Welcome to the latest edition of Across the Board – KPMG’s newsletter focused on the key issues facing Non-Executive Directors.

In this edition, we feature the key messages from the recent KPMG sponsored ‘International Trends in Corporate Governance’ forum at the Company Directors Conference Directorship:14 and the impacts of the ASX Corporate Governance Principles & Recommendations on financial and diversity reporting. We also share useful tips on taking the complexity and clutter out of financial reports and highlights from the recent CeBIT conference on combating cyber threats.

We hope you find this edition of Across the Board of interest. If you would like to discuss any featured articles in more detail, please contact me or your local KPMG partner.

Peter Nash
National Chairman,
KPMG Australia

For feedback on Across the Board please contact us.
Company director issues from around the world

A KPMG sponsored forum at the Company Directors Conference
Directorship: 14, Igniting the growth agenda

In May 2014, over 400 directors gathered in Hamilton Island at the Company Directors Conference. With ‘Igniting the growth agenda’ as the theme, the directors discussed the challenges and opportunities for organisational and economic growth.

A key part of the conference was a KPMG Australia-sponsored forum on International Trends in Corporate Governance. Hosted by Chris Hall, KPMG National Managing Partner, Risk & Regulation, the forum included an influential panel of Australian and international business leaders who shared their insights into the current and emerging trends in corporate governance and the issues facing directors across different jurisdictions worldwide.

Moderated by Rob Elliott FAICD, General Manager, Policy and General Counsel, Australian Institute of Company Directors, the panellists included:

- Stan Magidson
  President and CEO, Institute of Corporate Directors, Canada
  Global Network of Director Institutes (GNDI)
- Dr Bandid Nijathaworn
  Secretary to the board of directors, president and CEO, Thai Institute of Directors.
  Global Network of Director Institutes (GNDI)
- Ansie Ramalho
  CEO, Institute of Directors, Southern Africa
  Global Network of Director Institutes (GNDI)
- Dr William Whittaker
  CEO, Institute of Directors, New Zealand
  Global Network of Director Institutes (GNDI)
- John H C Colvin
  CEO and managing director, Australian Institute of Company Directors.
  Chair of the Global Network of Director Institutes (GNDI)
- Dr Roger Barker
  Director of corporate governance and professional standards, Institute of Directors, UK
  Global Network of Director Institutes (GNDI)

As Chris Hall noted, “the forum wasn’t just a great opportunity for the audience to hear first-hand from such a distinguished panel with different perspectives and experience, but engage in discussion about the opportunities and key challenges that corporate governance presents for Australian businesses.”

Of particular interest for Australian company directors was the opportunity to understand the ‘hot topics’ for company directors around the globe.

South Africa
Hot topics: board diversity and Integrated Reporting

Ansie Ramalho explained to forum participants the Institute of Directors in Southern Africa (IoDSA) does not support board quotas in relation to diversity, holding the view that while they may deliver the numbers, these do not necessarily translate into quality. Rather, their approach has been to create career pathways and a pipeline of qualified directors through their Director Charter (SAI which aims to give boards confidence around competency and enable directors from more diverse backgrounds to be considered for board appointments.

General concern was expressed that the pressure to appoint female directors has an impact on quality, but it is the view of director institutes that boards need to look harder and in different places for talented women. As one director commented at the forum, “there is a tendency when looking for a NED to look to CEOs or senior executives, and there aren’t a lot of women in those roles. Boards need to be more imaginative and look for people from other backgrounds”.

The move to Integrated Reporting is another hot topic in South Africa. As with Australia, there is concern that traditional reporting is no longer ‘fit for purpose’. The IoDSA is looking at the ‘six capitals’ model identified by the International Integrated Reporting Committee which, in addition to the traditional financial and manufactured capital, focuses on societal, human, intellectual and environmental capital.

Canada
Hot topics: director engagement with shareholders; short-termism; proxy firms and shareholder activism

A primary consideration for directors is Canada is how businesses engage with their shareholders.

There’s no doubt, as noted in the forum, that effective communication with stakeholders, including activist shareholders, is becoming increasingly important for directors.

Stan Magidson detailed a recent case study in Canada concerning activist shareholders in which the court determined directors owe their primary duty to the corporation and they should have regard for all stakeholders when making decisions and no single stakeholder has primacy. The court also determined that directors should look to the long-term and the business judgement rule was upheld.

In Canada, it is anticipated this ruling will give directors greater confidence in communicating the company’s long term strategy to the market.

The general view of the forum panelists was that, where activist investors are seeking to affect change to the company’s strategy, the board should focus on the strategy itself – “do all the work that activists would have done for you so there is nothing left for the activists to do”.

The increasing influence of proxy advisers is also of concern for directors in Canada. In contrast to the requirements of shareholder issuers and their directors who must comply with a number of regulations regarding shareholder communication, proxy advisers are not currently held to any standard when it comes to their shareholder communications.

Concern was also expressed about potential conflicts of interest. In Canada, the Institute of Corporate Directors (ICD) is calling for full disclosure of regulations regarding shareholder issuers and their directors communications.

Stan Magidson is of the view that “there are no regulations regarding shareholder activism which, in contrast to the requirements of activist shareholders, is currently not held to any standard when it comes to their communications.

In contrast to the requirements of shareholder issuers and their directors who must comply with a number of regulations regarding shareholder communication, proxy advisers are not currently held to any standard when it comes to their shareholder communications.

United Kingdom
Hot topics: role of controlling shareholders in corporate governance

Dr Roger Barker told the forum the UK’s Institute of Directors (IoD) is currently undertaking a review of dominant shareholder conflicts with minority shareholders for those organisations

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Company director issues from around the world (continued)

listed on London Stock Exchange, with some recent examples creating stress for individual boards and the UK’s corporate governance model.

As a result, the UK has adopted a new governance model, with new rules insisting on relationship agreements being put in place to control the majority shareholder and allow minority shareholders to have their own election procedures for independent directors.

This issue is expected to become more prevalent as more family-run businesses from emerging markets seek to list on stock exchanges in developed nations.

New Zealand
Hot topics: changing role of NEDs; compliance and conformance; performance of boards and directors

A shift towards improving board performance and self-regulation is leading towards increased professionalism for directors in New Zealand.

Similar to South Africa, the Institute of Directors in New Zealand (IoDNZ) is developing a director charter, along with a requirement for its members to undertake continued professional development.

The panelists noted a number of suggestions have also been put forward in the UK to address director performance, including limiting the number of boards directors can join, a minimum requirement in terms of the number of days committed to an organisation each year, introducing full time directors on boards. Professional development also remains a key area of focus.

One option discussed by the panel at the forum was that directorships evolve to a ‘fully-fledged’ profession with a professional standards committee.

It is anticipated these ‘hot topics’ in New Zealand will remain central for company directors in jurisdictions across the globe.

Thailand
Hot topics: Corruption and bribery

In Thailand, new legislation is being developed to introduce a stricter definition of corruption with an expectation that, once in force, companies will be expected to comply and take action to eliminate corruption.

Boards will be required to be better informed on the requirements of anti-corruption legislation and understand the steps their company is taking to comply with the requirements. As Dr Bandit Njathaworn explained, “clean business is a choice that the board can make and must make to set a very clear tone from the top as to how the company is to operate.”

Australia
Hot topic: education

John Colvin put to the forum that director education is an essential complement to director experience and background and is key to getting directors to focus on the right issues.

In Australia, there is no formal requirement for director education; however, the ASX adopts the ‘if not, why not’ approach to continuous development. This contrasts with both Malaysia and Spain, where directors of financial institutions must have recognised forms of training, a requirement which will also soon be introduced in Italy.

In Hong Kong, directors are also required to undertake continuous professional development.

In January 2013, the Australian Institute of Company Directors (AICD) extended its compulsory Director Professional Development (DPD) requirements to all members.

The topic of international governance was well received by the delegates at this year’s Directorship: 14 conference, with the KPMG sponsored sessions at capacity on both days. As Chris Hall commented, “KPMG is delighted with the quality of conversation at this year’s Company Directors Directorship: 14 conference at Hamilton Island and, in particular, the quality of presenters and level of interest in our sponsored forum on international governance.”

“The forum wasn’t just a great opportunity for the audience to hear first-hand from such a distinguished panel with different perspectives and experience, but engage in discussion about the opportunities and key challenges that corporate governance presents for Australian businesses.”

– Chris Hall
The journey to better business reporting continues

**Revised ASX Corporate Governance Principles and Recommendations**

In March 2014 the ASX Corporate Governance Council introduced the third edition of its ASX Corporate Governance Principles and Recommendations. The revised Principles and Recommendations came into effect for Australian listed public companies from 1 July of this year. They are more evolutionary than revolutionary and are unlikely to result in any massive shift in the way boards think about governance issues. They do however contain several new elements that could trip up unwary boards.

For example, throughout the new document the term ‘financial reporting’ is replaced by the words ‘corporate reporting’. This seemingly innocuous change actually helps elevate reporting to an important governance issue in its own right. In addition, the Principles and Recommendations make it clear that boards and their audit committees are responsible for ensuring that their companies possess processes for independently verifying and safeguarding the integrity of corporate reporting.

Although the Principles and Recommendations do not define ‘corporate reporting’, we think their intent can be satisfied by adoption of the Integrated Reporting Framework, supported by the financial report, and anticipate the change will hasten its adoption. Defining the corporate reporting portfolio is a matter for individual boards to determine for their own organisation.

Integrated Reporting responds to demands for more insight into how businesses create and sustain value and that, in turn, will allow more informed capital allocation decisions. It should allow investors to look beyond transitory, short-term performance fluctuations.

We believe Integrated Reporting can also prompt fresh thinking, innovation and better decision making within reporting entities, better aligning their internal and external reporting with stakeholder concerns, including those of long-term investors. Integrated Reporting may not free companies from the tyranny of quarterly, half-yearly and annual reporting cycles and the corresponding emphasis on short-term performance metrics, but it certainly promises to make the reporting process more meaningful and productive in both internal and external contexts.

Companies can prepare an integrated report today within its Operating & Financial Review (OFR) under current law, and a number of leading Australian companies are already using this approach. Others are applying the Integrated Reporting Framework in preparing annual reviews published outside of their annual reports. Demand is growing from users and preparers for change, and we believe that this may in time, if the required groundswell develops, lead to the ASX Corporate Governance Council’s Principles and Recommendations being updated to recommend on an ‘apply or explain’ basis preparation of an integrated report.

In the meantime, boards could use this time to familiarise themselves with the revised governance guidelines and consider the implications of Integrated Reporting for their own organisations. As a start we recommend that boards reveal the components of their corporate reporting portfolios in their annual corporate governance statements, explaining how directors oversaw the integrity of the portfolio. In this context it is worth remembering that much of the volume and complexity of today’s corporate reporting does not actually reflect the formal requirements of mandated reporting practices. Boards still enjoy considerable freedom in their ability to reduce reporting volume and complexity while enhancing clarity and disclosing better information about business models, strategies, performance, risks and prospects.

Boards can consider taking advantage of the more evolutionary character of the revised Principles and Recommendations for listed entities to publish much of their corporate governance statements on their corporate websites rather than in their annual reports. Material on websites can provide more detail on standing data, specific frameworks and charters.

More generally they could use the revision of the Principles and Recommendations to reduce the volume and complexity of their current voluntary reporting as well as in their legislated and regulated reporting, closely reviewing the application of materiality requirements and taking a fresh look at the clarity and flow of existing reports.

We understand that resolving the issue of director liability is a prerequisite in allowing more forward looking material to be included in corporate reporting and to encourage the full application of the Integrated Reporting framework. The Federal Government has already been approached to legislate an “honest and reasonable” director defence for individual director liability and to consider a “safe harbour” protection for companies using their best endeavours to make forward looking disclosures with appropriate cautionary wording.

In summary, we believe that the revision of the corporate governance Principles and Recommendations, particularly Principle 4, is an ideal opportunity for the ASX Corporate Governance Council, and indeed for Australia, to lead corporate reporting reform.
We’ve all been there. You have read up to note 26 on page 140 of the financial report, your eyes are glazed over, and you are finding it hard to differentiate between what’s important and what’s not. And why does the content and the structure of the financial report bear no relationship to the messaging contained in the front of the annual report regarding financial performance and KPIs?

These frustrations have been the catalyst for companies to take the complexity and clutter out of financial reports by removing immaterial or duplicated disclosures built up over time, re-ordering notes and putting complex disclosure wording into plain English. Initially a financial reporting trend coming out of the United Kingdom, Australia is also now tackling the challenge of making financial reports less complex and better aligned to other information released to the market.

What do the regulators say?

The call for less complexity in financial reports has been supported in recent times by both regulators and accounting standard setters. The Financial Reporting Council in the United Kingdom, SEC in the United States and International Accounting Standards Board have all publicly endorsed the benefits of focussing on material disclosures and de-cluttering in order to improve financial report quality.

How do I go about de-cluttering the financial report?

The process of de-cluttering a financial report involves three key steps:

**Step 1** – Remove disclosures that are immaterial or duplicated. Many financial reports have picked up boiler-plate disclosures over time that are not relevant or material to the overall financial report and can be removed without compromising compliance with regulatory requirements.

**Step 2** – Re-order and group disclosures into sections so that it better links to the front of the annual report. For example, notes could be grouped so that they better explain current year financial performance, how the balance sheet is funded, off-balance sheet exposures, and other less significant disclosures.

**Step 3** – Re-write complex disclosures in plain English.

The key to success

Companies which have undertaken this process highlight the need for strong stakeholder engagement across the finance team, investor relations, audit committee and relevant external users in order to gain support and manage expectations. Your KPMG contact can also play a key role in helping to assess the updated financial report against accounting standard requirements.

Whilst for some it may take a ‘leap of faith’ to embrace the de-cluttering process, the end product should be a clearer and more focussed document that will better tell your story.
Getting on board with cyber and digital security

The fight against cyber threats

On May 5, 2014 at the annual CeBIT conference in Sydney, KPMG hosted three major corporates on a panel discussion about one of the biggest challenges organisations face today: Making sure the board understands and endorses the right measures to combat cyber threats.

Digitally organised crime. Zero day attacks. Cyber crime declared a potential Black Swan event. Cyber threats are growing in ferocity and volume, posing the biggest challenge to businesses navigating the complexities of the 21st century.

“Risk indices now show that managing cyber threats has moved from a No. 20 priority in 2009 to a top three risk,” comments Mark Tims, Partner at KPMG.

The good news is that C-level executives and the board are far more informed about cyber security than ever before. “Boards are demanding more from management in terms of information about threats and seeking a real understanding of how to deal with such threats. The days are long gone when IT professionals struggled to be heard at board level,” notes Tims.

Nonetheless, all large complex organisations face continuously changing business dynamics, a drive towards greater innovation and pressure to do more with less. “Most CISOs face the challenges of providing a greater and better response to cyber threats and calibrating more capabilities with less budget,” comments Tims. This means creating powerful engagement with the board is more important than ever.

For Troy Braban, Chief Information Security Officer, Australia Post, engagement begins and ends with aligning the cyber discussion to business strategy. “We take a strategic approach to information security, the focus for which is protecting our trusted brand. Our governance framework means regular contact with the board, monthly reports and a range of forums at senior leadership level to discuss how to enable the business and manage risk.”

Greg Baster, CIO at GPT, found that board engagement increased when the business undertook a major operational shift from a compliance framework for cyber and security into the cloud via Amazon Web Services and Microsoft. “High profile media attention on security has helped the conversation, which is no longer a matter of simple compliance to a broader and far more proactive view on both cyber and security and their role across the business.”

Speaking their language

Keeping a board engaged in positive discussion can be challenging, particularly when the talk turns technical. David Fisher, Global Head of Technology Risk & Information Security, ANZ, emphasizes that using the right form of communication is crucial to getting the buy-in you need. The key is summarising the issues and solutions in a way that’s real and personal to the board member. “We have to learn to use less technical language and make the discussion more relevant to their language,” he notes.

“We focus on how we are enabling the business,” says Australia Post’s Braban. “We stick to their key principles: Make it fact-based, be tangible and use examples to illustrate and make it relevant.”

Ultimately all IT and Information Security leaders need to agree with the board the business risk appetite and how information security will be managed. Notes Fisher “The commercial imperative is important to keep front and centre.”

Trickling down

While engaging the board is critical, it’s equally important to ensure cyber security is heard and understood throughout the organisation. “Full organisational awareness is an important requirement to fighting cyber threats,” notes KPMG’s Tims.

Says ANZ’s Fisher: “There’s no single method. You have to understand the right timing and how to tailor the message to the audience so the content is appropriate.”

Australia Post and ANZ both have a dedicated awareness team that works with external and internal communications and media teams to engage internal stakeholders and consumers.

Meanwhile, GPT is in the process of establishing a multi-tiered approach to security awareness. “Security is always built into our onboarding process – it almost ‘dovetails’ in with physical security. We’re now developing a more detailed audience and channel specific approach to communicating on this issue,” notes Baster.
Progress on gender diversity continues

ASX Corporate Governance Principles and Recommendations on diversity

With more employment opportunities and higher rates of education, Australian women are today stamping their (il)gender in the workforce, having almost doubled their participation in the labour force over the last 50 years.1

However, it has taken time to get here and involved a re-adjustment in how people think. Today, the importance of women in the workforce, especially in senior roles, is well established. Not only is gender equality and diversity in the workplace seen as both ‘fair’ and the ‘right thing to do’, but essential for business health and growth.

Business may be embracing a diverse workforce however there are still areas that can be improved. Women, for example, may make up more than 50 percent of the workforce but, as noted in a 2012 census by the Australian Government’s Workplace Gender Equality Agency, while there has been a recent acceleration of women on ASX200 boards, the progress for women in executive ranks since 2002 has been negligible.2

This raises the very real question of whether corporations are doing enough to encourage and reward women in the workplace. Corporate cultures and mindsets – more so than individual factors – still determine what a woman can achieve.

It is encouraging, then, to see that changing such cultural environments and resetting mindsets through true diversity policies has become a clear objective of corporate Australia. With more employment opportunities and higher rates of education, Australian women are today stamping their (a)gender in the workforce, having almost doubled their participation in the labour force over the last 50 years.2

The Board and Executive Committee can ensure the effectiveness of their diversity strategies with actions like:
- unlocking the power of data to manage their talent pipeline
- being authentic if it is a strategically critical priority
- being accountable for any corporate commitments
- encouraging responsibility for delivering change at all levels in their organisation.

‘What gets measured gets done’ may only be partly true on this issue but, nevertheless, it is a critical path to getting change. There are more similarities than differences between men and women at work. So there should be little difference in career outcomes for men and for women. Given that we continue to see significant difference in career paths, organisations could make a difference by providing more targeted support to women on:
- long range career navigation
- building a strategic portfolio of experience
- conveying Board-readiness.

Not only is gender equality and diversity in the workplace seen as both ‘fair’ and the ‘right thing to do’, but essential for business health and growth.

Diversity rules

This effort to change how listed corporations approach diversity has been championed by the ASX Corporate Governance Council (CGC), which, in 2010 introduced changes to its Corporate Governance Principles and Recommendations on the reporting of diversity.

Recommendation 1.5 requires a listed entity to establish a diversity policy with measurable objectives to assess gender diversity set by the board or a committee. All entities across the ASX have now had two reporting seasons to respond to these changes. The CGC recommendations on diversity require companies to disclose, on an ‘if not, why not’ basis, whether they have established a diversity policy, the measurable objectives they have set for achieving gender diversity and the progress towards achieving such objectives, as well as the number of women at various levels of the company.
Progress on gender diversity continues (Continued)

For a second successive year, the ASX commissioned KPMG to conduct an independent analysis of the diversity disclosures made by listed companies. The results, published in the ASX Corporate Governance Council Principles and Recommendations on Diversity 2014 report, are encouraging. Importantly, there is a clear acceptance of the benefits of a diversity policy, and ASX listed entities are increasingly realising and reporting on the benefits of having a diverse workforce. Among 600 companies, the report found a high level of compliance, and within ASX200 companies, 98 percent had a diversity policy. Another recent study also showed that women now comprise 28 percent of new appointments to ASX200 boards. However, in ASX201-500 and ASX501+ companies, the percentage of organisations with a diversity policy dropped off to 85 percent and 66 percent respectively. The most common reasons for not following the “if not, why not?” Diversity Recommendations were that an entity was in the process of adoption or, for smaller entities, the entity size or stage of development made adoption impractical. However, while overall compliance to the diversity policy was high, the report shows that measurable objectives have not been adopted to the same extent, and their quality is also variable.

ASX200 companies that set “measurable objectives” were 86 percent compliant. But, again, for smaller companies, the numbers dropped off. In the ASX201 – 500 group, 56 percent had set measurable objectives, while only 29 percent had for ASX501+ companies. We expect that those companies which set measurable objectives of a more qualitative, and less quantitative, nature are likely to find it difficult to show progress against those objectives in coming years. It is also likely that investors will be looking more closely at the type of objectives that have been set and the company’s progress in achieving those objectives. In relation to gender metrics, more entities have provided clear definitions and explanations of terms, such as women in ‘senior executive’ positions, although disclosure around metrics did vary significantly. One thing was beyond doubt. Companies that were transparent and detailed in disclosing their metrics were able to communicate their commitment to diversity more powerfully than companies that provided minimal detail. This sends a strong message to stakeholders and the market. The results show an improvement in the level of reporting and disclosure from the previous year. However, many organisations still have a long way to go in terms of establishing clear and measurable objectives and working towards improving the number of women at all levels across the organisation. It is nevertheless evident that progress towards gender equality is happening.

Companies that were transparent and detailed in disclosing their metrics were able to communicate their commitment to diversity more powerfully than companies that provided minimal detail.

Further Information

ACI Roundtable Insights

Our latest issue includes highlights of the ACI Roundtable Series 1, held across Australia in April and May, 2014. This first roundtable series of the year focused on the priorities and future trends for audit committees based on the findings from our 2014 Global Audit Committee Survey.

Click to read the discussion summary, with a focus on equipping internal audit to deal with emerging risks, and to view previous discussion summaries.

Directors Toolkit

To support directors in their challenging role KPMG has created The Directors’ Toolkit. This guide, in a user-friendly electronic format, empowers directors to more effectively discharge their duties and responsibilities while improving board performance and decision-making.

Key topics

- Duties and responsibilities of a director
- Oversight of strategy and governance
- Managing shareholder and stakeholder expectations
- Structuring an effective board and sub-committees
- Enabling key executive appointments
- Managing productive meetings
- Better practice terms of reference, charters and agendas
- Establishing new boards.