



Corporate Governance in New Zealand

Consultation on Issues and Principles

*To be read in conjunction with the
Background Reference Paper*

Securities Commission
September 2003

Q U E S T I O N N A I R E

Background

The Securities Commission has been charged with leading a process through which consensus can be gauged for a set of principles for Corporate Governance in New Zealand.

The Commission has initiated the development of a background paper that builds on the work that has been undertaken in this area, both within New Zealand and internationally. The paper has been distributed as a companion document to this questionnaire.

The Consultation Process

The consultation process has been developed to enable the Securities Commission to identify the level of consensus within New Zealand around:

1. What a set of **governance principles** should encompass
2. The **range of issues** that need to be reflected in the principles
3. The **range of entities** to which the governance principles should apply.

The Commission has used external advisers to develop the Background Reference Paper and the Questionnaire that underpin the consultation process. Both the Questionnaire and Background Reference Paper have been subject to rigorous peer review.

1. The Principles

Based on the review of local and international perspectives and practices, nine core issue areas have been identified (see page four).

Using the feedback obtained through this consultation practices, overarching principles will be crafted in relation to each of the nine issue areas – eg Ethical Conduct, Board Committees, Shareholder Relations etc.

For the principles to be **relevant** to the range of entities that operate within the New Zealand business environment and **effective** in guiding decision making processes and behaviours, it is important to identify the range of issues that each principle might encompass, what people think about these issues and the extent to which they might apply to different entities.

2. The Issues

While there is consensus in some areas about the issues that the governance principles should address, there are also a number of issues around which opinion is divided.

Based on the review of local and international material, a series of propositions have been developed to enable the Securities Commission to gauge the depth and range of opinion around governance practices to establish the norms of behaviour that the principles should inform.

If the propositions appear to suggest a rules based approach, this is neither the intention of the Commission nor the mandate that the Commission has been given.

The Securities Commission is interested in assessing the extent to which there is consensus around specific issues to inform the development of a set of principles.

3. Range of Entities

The focus overseas has been primarily on the governance of publicly listed companies. In this consultation process, views are being sought about the extent to which governance principles should apply to a wider range of entities including:

- subsidiaries of overseas companies
- supplier or purchaser owned cooperatives
- widely held unlisted companies
- government and local authority owned entities
- closely held or family owned companies
- large trusts

4. The Outcomes

The consultation process has been developed to enable the Commission to present the Minister of Commerce with a set of Corporate Governance Principles, around which there is broad based consensus in New Zealand. If there are areas where there is a clear lack of consensus, then these will be acknowledged.

The Securities Commission, in undertaking this exercise, has not been mandated to develop rules or regulations or recommend legislative change or remedies with respect to these Corporate Governance Principles.

The Commission is concerned to ensure that the report of findings resulting from this exercise that is presented to the Minister builds on the considerable body of work that has already been undertaken in New Zealand and that the Principles are broadly aligned with both international and local developments in this area.

The Commission has undertaken to report to the Minister before the end of December.

5. The Next Steps

The consultation process is open to all interested parties.

To enable the Securities Commission to present the findings of this process to the Minister by the end of December, the Commission has set a deadline for submissions of **5pm Friday November 7**.

Submissions should be made using the questionnaire – an electronic version of which is available on the Securities Commission website (see below). This may be more useful if the replies require more space than provided in the printed version of the questionnaire.

The project has been designed for qualitative rather than quantitative analysis. This means that responses will neither be analysed nor tabulated in percentage terms, but considered in relation to the level of agreement around the key issues or themes that the findings suggest.

Please note that the comments provided in the questionnaire will not be attributed to individuals or organisations.

A set of principles will be drafted based on the response to the questionnaire. If you are interested in being kept informed about the process, please tick the appropriate box in the questionnaire and make sure that you provide your email and/or postal details.

Additional copies of the Background Reference Paper and Questionnaire are available on the Securities Commission website – www.sec-com.govt.nz

Thank you for your assistance.

The Issues

Nine main issue areas have been defined:

1. **Ethical Conduct** – including the use of codes of ethics
2. **Board Composition and Performance** – including the role and definition of independent directors and the issues of certification/accreditation
3. **Board Committees** – including composition of committees
4. **Reporting and Disclosure** – including quarterly reporting and the certification of financial statements
5. **Remuneration** – of executives and directors
6. **Risk Management** – including levels of disclosure
7. **Auditors** – including rotation and oversight
8. **Shareholder Relations** – including institutional shareholders, public reporting
9. **Stakeholder Interests** – addressing the interests of stakeholders

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Completing the Questionnaire

For each issue area a series of propositions have been developed to elicit where and why there is agreement/disagreement in relation to core issues.

We are seeking your perspective on the opinions/advice/practices posed in each area, and your rationale for agreement or disagreement with the propositions.

Space has been provided at the end of each section to enable you to raise any additional issues that you consider to be relevant to the debate.

An electronic version of this questionnaire is available on www.sec-com.govt.nz which will enable more extensive responses.

Issue One: Ethical Conduct

Refer Background Reference Paper page 9

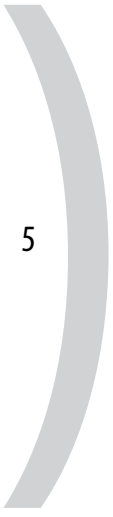
1. There is a view that companies should have formal Codes of Ethics or Conduct to guide the actions of Board and Management, as well as other staff. To what extent do you agree with this?

2. It is also said that such Codes of Ethics or Conduct should be published. What is your view?

3. Codes of Ethics may address various issues, including issues of integrity the use of company assets, conflicts of interest and confidentiality. What issues do you think it is most important for such Codes to include?

4. What do you consider the appropriate responses – both internal and external to the company – where such a Code has been breached?

5. If you have any other comments on **Ethical Conduct** in relation to Corporate Governance, please include these below.



Issue Two: Board Composition and Performance

Refer Background Reference Paper page 10-11

1. There is debate around the definition of an 'independent director'. Drawing on work undertaken in New Zealand and Australia, one definition is:

"Someone who is not an executive and who has no business or other relationship that could compromise – or could reasonably be seen to compromise – the ability to exercise their unfettered judgment. Such business or other relationships include being a substantial shareholder (or its representative), a material customer, supplier or professional advisor to the company"

- a. Do you believe the elements included in this definition are appropriate for the New Zealand environment?

- b. If not, are there any other elements that should be considered?

2. Some commentators on Corporate Governance suggest independent directors should make up the majority of a Board. To what extent do you agree with this?

3. In what situations (if any) do you believe that it might not be appropriate for a Board to include a majority of independent directors?

4. There is a view that a Chair and CEO should not be the same person. To what extent do you agree with this view?

5. What is your view on the suggestion that a CEO should not go on to become Chair?

6. Do you agree or disagree with the proposition that a company's Chief Executive should automatically be a member of the Board?

7. What factors do you believe should be considered in determining Board size and do you think it is feasible to define an optimal size?

8. How regularly should Boards review their own performance?

9. It has been suggested that Boards should also review the performance of individual directors. Do you agree or disagree?

10. In general, do you believe current mechanisms which enable shareholders to assess the performance of Boards/directors are adequate? If not, how would you suggest these be improved?



11. Some commentators suggest that certification or accreditation of directors should be encouraged. What is your view on this?

12. What processes do you believe Boards should have in place to ensure:

a. that suitable directors are recruited?

b. that directors remain fit to perform the role for which they are appointed (through, for example, induction, training and other professional development)?

13. If you have any other comments on **Board Composition and Performance** in relation to Corporate Governance, please include these below.

Issue Three: Board Committees

Refer Background Reference Paper page 12

1. There is debate concerning whether by establishing board committees, and assigning responsibilities to them, Boards can function more effectively. What do you see as the benefits and/or drawbacks of Board committees in the New Zealand environment?

2. In the United States, United Kingdom and Australia all public companies are required to establish board audit committees with formal responsibilities for appointing and overseeing external auditors. Would you consider this appropriate in the New Zealand context?

3. In the US, UK and Australia, audit committees are required to include a majority of independent directors and an independent Chair. Again, would you consider this appropriate in the New Zealand context?

4. It is often a requirement for audit committees to have at least one member with financial expertise. What (other) capabilities or credentials do you believe ought to be reflected within the membership of an audit committee?

5. International opinion suggests that Boards above a certain size should delegate responsibility for director and executive remuneration to a board remuneration committee. To what extent would you consider this appropriate in New Zealand?

6. International opinion also favours the establishment of appointment committees with delegated responsibility for recruitment and appointment of new directors and executives. To what extent would you consider this appropriate in New Zealand?

7. Do you agree with the view that independent directors should make up the majority on remuneration and appointment committees?

8. And, do you agree or disagree with the view that audit and remuneration committees should comprise of different people – i.e. that no director should sit on both?

9. If you have any other comments in relation to **Board Committees** in relation to Corporate Governance, please include these below.

Issue Four: Reporting and Disclosure

Refer Background Reference Paper page 13

1. Continuous disclosure has been a requirement for publicly listed companies in New Zealand since December 2002. In relation to good Corporate Governance, are there any areas or matters on which you believe additional disclosure should be encouraged?

2. In regard to unlisted companies, do you believe there is a need for greater emphasis on timely, accurate and complete disclosure?

3. There has been debate in New Zealand around whether listed companies should report quarterly, as required on some US markets. What is your view?

4. It is a requirement in some markets for the company CEO and CFO to publicly certify the accuracy and completeness of financial statements. Do you think this is appropriate in the New Zealand market?

5. What other safeguards do you see for ensuring integrity in reporting practices and outcomes?

6. What is your perspective on the proposition that companies should report on their performance against accepted principles of good Corporate Governance, or explain why they haven't?

7. If you have any other comments on **Reporting and Disclosure** in relation to Corporate Governance, please include these below.

Issue Five: Remuneration

Refer Background Reference Paper page 14-15

1. Internationally, there is a trend to explicitly link directors' remuneration with company performance. To what extent do you think this should be the case in New Zealand?

2. Do you agree that, in New Zealand, non executive directors' remuneration is currently set at a level to attract and retain individuals who will make a significant contribution to company performance?

3. Do you believe there are any circumstances in which it might be appropriate for non-executive directors to receive retirement payments?

4. Do you agree with the view that at least part of a non executive director's remuneration should be 'at risk' on the basis of company performance?

5. There is some debate around non executive and executive directors being paid in company shares.

a. Do you believe it is appropriate for a proportion of directors' remuneration to be paid in shares or in options in the company's shares?



b. If so, should this be expensed against company earnings?

6. Some commentators warn that linking executive and directors' remuneration to company performance over one or two years can create a "short-term" bias in thinking. To what extent do you think this is an issue in New Zealand today?

7. There is an argument that the remuneration terms of a CEO's contract and those of senior management including any termination payments should be disclosed to shareholders. To what extent do you agree with this view?

8. There is a view that executive remuneration should be directly subject to shareholder approval. Under what circumstances, if any, would you consider this appropriate in New Zealand?

9. If you have any other comments on **Remuneration** in relation to Corporate Governance, please include these below.

Issue Six: Risk Management

Refer Background Reference Paper page 16

1. Adequate identification and management of risk is considered to be integral to good Corporate Governance. To what extent do you believe New Zealand Boards are adequately addressing this issue today?

2. It is suggested that companies should develop risk management policies and procedures.

- a. What would you consider appropriate for such risk management policies and procedures to encompass (for example, financial, market, operational, environmental risk, delegation of authorities and succession planning)?

- b. And do you believe that these risk management policies and procedures should be published?

3. If you have any other comments on **Risk Management** in relation to Corporate Governance, please include these below.

Issue Seven: Auditors

Refer Background Reference Paper page 17

1. There is international debate about whether audit **firms** should be rotated from time to time.

a. To what extent do you consider rotation appropriate in the New Zealand context?

b. If appropriate: How often should audit **firms** be rotated?

2. There is also debate suggesting that audit **partners** should be rotated from time to time.

a. To what extent do you consider this appropriate in the New Zealand context?

b. If appropriate, how often should audit partners be rotated?

3. There are concerns over audit firms also providing other services to client companies.

a. In your view, what types of non-audit work should be of concern in the New Zealand context (e.g. valuation services, executive recruitment)?

b. Do you think disclosure of fees paid to audit firms should differentiate between types of non-audit work?

c. Do you think the total of non-audit work should be limited to some proportion of all fees paid to audit firms each year and, if so, what proportion?

4. It has been argued that board and/or board audit committees should develop and disclose policies for handling complaints by auditors or internal “whistleblowers”. Do you agree or disagree?

5. In the U.S. and Australia, audit oversight bodies – independent of the profession – are required. There is debate around whether such a body is required in New Zealand. What are your views on this?

6. If you have any other comments on **Auditors** in relation to Corporate Governance please include these below.



Issue Eight: Shareholder Relations

Refer Background Reference Paper page 18

1. In your view, how well do companies in New Zealand encourage meaningful dialogue between the Board, management and shareholders?

2. Auditors are required to attend Annual Meetings and some commentators suggest that companies should facilitate shareholder access to auditors. Do you agree or disagree?

3. There is a view that relations with institutional shareholders are of particular importance and that these shareholders should always participate in voting on shareholder resolutions. Do you support this view?

4. Do you agree that listed companies should publish a formal policy on their relations with shareholders?

5. In your view, how well do you think listed companies in New Zealand provide shareholders with comprehensive and easily understood commentary on their financial performance?

6. In your view, should other business entities – such as co-operatives, large trusts, and unlisted companies – provide more comprehensive public reporting on their performance?

7. If you have any other comments on **Shareholder Relations** in relation to Corporate Governance, please include these below.

Issue Nine: Stakeholder Interests

Refer Background Reference Paper page 19

1. Some people argue that, while shareholders have the primary interest, there are other stakeholders with legitimate interests that should be considered in the context of Corporate Governance. To what extent do you agree with this view?

2. It has been suggested that the interests of these other stakeholders should be actively considered by the Board.

a. Do you think this is appropriate in the New Zealand context?

b. If so, how should these interests be addressed?

3. If you have any other comments on **Stakeholder Interests** in relation to Corporate Governance, please include these below.

Other Issues

1. New Zealand opinion appears to favour a principles versus rules-based approach to Corporate Governance. Do you believe this is the most appropriate approach for New Zealand?

2. Do you think the nine issue areas that have been identified in the Background Reference Paper and this Questionnaire are the core issues that should be included in the New Zealand principles for Corporate Governance?

3. Are there any other issues you believe a set of principles for good Corporate Governance in New Zealand should address?

About You

Your response to the following questions will help us to understand how the views gathered during this consultation process vary across business entities.

1. Are you responding in a personal capacity or on behalf of an entity?

In a personal capacity

On behalf of an entity or organisation

2. If responding on behalf of an entity, please clarify:

a. The **name and/or type** of entity on whose behalf you are responding (e.g. publicly listed company, unlisted company, State Owned Enterprise, cooperative, industry association, privately held company etc.).

b. Your **position** within this entity (e.g. CEO, CFO, Chair, independent director, executive director, non-executive director etc.).

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Official Information Act and Privacy Act Requirements

The contents of the questionnaires provided to the Securities Commission in response to the consultation process are subject to the provisions of the Official Information Act 1982 and the Privacy Act 1993. It is the Commission's policy to make responses to formal consultation available for public inspection. Please confirm below whether you consent to the release of your submission. Any requests for information will be dealt with in accordance with the Official Information Act 1982 and the Privacy Act 1993.

Yes No

In case we need to contact you for further clarification on points raised in your response, please include your contact details below.

NAME: _____

BUSINESS PH: _____

BUSINESS EMAIL: _____

Would you like to be kept informed about the process? Yes No

Please return completed questionnaire by 5pm November 7 to:

Postal: Securities Commission
Corporate Governance Project
PO Box 1179
Wellington
email: Julie.Myers@sec-com.govt.nz