclosed as an ASX announcement due to section 323DA.

- A company can comply with section 323DA by sending the ASX a .PDF document electronically, at modest expense.

- As the above example indicates, section 323DA means that Australian shareholders in Company X can keep abreast of information disclosed by Company X anywhere in the world simply by reviewing the constantly updated list of ASX announcements. But if section 323DA were to be

repealed, these investors would have to monitor not only ASX company announcements but also SEC disclosures and possibly also disclosures made to the London Stock Exchange and other regulatory bodies overseas.

- Given the modest expense incurred by the company in making an identical disclosure to the ASX (by .PDF electronic filing), the potential benefits to shareholders – particularly those who have adopted a responsible approach to corporate governance – from retaining section 323DA outweigh the costs of complying with the section[2].

Conclusion

ACSI supports the general thrust of proposals that have formed part of this package, with the only divergence relating to a call for a modified position with respect to shareholders being able to call a general meeting and a re-think on practical grounds of the disclosure of information filed overseas.

We do regard the overall measures, when combined with other provisions contained in various corporate governance guidelines, coupled with increased shareholder activism and vigilance should establish a better corporate governance regime.

Should you require any further information please contact ACSI's Executive Officer Phillip Spathis on 03 9657 4386 or pspathis@mail.ifs.net.au.

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[2] ACSI would like to acknowledge the assistance of Dr. Geof Stapledon from Proxy Australia with respect to disclosure of information filed overseas.