

**Submission to  
Senate Committee of Rural and Regional Affairs  
and Transport Inquiry**

**REVIEW OF AUSTRALIAN WOOL INNOVATION  
LTD**

**June 2003**

**Prepared by WoolProducers**

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## 1.0 Introduction

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- 1.1 WoolProducers is the peak representative body for woolgrowers in Australia. WoolProducers is funded by voluntary contribution from State and individual members, and currently represents approximately 14,000 Australian woolgrowers.

WoolProducers has a mission to work on behalf of this membership to ensure that any company or organisation in receipt of compulsorily acquired levies operates in an ethical, transparent and efficient manner and such funds are carefully applied for the benefit of woolgrowers.

- 1.2 Pursuant to this core business activity, WoolProducers have closely monitored, liaised with and reported on the activities of Australian Wool Innovation Ltd (AWI) from the Company's inception to the present day. In fulfilling this role, WoolProducers have diligently monitored the Company's activities with direct regard to the legislative and other documents that bind the expenditure and operation of the Company. These are:

1.2.1 **The Statutory Funding Agreement with the Commonwealth (SFA or The Agreement)**

This agreement between the Commonwealth and AWI (and AWS during the holding period), governs how the compulsorily acquired levies may be expended, and obliges the Company to assume the arrangements outlined in the agreement to satisfy the Commonwealth that funds are being expended efficiently and for the purpose they were intended. It also outlines how the Company must satisfy the Commonwealth that Commonwealth Matching Funds are being expended for the purpose for which they were intended. Minister Truss agreed to contract with AWI the provision of Commonwealth Matching Funds on the terms and conditions of this Agreement. A breach of this agreement by the Company places this provision of Commonwealth funds into wool research and development into most serious jeopardy.

WoolProducers have identified in Point 3 of this submission, the clauses of the SFA that are applicable to the key areas of concern and questionable expenditure.

1.2.2 **The Commonwealth Levy Guidelines and Principles**

The Government introduced 12 Levy Principles in January 1997. These principles must be met when an industry proposes a new levy, or changes to an existing, Statutory Levy. Levy Guidelines have also been established as an adjunct to the Principles to assist industries with implementing the Levy Principles. The SFA refers to the Levy Guidelines as follows:

*Clause 5.3 "In determining how to spend the funds the Company must have regard to: (d) the Guidelines (to the extent applicable to the type of expenditure concerned.);"* and *Schedule 4, Clause 2.1 "In deciding on expenditure for research and development, the Company Board shall take into account the Guidelines."*<sup>12</sup>

The Guidelines note that application of compulsorily acquired levies must meet the principle requirements for the collection of Statutory levies, which is the establishment of net industry benefit and market failure. The Guidelines note that where there is a failure to demonstrate a net industry benefit and market failure, statutory levies will not be supported.

(Ref L) Guideline M) states that:

Statutory Levies are not to be used to fund agripolitical activities.

SFA Clause 16.3 states that the Company must also take into account the Guidelines in developing the strategic plan.

SFA Clause 17.1 (b) states that when delivering the Operational plan to the Commonwealth, AWI must include a compliance statement as to how those programs align with the Company's Strategic Plan and the Guidelines.

The relationship of the SFA to the Guidelines is inextricably linked.

While the Levy Guidelines and Principles are essentially non-binding, the requirement for AWI to acknowledge and adhere to them under the Agreement, is binding.

#### 1.2.4 The Company's Strategic and Operating Plans

The Agreement requires that the Strategic Plan of the Company must be provided to the Commonwealth. It is as part of this strategic plan, that a Corporate Governance Statement must be provided to the Commonwealth, outlining the Directors responsibilities in terms of planning (Ref SFA pg 13, 16.2, dot point 5.).

The Agreement also requires the Company to provide the operational plan prior to July 1 each year to the Commonwealth. The Operational plan should cover issues such as:

- (a) the intended operations of the Company for the next financial year;*
- (b) research and development programs to be undertaken by the Company, including a compliance statement as to how those programs align with the Company's strategic plan and the Guidelines.*
- (c) Budgets of expenditure; and*
- (d) Any other matters the directors consider should be set out in the plan*

#### 1.2.5 Corporations Law

Woolgrowers endorsed through a plebiscite, the establishment of a Corporations Law Company, with a commercial board with skills relevant to its objects, to undertake research and development activities and other activities for the benefit of woolgrowers. In addition to the Agreement and obligations noted above, the Company must at all times act within the Corporations Law.

1.3 **Australian Wool Services (AWS) and Australian Wool Innovation (AWI)**

Australian Wool Services (AWS) was established as the Holding Company in November 2000. AWI demerged from AWS in May 2002, and as such some information in this submission will relate directly to the activities of AWS as the parent Company responsible for addressing the Company's obligations to woolgrowers and the Commonwealth.

Section 37.1 of the SFA states:

*"- For so long as the Company is a subsidiary of AWS, AWS must ensure that the Company complies with all its obligation under this agreement."*

Therefore the individual Directors of both AWS and AWI are responsible for the ensuring the Company's compliance with the SFA and other obligations.

1.4 Until May 2002 the Board of AWS comprised "A" Class directors and "B" Class directors. The "A" directors as indicated below, were also directors of Australian Wool Innovation Pty Limited (AWI). The "B" directors as indicated below, were directors of TWC Holdings Pty Limited (TWCH). Directors appointed to these positions on AWS were:

Mr Rodney Price (AWS and TWCH Chairman) - B  
Mr Sam Chisholm - B  
Mr Trevor Flugge AO - B  
Mr Dieter Vollstedt - B  
Mr Donald Nelson - B  
Mr David Connors was the Managing Director of TWC

Ms Maree McCaskill (AWI Chair) - A  
Mrs Patricia Murphy - A  
Mr John Patten - A  
Mr Michael Staley - A  
Dr Andrew Vizard - A  
Mr Colin Dorber was the Managing Director of AWI (with board voting entitlement)

1.4.1 Changes to the composition of the boards began in March 2002, when:

- Director Vizard resigned from the Board of AWI;
- Director John Patten resigned from the Board of AWI and was appointed to the board of TWC by the Board of AWS;
- Director Don Nelson was removed from the board of TWC and was appointed to the Board of AWI by the board of AWS and AWI to fill the vacancy created by the resignation of Director Patten;

- Director Alan Trounson was appointed in July 2002 to the Board of AWI by the Board of AWI to fill the vacancy created by Dr Vizards resignation; and

- Director Peter Sykes was appointed to the Board of AWI by the board of AWI in August 2002 to address the publicly argued shortage of wool industry expertise on the board.

Concerns raised due to the changes to the without shareholder involvement are addressed in further detail in Section 4 of this document - 'Corporate Governance.'

This list identifies those Directors, who under Corporations Law, were personally responsible for the ethical and efficient conduct of the Company at one time or another throughout the period in question. It was the responsibility of these individuals to ensure the Company complied in a transparent manner in all respects to the Statutory Funding Agreement and other obligations imposed upon it due to the receipt of statutory levy monies.

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## 2.0 Executive Summary

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### The Nature of Australian Wool Innovation Limited

Australian Wool Innovation is a unique organisation that functions as a commercial company, under Corporations Law, yet is governed by its agreements with government under which it received compulsory acquired funds.

- While it is a company, that has shareholders and responsibilities accountable to ASIC, no shares are tradeable and therefore there is no degree of rigour placed on the organisation by the market. i.e. the company's performance is not determined by the market. There is no way that shareholders can redeem their equity in the company.
- In many ways it is a hybrid organisation which has been developed to solve the perceived problems that industry and government has had with statutory organisations. Therefore Corporations Law, Common and Case law as well as the Statutory Funding Agreement with Government are all needed to give effective oversight of its functions.
- The Directors of this Company must attend to their normal fiduciary duties as a Director in addition to the obligations placed upon them as the trustees of monies compulsorily contributed by Australian woolgrowers.

### Agreement on Structure

The wool industry was united in agreement that the structure of the industry's service organisations was finally right. The new structure was to deliver on the recommendations of the McLachlan Taskforce report for the future of the wool industry, thus ensuring levy funds were invested in targeted research, development and innovation. This is, it was hoped, would ensure that the decisions on how wool levy funds were spent were more transparent and supply of services more contestable.

- The Statutory Funding Agreement (the Agreement, or SFA) was established under the Act to govern the use of taxpayers' dollars and woolgrowers levies. Again, the wool industry as a whole was satisfied that the agreement was entirely suitable for the unique purpose it was drafted to serve.
- WoolProducers believe it is not the structure of the wool industry service organisations, nor the Agreement, that has been responsible for what has occurred over the past two years involving debate about the appropriate controls and expenditure of grower and government funds. Rather it has been the application of that structure that was in a large part removed from woolgrower shareholders by those that were initially appointed to oversee the companies.
- WoolProducers believe that greater care should have been given to the initial appointments.

### Major Discussion points

This submission will concentrate on the following:

- breaching the Statutory Funding Agreement;
- operation inconsistent with the Commonwealth Guidelines;
- poor governance and business practices;

- oppressive conduct toward shareholders;
- excessive periods without proper strategic plans in place; and
- failure to adhere to the strategic and operational plans that did exist.
- - a constitution which has major impediments in allowing shareholders to nominate to a ballot for the position of director of AWI.
- clear errors of business and of governance practice.
  - it appears that there may have been other practices (which we trust the Senate subcommittee will shed some light) that while not necessarily illegal, would be morally repugnant to most woolgrower shareholders.

#### Shareholder Franchise

We do believe, in the absence of the knowledge the Committee will acquire, that most problems have been addressed, largely by the determined involvement of shareholders' in the election of the McLachlan Board. This involvement was promoted and led by WoolProducers in its national leadership role.

- The fact that these problems have been addressed without changes to the structure of the organisation or to the Agreement, by changing only those persons responsible for directing t from the AWI board, is a true indication that the problem is not a structural one.

#### Executive Conclusion

We commend the Senators who called for the formation of this Inquiry and feel that for the Inquiry to be successful that it needs to reach the underlying reasons why an organisation, with a structure that is apparently correct, betrayed the trust of woolgrowers and broke its agreement with the Government.

### 3.0 Statutory Funding Agreement - Key areas of concern

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*“Every decision of the directors is made to provide a return on the investment of members... and all projects are constantly assessed and managed on the basis of being able to provide a return, or potential return.”*

AWI Chair Ms McCaskill, letter to the editor of the Weekly Times  
28/08/02

WoolProducers concerns with the expenditure and operation of AWI from Nov 2000 to November 2003 in many instances relate directly to the Company’s compliance with the Statutory Funding Agreement.

It is the opinion of WoolProducers that the programs and items of expenditure detailed below are inconsistent with the Company’s obligations under the Statutory Funding Agreement and the Commonwealths Guidelines for the collection and expenditure of statutory levies.

An overview of potential breaches of the Agreement is provided in Tables 1 & 2 in *Attachment A*.

#### 3.1 AWI funding of global design awards

*Attachment B* – AWI press release January 4, 2002 – “Wool to actively support UK design awards”

*Attachment C* – WoolProducers correspondence to Minister Truss, February 2002

*Attachment D* – WoolPoll Voter Information Kit (copy)– pages 10 & 11

- 3.1.1 In January 2002, AWI announced that the Company would be spending growers levy money for a series of global design awards.
- 3.1.2 The quantum of expenditure committed to these awards was published to be 10,000 pounds per year. However the 2002-2003 Operational Plan, which was produced and published AFTER the program had been initiated by AWI, states that European Wool Innovation Awards would be funded to the tune of \$2.3 million over the five year period 2003 – 2008.
- 3.1.3 WoolProducers expressed to both AWI and the Commonwealth that, according to the documents and principles that bind the expenditure of the Company, that we found the application, amount, and source of levy funds to be applied in this instance to be inappropriate, particularly as:
  - 3.1.3.1 - Distancing any promotional activities from R & D was the preference of the wool industry post-Goulbourn, hence The Woolmark Company now exists in its own right to market and

promote the developments of the Australian Wool Industry. TWC has clear indicators for performance measurement of its promotional activities and mechanisms to identify resulting grower benefits. The funding of global design awards should therefore be the business of The Woolmark Company, or perhaps, Woolmark Design International.

3.1.3.2 - There are no means in place for AWI to measure the performance of these R&D levy funds and report to growers a tangible return on investment.

3.1.3.3 - This promotional activity does not address the core business of a company in receipt of statutory levy funds, namely market failure research, as clearly defined by the federal Government's Levy Principles and Guidelines and Statutory Funding Agreement.

3.1.4 WoolProducers requested that AWI provide immediate advice to shareholders regarding the concerns noted above, and requested a written reply to the following points;

- I. How AWI will demonstrate that an investment into global design awards results in definable and measurable benefits to Australian wool producers,
- II. How promotional expenditure is justified as a valid investment of levy funds and how this activity will be reconciled in regard to Commonwealth Statutory Funding Agreement, and
- III. How promotional expenditure is justified as a valid investment of levy funds considering the role of The Woolmark Company in international marketing, promotion and innovation.

3.1.5 No reply was forthcoming from AWI.

3.1.6 The WoolProducers correspondence to the Minister dated Feb 2002, noted that this activity did not address the core business of a Company in receipt of statutory levy funds, namely market failure research, as clearly defined by the Levy Guidelines and obligations under the Statutory Funding Agreement. WoolProducers sought advice from the Minister as to whether AWI had provided a compliance report to the Commonwealth to outline how programs such as this align with the Company's strategic plan and Levy Guidelines. No reply was forthcoming from the Commonwealth.

3.1.7 A newspaper report by The Weekly Times on Wednesday 26<sup>th</sup> June 2002 entitled "Vizard tells: Why I Quit" (Attachment U) on the reasons for Director Andrew Vizard's resignation from the Board of AWI, stated:

*"Mr Vizard said he was also concerned that a number of controversial projects were never discussed at Board level. He said the forestry and revegetation program –*

*announced last year to a storm of protest – was never discussed by the Board. Nor were most of AWI's current wool marketing initiatives, such as the funding design awards and assistance to mills."*

- 3.1.8 Mr Dorber replied that it was board policy that projects requiring funding of less than \$2million did not need Board approval. Mr Dorber also said that he realised this was a grey area for AWI and, for this reason, he would be putting the matter to shareholders at the next AGM. Subsequently this action never occurred.
- 3.1.9 On close examination of AWI AGM transcript (refer to Attachments Z) and meeting notices it was noted that this information was never offered to Shareholders.
- 3.1.10 WoolProducers believe that this item of expenditure is not consistent with the SFA and Levy Guidelines in the following areas:
- 3.1.10.1 This project does not adhere to requirements under Section 5 of the Agreement, which defines how the Company may apply Levy Funds. Promotion by way of financial rewards for international designers does not align with any of the allowable areas under Section 5.1.
- 3.1.10.2 This section 5.1 of the Agreement also states that in each case the application of funds must be for the benefit of Australian woolgrowers. The net industry benefit of this project was not identifiable or quantifiable, and was not addressing market failure, therefore was also inconsistent with the Commonwealth Levy Guidelines and Principles.
- 3.1.10.3 This project does not address the criterion to qualify as a 'research and development activity', under Schedule 4 of the Agreement, as required by Clause 5.2. It also appears that the Company did not properly consider Section 5.3 of the Agreement when determining to spend funds in this manner.
- 3.1.10.4 This project does also not fit into any area of the R & D definition as described on page 4 of the agreement:
- 'R & D', in relation to Industry, means systematic experimentation and analysis in any field of science, technology, economics or business (including the study of the social or environmental consequences of the adoption of new technology) carried with the objective of:
- (a) acquiring knowledge that may be of use in achieving or furthering an objective of the Industry, including knowledge that may be used for the purpose of improving any aspect of the production, processing, storage, transport or marketing of wool or wool products; or

(b) applying such knowledge for the purpose of achieving or furthering such an objective.

3.1.10.5 Section 5.3 a) states that: In determining how to spend the funds the Company must have regard to the outcomes of the most recent poll of Australian woolgrowers. In this case, it is the results of the inaugural WoolPoll 2000.

On page 10 of the WoolPoll Voter Information Kit (Attachment D), which outlines what growers would be investing in should they vote for a 2% levy, clearly stated that there would be no investment in Retail and Consumer Marketing. It was also made clear to growers (page 11) that should they vote for a higher levy which would include investment into Retail & Consumer Marketing projects, that these projects would be assessed on a competitive basis and would have to demonstrate real benefits before funds would be allocated to them.

3.1.10.6 If the Company had intended this project as an eligible R & D activity, they would be obliged under the SFA to have a documented account of internal controls that define how that activity is eligible for matching Commonwealth Funds and is within the R & D component of the Strategic Plan and Operational Plan, in accordance with Schedule 4, Clause 4.1 a – b.

3.1.10.7 The Company should have provided notice of this proposed expenditure to the Commonwealth in the Operational Plan required to be delivered before July 1 each year in accordance with Section 17 of the Agreement. The Company is also required to provide assurance to the Commonwealth by way of a 'compliance statement', (as required under Section 17.1 b) of the Agreement) that this program of expenditure aligns with both the Company's Strategic plan and the Commonwealths Guidelines.

3.1.11 At this time, February 2002, AWI was yet to demerge from AWS. Therefore in this instance, the Board of AWS under the Chair of Mr Rod Price was responsible for these breaches of the Agreement, according to Section 37.1 of the Agreement, which states:

*"For so long as the Company is a Subsidiary of AWS, AWS must ensure that the Company complies with all its obligations under this Agreement."*

3.1.12 Mr Price's board in this instance would be responsible for, and therefore in breach of, Section 4 and Schedule 4 of the Agreement, which provides that the Company must have adequate internal controls that ensure:

*“Section 4. Management of Funds*

- 4.1 (a) *the Funds are used only in accordance with the agreement;*  
(b) *all dealings with the funds are properly authorised, conducted and accounted for; ... ..”*

Schedule 4

*R & D Expenditure Management*

*Clause 4, 4.1 The Company shall implement a documented system and appropriate internal controls to ensure:*

- (a) *that R & D activities and expenditure which the Company intends to be Eligible R & D Activities and expenditure are eligible for matching funds in line with the agreed definition; and*  
(b) *that R & D activities and expenditure which the Company intends to be eligible R & D activities and expenditure are within the research and development component of the Strategic and Operational Plan; and*  
(c) *clear lines of accountability are present and identifiable.*

3.1.13 WoolProducers sought advice from the Commonwealth in February 2002, as to how this expenditure aligned with the Company's obligations under the Agreement and Levy Guidelines. WoolProducers also sought advice from the Commonwealth relative to the provision of the Operational Plan and subsequent compliance statement by AWI as required by the Agreement. To date, no response has been forthcoming.

3.1.14 It is important to note that the issue at stake with regard to market-like activities is about compliance to the SFA (and the commitment to “test” this concept at an AGM). As we approach 3 years since the Goulburn AGM it is likely that growers may wish to re-evaluate the nature, (direct or indirect) and direction of their investment in marketing or promotion in the industry more broadly than currently. However if in responding to changing demands and circumstances a need is identified to provide AWI levy funds for promotion, then the company must ensure that:

- the SFA is not breached, and that;
- this process is done overtly and in careful consultation both with growers, their representative bodies such as WoolProducers, and with government
- It would logically also be developed with other key wool companies, such as The Woolmark Company.

3.2 **National Woodlots Advisory Service Project**

*Attachment E* – AWI press release 28<sup>th</sup> January 2002 – “National Woodlots Advisory Service to add further value for wool

*Attachment F* - AWI press release 18 February 2002 – “What’s in a name – woodlot gets the chop.”

3.2.1 AWI announced funding into a farm forestry advisory service on January 29, 2002. WoolProducers called for AWI to immediately cease establishment and funding of the proposed National Woodlot Advisory

Service. The project did not address any area of market failure, provide demonstrated benefits to the wool industry not already available commercially or publicly, or align with the Company's obligations under the Agreement.

- 3.2.2 WoolProducers advised the Commonwealth of this program and its inconsistencies with the SFA and Levy Guidelines in correspondence dated February 2002 (Refer Attachment C). WoolProducers also met with the Ministers office on in February to bring this matter to the urgent attention of the Minister.
- 3.2.3 The project clearly demonstrated lack of regard to:
- the published AWI strategic plan,
  - government guidelines for the expenditure of compulsory levy funds,
  - Commonwealth Statutory funding agreement
  - real issues affecting the profitability and sustainability of Australian woolgrowers
- 3.2.4 There was no positive reply from AWI. The only action taken by the Company in light of woolgrowers' reaction was to change the name of the project. The Managing Director explained in a press release dated February 18, 2002 (Attachment F), the name had caused confusion and the project was actually an NRM/sustainability initiative.
- 3.2.5 WoolProducers rejected this explanation as AWI had already invested \$18 million into a \$58m joint initiative with Land & Water Australia (LWA) named "Land, Water and Wool." LWA's total investment into this project was approx. \$40m.
- 3.2.6 The newspaper report by the Weekly Times on Wednesday 26<sup>th</sup> June 2002, on the reasons for Director Andrew Vizards resignation from the Board of AWI, stated:
- "Mr Vizard said he was also concerned that a number of controversial projects were never discussed at Board level. He said the forestry and revegetation program – announced last year to a storm of protest – was never discussed by the Board. Nor were most of AWI's current wool marketing initiatives, such as the funding design awards and assistance to mills."*
- 3.2.7 WoolProducers believe that the expenditure committed by the Managing Director in this instance, constitutes possible breaches of the Agreement and Levy Guidelines in the following areas:
- 3.2.7.1 This project does not adhere to requirements under Section 4 and Schedule 4 of the Agreement, Management of R & D funds. The project is also inconsistent with Section 5, which defines how the Company may apply Levy Funds. This expenditure does not align with any of the allowable areas under Section 5.1., and is in direct conflict with Clause 5.1 f) that allows the Company only to spend funds on providing

wool industry services that are not otherwise commercially available.

3.2.7.2 Section 5.1 of the Agreement also states that in each case the application of funds must be for the benefit of Australian woolgrowers. The net industry benefit of this project to woolgrowers was not identifiable or quantifiable. As the forestry consulting service was otherwise commercially or publicly available, the project was not addressing any form of market failure, and as such was also inconsistent with the Commonwealth Levy Guidelines and Principles.

3.2.7.3 The Company should have provided notice of this proposed expenditure to the Commonwealth in the Operational Plan required to be delivered before July 1 each year in accordance with Section 17 of the Agreement. The Company is also required to provide assurance to the Commonwealth by way of a 'compliance statement', (as required under Section 17.1 b) of the Agreement) that this program of expenditure aligns with both the Company's Strategic plan and the Commonwealths Guidelines.

3.2.8 At this time, February 2002, AWI was yet to demerge from AWS. Therefore in this instance, the Board of AWS under the Chair of Mr Rod Price was responsible for these breaches of the Agreement, according to Section 37.1 of the Agreement, which states:

*"For so long as the Company is a Subsidiary of AWS, AWS must ensure that the Company complies with all its obligations under this Agreement."*

3.2.9 Mr Price's board in this instance would be responsible for, and therefore in breach of, Section 4 of the Agreement, which provides that the Company must have adequate internal controls that ensure:

*"... 4.1 (a) the Funds are used only in accordance with the agreement;  
(b) all dealings with the funds are properly authorised,  
conducted and accounted for; ... .."*

3.2.10 WoolProducers sought advice from the Commonwealth in February 2002, (Attachment C) as to how this expenditure aligned with the Company's obligations under the Agreement and Levy Guidelines. WoolProducers also sought advice from the Commonwealth relative to the provision of the Operational Plan and subsequent compliance statement by AWI as required by The Agreement. To date, no response has been forthcoming.

3.3 **AWI Red Cross Farmhand donation**  
*Attachment G* – Transcript from Alan Jones program 24<sup>th</sup> October, 2002  
– Interview with Mr Colin Dorber announcing the donation.

*Attachment H* – Transcript from Jeff Kennet radio program – Interview with Red Cross on the return of the AWI funds.

*Attachment I* – Weekly Times article November 27, 2002 – “Drought cash reclaimed.”

*Attachment J* – Weekly Times article, December 4, 2002 - “Donation legality in doubt.”

- 3.3.1 In the lead up to the election of AWI Directors on 24<sup>th</sup> October 2002, AWI MD Mr Col Dorber announced on the Alan Jones radio program that they were donating \$500,000 to the Farmhand Appeal. The Farmhand Appeal was established to provide financial assistance to drought affected farmers.
- 3.3.2 When questioned at the AWI AGM, Mr. Col Dorber announced that AWI had placed caveats on the donation and strict guidelines on the application of the funds. He stated that these funds would only be applied to research and development that would provide a measurable return to growers, and that any excess funds would be returned to AWI. He also said that anyone wishing to see a copy of the agreement between AWI and the Red Cross only had to ask.
- 3.3.3 WoolProducers asked Mr Dorber for a copy of this agreement on (ph)14<sup>th</sup>, (e-mail)15<sup>th</sup>, (ph msg)18<sup>th</sup> and (ph) 19<sup>th</sup> of November. Whilst promising the provision of the agreement on each occasion, Mr Dorber never did provide the ‘agreement’ referred to in 3.3.2.
- 3.3.4 In the meantime, after speaking to various people at the Red Cross, WoolProducers Executive Director Ms Turner was put in touch with the coordinator of the Farmhand Appeal, Mr David Childs, who had been dealing with AWI on this matter.
- 3.3.5 The sequence of events as relayed by the Red Cross coordinator were as follows:
  - 3.3.5.1 AWI attempted to transfer the \$500K electronically to the Farmhand Appeal through the Farmhand Foundations web-site on 18<sup>th</sup> October. The website rejected this transaction due to the size.
  - 3.3.5.2 A cheque for \$500K was then hand delivered to the Red Cross Coordinator on the 18<sup>th</sup> October, with NO accompanying letter or anything else for that matter. Just the cheque was provided.
  - 3.3.5.3 After discussions between the Red Cross and AWI, the donation was to be announced at the Farmhand Benefit Concert in Sydney.

- 3.3.5.4 Red Cross received a call from Mr Col Dorber AWI on the night before the concert where they were advised that there was to be absolutely no more publicity on the donation. The concert announcement was cancelled.
- 3.3.5.5 More than a week after the money was donated, and approximately 5 days after the Alan Jones interview, the Red Cross rec'd a letter from AWI requesting that certain conditions be applied to the donation. (WoolProducers have requested a copy of this letter.) The Red Cross refused this request by AWI MD Mr Col Dorber, and expressed their annoyance at being placed in such a position. They stated that the terms of the appeal were widely published and deemed to be understood by anyone who offered a donation. The Red Cross coordinator also advised that it would be very difficult, if not impossible, to ensure that those funds were directed specifically to woolgrowers in any way.
- 3.3.5.6. The Red Cross was then contacted by an AWI staff member requesting a letter of commitment to the 'new arrangement' proposed by AWI. The Red Cross coordinator was advised by the AWI staff member that this signed agreement was necessary immediately as AWI had a Board meeting in half an hour. (This was the newly elected Board).
- 3.3.5.7 As far as WoolProducers understand that under advice the Red Cross took the matter to the new Board of AWI in pursuit of a suitable outcome.
- 3.3.6 On the morning of the Senate Estimates Hearing in November 2002, Mr. Dorber contacted WoolProducers looking for contacts in the Senate Estimates Committee and to tell WoolProducers "The Farmhand donation was no longer their business". Mr. Col Dorber advised that the cheque had been returned to AWI.
- 3.3.7 WoolProducers believe that these funds were clearly not allocated for the purpose of R & D investment to benefit the wool industry as:
- there was no relevance to the Company's strategic or operational plans
  - there was no competitive tender process for the R & D
  - there was no evidence of any formal process by which the Red Cross was identified as the best provider of drought / water management research.
  - Dorber had outlined in a release with Minister Truss in October, that AWI would deliver a \$760,000 package of commercially relevant drought R & D on 25<sup>th</sup> October. There was no mention of Red Cross / Farmhand involvement in this program, and \$500K donation was not included in the \$760K program total that was announced and advised to the Minister.
- 3.3.8 The assessment process for projects taken from the AWI web-site states:

### *Assessment*

*We have developed two objective project assessment tools to evaluate project proposals at both the concept and project stages.*

*The AWI Project Scorer is complex series of spreadsheets used to assesses each proposal across a number of areas. It generates an overall project score, which may be used to compare the proposal with others. It features:*

- *A quality control checklist;*
- *A project scoresheet for technical and commercial success, benefits, and strategic fit; and,*
- *A net present value (NPV) calculator.*

WoolProducers believe that no checks and balances such as establishment of performance indicators, or industry return on investment were reviewed in regard to the donation. The expenditure of growers' money in this instance is not only inconsistent with the Agreement, but also normal internal controls and operational procedures.

- 3.3.9 WoolProducers believe that the expenditure committed in this instance, regardless of the return of the cheque, constitutes most serious breaches of the Agreement and Levy Guidelines in the following areas:

3.3.8.1 The donation of funds in this manner aligns with the definition of agripolitical activity described on page 2 of the Agreement:

*"Agri political activity means political campaigning or funding, developing, designing, resourcing or participating in activities intended to exert political rather than advisory influence on government policies or in activities intended to exert political influence on public opinion."*

It is widely believed the intent of this donation was to influence the public perception of the McCaskill Board in the minds of drought-affected woolgrower shareholders who would be deciding on their choice of AWI Directors.

WoolProducers therefore believe this expenditure is in direct breach of: Section 5 Clause 5.6 of the Agreement, which states that the Company must not spend funds on Agri-Political Activity.

- 3.3.10 WoolProducers also believe that the Agreement and Guidelines were breached in the following areas:

- Section 4 and Schedule 4, 1.2 and 4.1 - Eligible R & D Activities and Management of R & D Funds;
- Section 5 -The application of Funds:  
Clause 5.1, which outlines how the Company may spend the Levy funds;

Clause 5.3, which states that the Company must have regard to the most recent grower poll, Company's strategic plan, Company's operational plan and the Guidelines, in determining how to apply the levy funds;

### 3.4 The Sommerville Collection

3.4.1 AWI had donated \$100,000 cash to a mineralogical collection at Charles Sturt University, named 'The Sommerville Collection', and committed to an "in-kind" donation of \$150,000. This was the purchase of wool carpets and fittings for the area housing the collection.

3.4.2 A plaque from the University acknowledging AWI as a major contributor to the Collection was displayed in the foyer of AWI.

3.4.3 WoolProducers have been advised that the current McLachlan board has successfully rescinded the \$150K "in kind".

3.4.4 Breaches of the Agreement in this instance would include:

- This project does not address the criterion to qualify as a 'research and development activity', under Schedule 4 of the Agreement, as required by Clause 5.2.

- This project does not fit into any area of the R & D definition as described on page 4 of the agreement.

- Section 4, Management of Funds; Schedule 4, 1.2 and 4.1 - Eligible R & D Activities and Management of R & D Funds;

- Section 5 -The application of Funds:  
Clause 5.1, which outlines how the Company may spend the Levy funds;

  - Clause 5.3, which states that the Company must have regard to the most recent grower poll, Company's strategic plan, Company's operational plan and the Guidelines, in determining how to apply the levy funds;

- Schedule 4, Eligible R & D Activities

- The project also fails to address the key principles of the Guidelines, being the establishment of market failure and net industry benefit.

### 3.5 'Moving Towards the Knowledge Economy' Seminar

3.5.1 A conference on the "Moving Towards the Knowledge Economy" (see *Attachment W*) was run by the NSW Government's Office of Western Sydney. The Conference was hosted by Mr Kim

Yeadon, the Minister for Information Technology, Minister for Western Sydney, and also Minister for Forestry.

The Managing Director agreed that AWI would be a platinum sponsor. Mr. Dorber obtained the right to add his welcome to that of the Minister for Western Sydney (who is also the Minister for Forestry), and the Premier.

3.5.2 AWI was the only platinum sponsor. WoolProducers established that a platinum sponsorship cost either \$30,000 in cash or \$50,000 of payment in kind. (Gold sponsorship was \$15,000, Silver \$10,000 and Bronze \$7500).

3.5.3 The decision to sponsor at any level was dubious. At the most the wool industry body should only have offered \$7,500 (Bronze), if the conference met appropriate communications or learning strategic criteria.

3.5.3 Breaches of the Agreement in this instance would again include:

- This project does not address the criterion to qualify as a 'research and development activity', under Schedule 4 of the Agreement, as required by Clause 5.2.

- This project does not fit into any area of the R & D definition as described on page 4 of the agreement.

- Clause 4, Management of Funds;

- Section 5 -The application of Funds:

  - Clause 5.1, which outlines how the Company may spend the Levy funds;

  - Clause 5.3, which states that the Company must have regard to the most recent grower poll, Company's strategic plan, Company's operational plan and the Guidelines, in determining how to apply the levy funds; and must always apply the fund in a manner that is efficient, effective and ethical.

- Schedule 4, Eligible R & D Activities

- The project also fails to address the key principles of the Guidelines, being the establishment of market failure and net industry benefit.

### 3.6 Election – General Expenses

*Attachment K* – Paid advertisement in The Land newspaper, 17 October, 2002

*Attachment L* – Paid advertisement in various Rural Press publications – 16 – 17 October, 2002

*Attachment M* – Weekly Times article, September 25<sup>th</sup>, 2002

*Attachment X* – The letter from Chairman Ian McLachlan 11<sup>th</sup> June 2003 page 6 re AGM payments in relation to election expenses

The AWI Board under the lead of Managing Director, Mr Col Dober, were very active in a campaign to protect their positions at the 2002 election. This section deals specifically with funds expended by the board in the lead up to that election. Further information detailing concerns relating to governance and board responsibilities is outlined in Point 4 – ‘Corporate Governance and Obstructive Behaviour’ – Key Areas of Concern’.

- 3.6.1 Col Dorber told journalists at the Victorian Rural Press Club on 18 October that the AGM election campaign had cost \$200,000 to date and that further expenditure was anticipated.
- 3.6.2 WoolProducers pulled together conservative cost estimates using publicly available information to give shareholders a guide to how much was being spent by Dorber and the McCaskill board on this campaign. Estimates were as follows:

- 3.6.2.1 Advertising - \$104,000

- AWI commissioned a number of full page advertisements in the lead up to the election.

- An advertisement (Refer Attachment K) was signed by ‘Concerned woolgrowers’. When Herald and Weekly Times staff were questioned as to who commissioned the ad, it was advised that AWI had attempted to place the ad but were refused by the publisher as the Company had requested the ad be placed without an authorisation from a/the grower.

- AWI then returned to the newspaper in a matter of hours with the name of grower, Geoff Raynor, to be used as the required authorising party to comply with the newspaper’s advertising protocols. AWI paid for the advertisements.

- WoolProducers believe this was deceitful and dishonest activity which was a clear breach of the Agreement relating to the expenditure of growers funds on agri-political activity. Clause 5.3, which states that the Company must have regard to the most recent grower poll, Company’s strategic plan, Company’s operational plan and the Guidelines, in determining how to apply the levy funds; and must always apply the fund in a manner that is efficient, effective and ethical, is clearly breached in this instance.

- 3.6.2.2 Telephone polling - \$12,000

- Among the questions included in the poll, were “Do you believe ex-politicians or state farm organisations should not

control AWI?" (Ref: Attachment M, Weekly Times article, September 25<sup>th</sup>, 2002).

3.6.2.3 Campaign related travel - \$6,000

It is the opinion of WoolProducers, that the McCaskill board and Mr Dorber used woolgrowers funds to pay for the attendance of their supporters at key events in the lead up to the election for the purpose of agri-political activity as defined in the Agreement. Further detail is included in Section 3.13.

3.6.2.4 TOTAL - \$122,000

3.6.3 WoolProducers members expressed outrage at the amount of levy-payer funds being marshalled by AWI to support the current board.

3.6.4 It was the opinion of legal advice commissioned by WoolProducers that the full page advertisements in The Land and The Weekly Times published by AWI in October 2002 were clearly aimed at:

- attacking the candidature of nominees not approved by the AWI Board; and
- promoting and soliciting votes in favour of the re-election of current Board members.

3.6.5 WoolProducers believe the Board had a fiduciary obligation to act in good faith in the best interests of the company and for a proper purpose, and that the use of AWI funds for the above purposes amounted to electioneering and could not be justified as a proper purpose.

3.6.6 According to the definition of the agri-political activity in the Agreement, the McCaskill Board and Mr Dorber again placed the Company in direct breach of Section 5 Clause 5.6 of the Agreement, which states that the Company must not spend funds on Agri-Political Activity.

3.6.7 This expenditure is also inconsistent with the requirement that the Company spend funds, as required for Category A and Category B payments under the Agreement, to provide woolgrower or broader community benefit.

**3.7 Strategic planning**

The McCaskill Board and Mr Colin Dorber took 18 months to produce a detailed strategic plan and business plan for AWI. A basic strategic statement largely prepared by the interim Board existed early in 2001, and should have meant that a full strategic plan and related business plan should have been available within 6 months of commencement – not 18 months. WoolProducers believe such the tardy delivery of the Strategic Plan is not consistent with the intent of Clause 16.1 of the Agreement which states:

*"The Company must provide to the Commonwealth a copy of a written strategic plan as soon as possible after the Conversion Time... .."*

- 3.7.1 Investments made in the absence of a public strategic planning framework in the interim are inconsistent with the Company's obligations under the Agreement.
- 3.7.2 AWI has failed to provide meaningful progress reports on R&D expenditure prior to the new strategic plan release. While large sums of money have been spent in the period between 1<sup>st</sup> January 2001 and the release of a strategic plan in mid 2002, there is no report which says how this expenditure has addressed strategic goals.

### 3.11 **Operating costs**

*Attachment N* – Ian McLachlan speech to NSW Farm Writers' Association, 28 March, 2003

*Attachment O* – Farm Weekly article, August 22, 2002.

*Attachment X* – The letter from Chairman Ian McLachlan 11<sup>th</sup> June 2003 page 5 re AGM payments in relation to election expenses

- 3.11.1 Ian McLachlan advised in his address the NSW Farm Writers' Association (refer Attachment N) the operating costs of the Company had been found to be ≈ \$20million. Subsequent to Mr. McLachlan's Farm Writer's interview, the former MD is believed to have claimed in an ABC radio interview that costs could only be ≈\$3.5million.
- 3.11.2 While WoolProducers accept that elements of this may be different accounting views of old and new Board, we still believe that an excessive amount is indicated. The amount appears very high to have spent on the administration of growers funds, and most unusual.
- 3.11.3 In an interview with the Farm Weekly, August 22<sup>nd</sup> page 1, Mr Dorber (Ref: Attachment O), had said that the operating costs of the Company were below the board approved budget.
- 3.11.4 The model that growers voted for in WoolPoll 2% model, flagged operating costs of \$6m (Refer Attachment D).

Section 5.3 a) of the Agreement states that: In determining how to spend the funds the Company must have regard to the outcomes of the most recent poll of Australian woolgrowers, in this case WoolPoll 2000. Operating costs of \$20m clearly breach the intent of this section of the Agreement.

### 3.12 **Unsigned contracts**

*Attachment P* – Weekly Times article April 2, 2003, - "Audit cans AWI contract process".

*Attachment Q* – Queensland Country Life article April 3, 2003 – “Board cleans up AWI mess”.

*Attachment X* – The letter from Chairman Ian McLachlan 11<sup>th</sup> June 2003 page 5 re AGM payments in relation to election expenses

- 3.12.1 Ian McLachlan advised in his address the NSW Farm Writers’ Association that a review has found 50 unsigned contracts, worth \$20-million. Ian McLachlan has said that an explanation has been sought from individuals previously employed by AWI, and investigations are continuing. The McLachlan Board has assured shareholders that absolutely no payments will be made in future without executed contracts in place. In his subsequent Letter to Shareholders (Attachment X) this figure for incomplete contracts is noted as \$22 million.
- 3.12.2 WoolProducers believe that in the absence of signed contracts such things as intellectual property and project outcomes are inadequately secured for growers who have put in their money. It seems large sums of money were spent without valid contracts in place and that kind of business practice is quite clearly not in the best interest of the Company and its shareholders.
- 3.12.3 Mr McLachlan also stated in this speech that:  
“ We have terminated contracts the Board has judged to be inappropriate or where it was not clear what the objects of the contracts were. Several lucrative consultancies have been terminated on this basis.”
- 3.12.4 Mr McLachlan said AWT’s audit also found an unsecured advance of \$500,000 was made to a sole-trader film production company, even though the company had not requested such an advance.
- 3.12.5 Breaches of the Agreement in this instance include Section 4. Management of Funds & Schedule 4 - R & D Expenditure Management Clause 4, 4.1.
- 3.13 **York St premises**
- 3.13.1 WoolProducers noted that AWI moving out of this purchased accommodation (the purchase itself being a dubious use of growers funds) after only 18 months from commencement was a sign of very poor planning and management, and a burgeoning staff. The public reply from Mr Dorber to these concerns, was that the rental of York St, completely covered the larger premises that they moved into in Barrack Street.
- 3.13.2 At the AGM, Dorber told shareholders that the return on the York St premises was 11.3 per cent per annum. This statement was untrue. The York Street premises had never been rented and was deriving no income at all for the Company.
- 3.14 **Directors fees**

*Attachment R* – The Land Queensland Country Life article, March 6, 2003 – “Ousted directors still on AWI payroll” and Queensland Country Life, article “AWI pays sacked Directors” also dated March 6, 2003.

*Attachment S* – AWI 2002 Annual Report, copy – page 32

*Attachment X* – The letter from Chairman Ian McLachlan 11<sup>th</sup> June 2003 page 4

3.14.1 When questioned by reporter, James Nason, if some members of the Board were pre-paid their annual Board fees in June 2002 for the entire 2002-2003 financial year, Ian McLachlan confirmed that this was the case. “The auditors have brought forward a couple of these matters, so that money is going to have to be paid back, even though those people are no longer there,” said Mr McLachlan.

3.14.2 It appears that this payment was not disclosed at the AGM or in the Annual Report, either as fees, or as loans to Directors, which should have rightfully been done as part of normal disclosure to shareholders. Page 32 of the AWI 2002 Annual Report states,

“Directors Interest:

During the reporting period there were no transactions between any of the Company’s directors or director related entities and the company and its associated entities...”.

### 3.15 Renegotiation of contracts

*Attachment T* – Weekly Times article 19<sup>th</sup> February 2003 – “Final deal for AWI Execs”.

3.15.1 Dorber assisted several key staff to renegotiate their contracts after the election so that they would receive a bigger payout if made redundant by the new Board. This meant that any reorganisation by the new Board as they reviewed performance was potentially very difficult and expensive. The terms were in general, 6 months notice, and 12 months payment of salary on retirement. Dorber changed these contracts between 18<sup>th</sup> and 25<sup>th</sup> of November, after the election, without consulting the newly elected Board.

### 3.16 Woolgrowers Advisory Group (WAG)

A twelve person Wool Advisory Group with the charter to provide input into the management of Australian Wool Services Limited (AWS) and Australian Wool Innovation was announced by AWS Chairman, Mr Rod Price and AWI Chairperson, Ms. Maree McCaskill on July 17, 2001.

3.16.1 WoolProducers were critical of the method of appointments, preferring that open and transparent processes apply to establishment of this or any advisory group, for example: wide publishing of clear terms of reference,

required skills and process of application, closing dates, etc. so that any grower with the appropriate skills could apply.

The WAG however, remained as a group of Price / McCaskill appointees, and increased in number when combined with the Women in Wool group. The WAG was apparently charged with providing the AWI Board with feedback from a growers perspective.

It is also our opinion that the operations of the WAG funded by woolgrowers levy in the lead up to the 2002 election of Directors, was almost entirely agri-political in nature, and as such constituted a most serious breach of the Agreement.

- 3.16.2.1 In a letter to the Editor of The Land newspaper on 10<sup>th</sup> October 2002, a group of WAG members claimed that the WAG was independent to AWI. This is a false and misleading statement.
  - 3.16.2.2 It is believed that WAG members were reimbursed expenses to travel to the Victorian Press Club address by Ian McLachlan, to pose questions in support of the McCaskill Board. A journalist, by the name of David Everist, was also paid to attend and posed hostile questions to Mr McLachlan. It is understood that AWI are in possession of receipt for this service.
  - 3.16.2.3 The WAG engaged in political debate in support by writing letters to the editors of various rural publications.
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## 4.0 Corporate Governance & Obstructive Behaviour

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- 4.1 Board governance is a critical issue with the Board of AWI responsible for the expenditure of ≈\$400 million over the next five years on research, development and innovation in the wool industry. The oversight functions of the Board come into sharp focus when dealing with this vast sum of money. WoolProducers raised significant concerns regarding the corporate governance of the Company in 2002 with both AWI and the Commonwealth.

Board transparency and open, accountable behaviour is expected by shareholders of any Company. It is WoolProducers opinion that a Company that works for *compulsory* shareholders has a *significantly* increased obligation in this area. It is WoolProducers opinion that in many instances Directors may have been responsible for oppressive conduct against shareholders and a failure to act in the best interests of the Company.

Corporate governance issues relate directly to the intent of Section 5.3 of the Funding Agreement, and as such, the failure of the Board to apply sound corporate governance practises to the expenditure and operation of the Company, places them in direct breach of this section of the Agreement.

These concerns related to a series of events which are outlined in detail below:

### 4.1 Resignation of Dr Vizard

*Attachment U* – Weekly Times article, 26 June 2002 – “Vizard tells: Why I quit”

*Attachment V* – Weekly Times article, 16 October, 2002 – “Can of worms – Leaked letter slams AWI Board”

- 4.1.1 The resignation of Dr Andrew Vizard from the Board of AWI in March 2002 sparked significant concerns regarding proper corporate governance of the Company.
- 4.1.2 At the time, Director Vizard was the only member of the board with skills and expertise in the areas of wool production and wool science.
- 4.1.3 In a newspaper report by the Weekly Times, Wednesday, 26 June 2002 (*Attachment U*) it stated that concern over a number of projects was among the reasons Mr Vizard resigned. The article revealed his concerns at:
- Facing re-election this year after being re-elected last year;

- The lack of expertise in wool production and technical knowledge on the AWI Board;
- The lack of investment in genetic research;
- The lack of discussion at board level on controversial projects such as forestry and revegetation;
- Decisions by the Board to spend money on marketing initiatives, such as fashion parades and assisting wool mills with promotion, which he believed were not in the understood remit of AWI as an R&D organisation.

4.1.5 Dr Vizard told the Weekly Times in this article that he was concerned that a number of controversial projects were never discussed at Board level. Mr Dorber replied that it was board policy that projects under \$2million did not need board approval.

4.1.6 Dr Vizard said he quit the board after being told in March that he would face re-election in October. The trigger for Dr Vizard's resignation was a dispute over last year's Australian Wool Services election in October 2001, where Dr Vizard and three fellow AWS Board members – Messrs. Rod Price, Trevor Flugge and Ms. Patricia Murphy – were re-elected for a three-year board term to the AWS Board. Mr Vizard said:

*“It was my understanding, and that of the board and shareholders, that Patricia Murphy and myself were being re-elected also to the AWI board.”*

4.1.7 Mr Dorber replied that, according to the Constitution, the election last year only applied for reappointments to the AWS Board. And because the AWI Constitution stipulated that the two longest serving directors be up for re-election this year, Vizard and Murphy would be the two candidates.

4.1.8 Dr Vizard contended the re-election applying only to AWS and not AWI was a process error in that both bodies should have recorded the retirement and reappointment of both Ms Murphy and himself.

4.1.9 Mr Dorber said the Board had sought legal opinion. That opinion provided three options for a resolution of the matter, one of which would have allowed the AWI Board to record a retirement and the subsequent re-election of Dr Vizard and Ms Murphy.

AWS Constitutional requirement to re-appoint Vizard and Murphy – Clause 15.5(b).

4.1.10 This option was rejected by the rest of the Board. Mr Dorber said that he voted against the option.

- 4.1.11 Dr Vizard told Rural Press that he hoped his resignation would make AWI think more clearly about corporate governance issues, and to act more responsibly on behalf of its corporate stakeholders.
- 4.1.12 WoolProducers were extremely concerned about Dr Vizard's resignation with particular regard to the reduction of skills available to the board and the serious matters of corporate governance raised.
- 4.1.13 There was no doubt in the minds of industry that in voting, the shareholders believed that they had re-elected Dr Vizard and Ms Murphy to the Board of AWI, at the AWS AGM and election in November 2001. In our opinion it was unacceptable that the value and intention of shareholders votes was undermined by a failure of process.
- 4.1.14 WoolProducers immediately sought advice from AWI Chair, Ms Maree McCaskill as to:
- Why this error in governance and process had occurred;
  - Why the Board voted against adopting a simple solution identified by legal advice; and
  - Why all shareholders were not advised immediately the error was detected.
- No reply was forthcoming from Ms McCaskill.
- 4.1.15 Ms McCaskill then took out full page advertisements in the rural press around Australia stating that Dr Vizard resigned due to workload pressures and that correcting the 'process error' that was among the principle reasons for his resignation would have been to deny shareholders of their basic democratic right. WoolProducers rejected the use of funds in this manner, and rejected the false assertions made by Ms McCaskill in advertisements.
- 4.1.16 It was also reported in a Weekly Times article 16/10/02 (Ref: Attachment V), that in a letter to board Chairman Ms. Maree McCaskill, Mr Vizard claimed that the performance review of Mr Dorber was conducted without "any normal measures of performance".
- 4.1.17 The Board had never communicated publicly to shareholders of AWI any of the following:
- That the 2001 AWS election had had no effect at all at on the AWI Directorships so that despite Vizard and Murphy standing for election at the AWS AGM in 2001, they remained the longest serving Directors of AWI. This was clearly not the intent of the election.
  - This failure of the intent of the election was never communicated publicly to shareholders

- That the Board actively voted against a solution which would have rectified the problem and maintained the integrity of the intention of the election at the AGM in 2001.

**It is our view that this:**

- Constituted a failure of the election conducted in 2001
- Raises questions about Board preparedness to resolve this failure by practical means
- Raises extremely serious concerns about the absence of any timely public notice to shareholders from the Board about an extremely important corporate matter, that is the appointment of Directors and the proper rotation of Directors subsequent to the AWS elections in October 2001.
- In excess of \$50M is raised annually by compulsory levies from shareholders. This is a very large amount of money constantly provided by the shareholders, and is unlike other public companies. Immediate and clear communication of any problem is essential to the rights of those shareholders.

This was further pursued on 25<sup>th</sup> June 2002 in a letter to AWI Chair Ms McCaskill which stated – “I refer to our letter to you dated 20<sup>th</sup> June and note that to date we have had no reply from you addressing the concerns outlined in that correspondence. That letter raises matters of significant and legitimate concern to WoolProducers and our members and we seek your reply as soon as possible”.

The issue of governance is very serious. It is quite clear that the current Board was aware of a failed election conducted at the AGM last year, and did not reveal this to the shareholders at all until it emerged in the public domain owing the resignation of concerned former Director Vizard and has resisted any prospect of nominating persons not on the current Board to provide its shareholders real choice.

**Evidence that other bodies in the industry were concerned, including WAG member Mr. Wally Merriman.**

The Australian Association of Stud Merino Breeders President Wal Merriman in a letter to WoolProducers dated 28<sup>th</sup> June 2002 stated:

“With reference to media statement... we wish to advise that as a supporter of Dr. Andrew vizard at the last election this Association is also disappointed with his resignation. In light of the strong vote of support, which he received at that election, we did expect him to be re-elected to his position quite comfortably. Press reports are our only source of information as to Andrew’s reasons for retiring, but we have to agree that the process appeared unwieldy and complicated.”...

Nick Burton Taylor quote – The Weekly Times July 3<sup>rd</sup> – “Mr Burton Taylor is Chair of the Major Woolgrowers Group. He said that he was disappointed Dr Vizard’s technical and production experience had been lost to the Board. ‘When a director resigns because of a principle, it sends an early warning signal that things are not right’, he said.”

## 4.2 Resignation of Director John Patten

4.2.1 WoolProducers sought advice from Ms McCaskill as to the reasons for the resignation of Director Patten, as well as the manner in which the vacancy so created was filled. Director Don Nelson was removed from the Board of The Woolmark Company (TWC) to fill the vacancy on the AWI Board.

4.2.2 In a meeting between Mr Dorber, WoolProducers President Simon Campbell and Executive Director Sharon Turner, Dorber said in regard to the Patten / Nelson swap issue that AWI had "too many financial skills on the Board" therefore they let Patten go to TWC who was lacking. They in turn gave up Nelson to AWI who added skills in the fibre processing area to the AWI Board.  
- Simon Campbell raised that Mr Rod Price had said prior to the AGM of AWS in 2001, that the reason for the IWS Board rejecting nominations of appropriately skilled persons onto the ballot paper to place in front of growers at the 2001 AGM was because the Boards' skills were adequate, and Directors needed a chance to work together. Mr Dorber said the Boards were adequate at the time but 'things change' and they needed to do the swap to even out the skills-set. These responses did not appear logical or consistent to WoolProducers.

4.2.3 Growers have had a reasonable expectation that the Board of AWI would keep them as well informed as if they were shareholders and the company was publicly listed. However, in relation to the elections at the AGM last year the Board has:

- Failed to accept nominations from industry onto the ballot papers for the 2001 and subsequently the 2002 election
- Failed to immediately inform "shareholders" when the 2001 election was subsequently found to be (effectively) invalid for AWI Directors in March '02
- Failed to communicate to shareholders the problem and the effect of the consequences of this non-election to AWI which included the fact that the appointed Chair of the AWI Board (and longest-serving unelected Director) was not going to be presented for election.

## 4.3 Directorship / Chair of AWI project - Shear Express

4.3.1 WoolProducers expressed to AWI and the Commonwealth (letter to Mr. Dorber dated Feb 2002), considerable concern that the Managing Director of AWI assumed the Chair of the Board for the Company's 'Shear Express' project. WoolProducers were of the view that this project could only be properly conducted and objectively reviewed if AWI as the investing party was at arms length from the Board or management of Shear Express. Contestability was greatly compromised for growers and other groups working in the wool harvesting field, as AWI's proposed

'dual' role immediately offered Shear Express a more favourable position than other research or commercial applicants.

- 4.3.2 WoolProducers believed it was inappropriate for AWI subsidiaries to be formed out of AWI projects that would financially benefit a Director of that Company by way of Directors fees. WoolProducers requested that AWI remove Mr Col Dorber as the Chair of Shear Express for the reasons noted above, however this request was refused by Mr Col Dorber.

It was never properly established if Mr Dorber received Directors fees for this position. If there had been a payment, it would contradict the statement to shareholders made in the AWI 2002 Annual Report (Refer Attachment S) which states,

“Directors Interest:

During the reporting period there were no transactions between any of the Company’s directors or director related entities and the company and its associated entities...”

It would also contradict a verbal report from a NSWF conference February 7<sup>th</sup> 2002 which Mr Dorber addressed and where he stated (in part of a response to a question) that he would receive no remuneration from Shear Express as Chairman, as it was allowed for in his salary package as MD of AWI. He also noted that he saw no conflict in the subsidiary company setup.

#### 4.4 Skills of the Board

- 4.4.1 The McCaskill Board failed to ensure necessary independent skills were present in the Board of Directors and only sought to address skills shortages identified by WoolProducers in the lead up to the 2002 election of Directors.

- 4.4.2 Since commencement however, and particularly since the resignation of some Directors, there appeared to be insufficient skills available in the then-current Board of AWI. Boards must have adequate knowledge of the company business internal to the Board so that they can effect judgement independent of management.

- 4.4.3 WoolProducers and many growers believed the McCaskill Board had inadequate representation of skills in the areas of:

1. Wool research and development
2. Wool Education and extension
3. Wool Textile Processing, Manufacturing and product development
4. Wool production for market segments
5. Wool marketing (along entire value chain)
6. Testing and Certification
7. Trade policy and Market access

8. Geographical and Climatic Understanding of Wool Production areas within Australia
  9. Understanding of the Ecological and Sustainability Issues as they relate to Wool production
- 4.4.4 The McCaskill Board appointed Professor Alan Trounson in July 2002 to address criticism over the skills base of the Board particularly since the departure of Dr Vizard. Despite some early formal wool-related training Professor Trounson could not alone adequately address the list of necessary wool industry skills, particularly production skills.
- 4.4.5 Woolaby Director Peter Sykes was appointed in August 2002. He likewise failed to address most production-oriented criteria for necessary skills.
- 4.4.6 A fundamental duty of Directors of any Company is to ensure that there are adequate skills amongst the Directors to attend to the business of the Company, independent of management. WoolProducers believe the McCaskill Board failed to do this and as such breached their obligation to shareholders to provide a Board with skills relevant to the Company's objectives.

#### 4.5 Pre-election 2002

WoolProducers concerns regarding the lack of corporate governance, acts of obstruction performed by the Board and funding of agri-political activity, reached new peaks in the lead up to the 2002 Board election. Our experience in assisting shareholders to nominate candidates was a litany of delays, non-replies and obstructive behaviour by the incumbent Board and Managing Director.

The period referred to in further detail below relates to events occurring in the pre-election period, June to November 2002.

- 4.5.1 The Boards obstructive behaviour was most obvious to shareholders throughout their attempt to refuse external nominations for the AWI Board elections, as AWS had also done in 2001. This was to be the second year running that the Board chose not to allow alternate nominations to be placed on the ballot paper. The Board was therefore to remain constituted solely by Government appointees, or the appointees of the Government appointed directors. Since the Goulburn vote of no-confidence, woolgrowers had not had one serious opportunity to elect their Board free from Government appointments.
- 4.5.2 Any representation that the Board of Government appointees was ratified by shareholders is potentially misleading if it does not refer to the fact that the appointees refused to allow external candidates to stand with them for election in the 2001 vote.
- 4.5.2 To address the serious nature of corporate governance, dubious expenditure and the lacking skills base of the McCaskill Board, WoolProducers fielded a group of five people headed by the Hon Ian

McLachlan, to nominate for election to the Board. WoolProducers believed these candidates could offer shareholders more skills, more focus on the role of a market-failure R & D Company, improved governance and improved standards for strategic investment if elected, but most importantly provide shareholders with a choice free of Government appointees.

- 4.5.3 By way of background, the AWI Constitution states that the incumbent Board may determine the rules and procedure governing the election of Directors, and that the Board's decision on the application of the rules is final. WoolProducers identified that it would be necessary to obtain the rules and procedures governing this process immediately if shareholders were to be afforded the chance to vote for external candidates. There was concern that late disclosure of these rules would severely limit shareholder participation in the AGM election process. WoolProducers strongly advocated that shareholders must be allowed sufficient time to involve themselves in the nomination and election process if they so choose.
- 4.5.4 WoolProducers and its member organisations and shareholder members, wrote to the AWI Company Secretary, Mr David Lewis beginning July 4, to request details of the rules and procedures that would govern the nomination and election process. The Company refused to release the rules for more than five weeks after the original shareholder request, which only left shareholders only a further five weeks to the deadline for nominations, to comply with the rules by obtaining 1,830 (5% of shareholders) signatures to nominate an alternate candidate. The Company Secretary then failed to clarify a number of shareholder queries made also at the beginning of July in relation to nomination, election and resolution matters, citing that they were 'self explanatory' or 'in the constitution'.
- 4.5.5 By way of background, the AWI Constitution states that a person is eligible for election to the office of Director if:

*Clause 13.3c(ii)(A-C) states:*

- the person is nominated by the Board onto the ballot paper; or
- the person's nomination is accepted by the Board for placing on the ballot paper; or
- the person must be placed on the ballot paper if he or she is nominated by five percent (5%) in number of the shareholders.

- 4.5.3 For the 2002 AGM, the Board deemed 5% of shareholders to be 1,830. Therefore unless shareholders were to succeed in gathering 1,830 signatures (with the correct Shareholder Reference Number and Address) the AWI Directors effectively had a permanent veto on all external candidates to the Board. The general convention for a Corporations Law Company is no more than 100 shareholder signatures to nominate. The rules were also made as difficult as possible. Shareholders were unable to put five nominee names on one form, consequently the number of signatures to be collected in total became 1,830 multiplied by five, which equate to 9,150 signatures.

- 4.5.4 WoolProducers, and the McLachlan team of candidates, wrote to AWI Chair, Ms. Maree McCaskill, to request that the Board exercise its power under the AWI Constitution Clause 13.3c(ii)(A-C) noted above, to accept the nominations of the five alternate McLachlan candidates for election without requiring the collection of 1,830 shareholder signatures.
- 4.5.5 Ms McCaskill said the Board would consider this request on September 16, only three days before the closing date for nominations on the 19<sup>th</sup> September. That left potentially only three days for shareholders to gather 1,830 signatures for each alternate candidate to nominate of the Board refused to accept the nominations without that requirement.
- WoolProducers found this type of behaviour to be consistent with shareholders perception that the McCaskill Board would do all that they could to keep the Board a 'closed shop' and stifle shareholder involvement in the election process. This behaviour denied shareholders their basic democratic right as (compulsory) shareholders to choose their Company's Directors.
- 4.5.6 The Board never did reply as to whether they would accept the alternate candidates to the ballot paper without collecting the signatures. On the 16<sup>th</sup> September, after flying media into Sydney for the announcement, Mr Col Dorber told press (WT 18/09/02) that no announcements would be made until after the close of nominations on September 19<sup>th</sup>.
- Trish Murphy stated at the AWI AGM that "... the decision was never made. The discussion was never had. The names arrived before we discussed it as a Board" (see Attachment Z, page 90). Therefore, the Board never considered the request.
- 4.5.7 WoolProducers were aware action was required well before the deadline of September 19, and were able to overcome for shareholders this very difficult and obstructive process by obtaining in excess of 12,000 signatures to ensure that all growers had a choice at the 2002 election. The cost to woolgrowers and their representative organisations to do this is estimated at ≈\$45,000.
- 4.5.8 There is no doubt that the McCaskill Board, including Managing Director Colin Dorber, were not simply conducting an election, as is normal business process, it is our view that they were actively campaigning and seeking to influence the opinion of its levy payers at the time of a Board election. In our view, this constitutes agri-political activity and a most serious breach of the Agreement.
- 4.5.9 To make matters more political, AWI issued a press release on 25<sup>th</sup> September 2002, titled: "Government supports AWI approach to candidate endorsement."

An article in The Land Newspaper entitled:  
"Truss backs AWI Signature Chase" appeared on September 19, 2002.

The article read:

*“Federal Agriculture Minister Warren Truss, has defended Australian Wool Innovation Ltd’s right to force board challengers to complete the arduous task of collecting more than 1,800 signatures for their nomination.*

*Mr Truss, who oversaw the drafting of the new company’s constitution during its formation, said the Board was within its rights to ask challengers to present signatures from more than five percent of shareholders, even though it is one of the most onerous systems in corporate Australia.*

*“At the time the new structure was put in place a deliberate decision was made by the industry to make it hard for challengers to overthrow the incumbent board because there was a perception the industry was suffering an inability to attract quality directors due to almost annual coups”, he said. “If growers now thought the system was too restrictive, they should pressure the Company to change its constitution,” he said. “It is their Company and they make the rules. If they want to change them they can change them.”*

WoolProducers expressed their concern to senior staff in the Ministers office that the Minister was being perceived to be endorsing the McCaskill Board and Dorber.

A statement was then released by Minister Truss on September 24 which read:

*“The Federal Government does not have a role in the choice of members of the Australian Wool Innovation (AWI) board,” said Minister Truss.*

*“My comments in the Land, should not be interpreted as supporting any particular candidates for the AWI Board,” he said.*

*“Nor should the comments be seen as either supportive or critical of the board’s actions requiring candidates to secure signatures to validate their nomination.*

*I was simply explaining the matter of fact that the AWI Constitution includes a provision... ..to collect 5% of shareholders. Whether or not the Board decides to enforce this provision, or use its power to accept nominations without the signature requirement, is a matter entirely for the Board. It is not a matter on which it is appropriate for the Government to have a view.*

*The new arrangements establishing AWI were designed to put the wool industry’s research arm in the hands of woolgrowers. It is the woolgrowers’ company, so they make the rules and can change them as provided for in their constitution.”*

In a subsequent interview on September 24 with ABC radio presenter Robin McConchie, to the question: “Are you disappointed at all that your comments have been used by AWI to say that you support their process?” Minister Truss replied:

“Well, I was trying to provide constructive information about what the process was and how it came to be put in place. Not to make any kind of observation on whether or not the power has been used wisely by the Board or not. And that is entirely a matter of judgement for the shareholders.”

4.5.10 In our view, the incumbent Board’s acts were designed solely to protect their respective positions on the board. As such, it is our opinion that they failed to exercise their powers in good faith and in the best interests of the Company, as required by sections 181 and 184 of the Corporations Act 2001. In our view, the Board engaged in conduct oppressive and unfairly prejudicial to shareholders that sought to nominate alternate directors for election to the Board of AWI.

#### 4.6 Performance measurement

4.6.1 To satisfy that funds have been applied consistently with the intent and obligations outlined in the Agreement, proper quantitative assessment of performance measurement is required.

4.6.2 The Board failed to report progress on any strategic plan developed. No meaningful report was provided to shareholders after 20 months which detailed how much money has been spent in what sectors of the value chain on what projects by dollar amount or percentage.

## 5.0 Accountability

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In WoolProducer's view, from the outset of the Ministerially approved and appointed Board, the Board was not equipped with important late value chain-skills, and was weak in the area of on-farm production, with only one member equipped with these skills, and only one Director with a sound working knowledge of corporate financial skills.

The resignation of two Directors, Dr. Vizard (who presented skills as a wool producer, and wool industry veterinarian, researcher, extension and information specialist, and academic with demonstrated capability in research evaluation) and Mr. John Patten (who had substantiated corporate governance and accountability skills) left the Board without effective skills or competence in these areas. It should be noted that both persons privately, and indeed for Dr. Vizard publicly, resignations by these two Directors were stated to be the direct result of concerns about corporate governance and/or accountability in the Company.

Mr. Patten was the Chair of the Finance and Audit Committee of the Board at the time that he resigned.

Subsequent Board appointments either could not be demonstrated to add value in these areas (Nelson appointment) or were extremely late additions that appeared to be tactically made both under pressure from industry (such as WoolProducers) and in the short timeframe before the AGM. The AGM we have noted elsewhere in this report was a process whose management was in itself extremely questionable. From the outset the Board did not demonstrate a good grasp of some fundamental corporate responsibilities and acts. The Board did not engage in any of the following sound and conventional business practices. It did not:

- define early and clearly a strategic plan for the Company to address the funders and beneficiaries requirements
- define the position of MD (and which form) with a proper position description before the search and appointment, with that position description matching the skills defined in the business plan, and
- engage in the widest possible search for the person with those skills that were required and defined
- engage in or demonstrate a rigorous and methodical evaluation process against selection criteria, by the Board, involving Directors directly, to arrive at the final candidate.

Having appointed in an inexplicably and apparently cavalier manner a Managing Director, the Board then ultimately (at some point after the resignations of Vizard and Patten) charged the Managing Director with enormous financial responsibility. The Board established that the MD need only return to the Board for approvals for expenses in excess of \$2million. To examine the absurdity of this, with an annual spend of ≈\$70million, an MD in this position at AWI could in fact spend the entire company budget within 35 projects.

This is an extraordinary decision, which in effect committed the evolution of the culture and direction of the brand-new organisation into the hands of one individual.

The Board is ultimately responsible both for its own collective and individual Director's actions, and also responsible for all of the actions of its MD, delegated or not. The results of this abrogation of so many key Board Director functions are clearly and devastatingly laid out in the McLachlan midyear report to AWI shareholders (Attachment X).

## 6.0 Conclusion

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### Conclusion

WoolProducers believe that several lessons can be drawn from this experience.

- 1) The process of establishing new structures for R&D post-Goulburn in this industry came close to failure, potentially with very significant impact on future R&D in the wool industry. This appears to be the consequence of multiple factors, including:
  - a) poor initial appointments
  - b) It is unclear by what process and criteria the MD of AWI was appointed.
  - c) a Constitution for AWI and AWS that is extraordinarily defensive and almost precludes the presentation of competitive candidates for Board Director elections, and
  - d) the collective failure by the first appointed Board to proactively and vigorously provide and pursue appropriate systems of control and reporting of key staff, (in particular the MD), and
  - e) failure to guide and provide for the early establishment of proper internal financial controls.
- 2) We believe that the Senate inquiry will reveal past problems of considerable magnitude, but will also find that the new Board of AWI elected in October 2002 appears to have addressed and managed and provided solutions for each discovery that they have made of poor management and governance. Available evidence in the public domain suggests they have done this professionally and properly.
- 3) The maintenance of an independent watchdog or agent (the role that WoolProducers fulfills) prepared to pursue accountability is essential in this new industry structure into the future.

It is our opinion that probably only the Senate Inquiry can establish the actuality, magnitude and implications of any errors and determinations by the Company AWI, whether under the Board Chairmanship of Price, or subsequent to May 2001, Chairperson McCaskill, or under the management of Mr Colin Dorber.

## 7.0 Actions

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Actions to address issues raised are suggested as:

- I. The importance of regular, honest, meaningful open reporting, and constructive dialogue with levy payers by the R&D organisation and Board on key strategic objectives and changes will be essential in the future to re-create the necessary trust in the now-reformed process.
- II. The Statutory Funding Agreement for AWI (SFA) as it stands is probably an adequate safeguard for government investment, providing it is monitored in a timely, efficient and responsive way. In our view it would be counterproductive to engage in more complex and constricting legislation or regulation. It is unlikely that there will be found to be fundamental flaws in the SFA. There may well be implications however for the efficiency and manner in which government fulfils its evaluation and monitoring roles against the SFA.
- III. The AWI Constitution: while WoolProducers understand that the new Board is currently planning changes at the AGM in 2003 to deliver a result to shareholders, the point requires reinforcing that the Constitution of AWI must be rendered effective as soon as possible. This process will enable more open shareholder participation, and encourage continuous review of AWI's performance
- IV. Similarly AWS (holding company for the Woolmark Company) should immediately promote Constitutional change along similar lines to ensure that similar problems cannot occur in this important Company.

## 8.0 Attachments

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- Attachment A* – Table 1: Governing Documents  
– Table 2: Potential Breaches of the Statutory Funding Agreement
- Attachment B* – AWI press release January 4, 2002 – “Wool to actively support UK design awards”
- Attachment C* – WoolProducers correspondence to Minister Truss, February 2002
- Attachment D* – WoolPoll Voter Information Kit (copy)– pages 10 & 11
- Attachment E* – AWI press release 28<sup>th</sup> January 2002 – “National Woodlots Advisory Service to add further value for wool
- Attachment F* – AWI press release 18 February 2002 – “What’s in a name – woodlot gets the chop.”
- Attachment G* – Transcript from Alan Jones program 24<sup>th</sup> October, 2002 – Interview with Mr Colin Dorber announcing the donation
- Attachment H* – Transcript from Jeff Kennet radio program – Interview with Red Cross on the return of the AWI funds
- Attachment I* – Weekly Times article November 27, 2002 – “Drought cash reclaimed.”
- Attachment J* – Weekly Times article, December 4, 2002 - “Donation legality in doubt.”
- Attachment K* – Paid advertisement in The Land newspaper, 17 October, 2002
- Attachment L* – Paid advertisement in various Rural Press publications – 16 – 17 October, 2002
- Attachment M* – Weekly Times article, September 25<sup>th</sup>, 2002
- Attachment N* – Ian McLachlan speech to NSW Farm Writers’ Association, 28 March, 2003-06-07
- Attachment O* – Farm Weekly article, August 22, 2002.
- Attachment P* – Weekly Times article April 2, 2003, - “Audit cans AWI contract process”.
- Attachment Q* – Queensland Country Life article April 3, 2003 – “Board cleans up AWI mess”.

*Attachment R* – Queensland Country Life article, March 6, 2003 – “Ousted directors still on AWI payroll”

*Attachment S* – AWI 2002 Annual Report, copy – page 32

*Attachment T* – Weekly Times article 19<sup>th</sup> February 2003 – “Final deal for AWI Execs”.

*Attachment U* – Weekly Times article, 26 June 2002 – “Vizard tells: Why I quit”

*Attachment V* – Weekly Times article, 16 October, 2002 – “Can of worms – Leaked letter slams AWI Board”

*Attachment W* – A copy of ‘Moving Towards the Knowledge Economy Conference’ Brochure.

*Attachment X* – A copy of the McLachlan Letter to AWI Shareholders dated 11<sup>th</sup> June 2003

*Attachment Y* – A copy of an article entitled “ Chief’s colourful history” The Weekly Times, March 2001

*Attachment Z* – Transcript of the Australian Wool Innovation AGM held on 31 October 2002 at Hay NSW

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