



Australian Council of Super Investors Inc.

CORPORATE CITIZENSHIP NEWSLETTER

May 2006 : Issue No.24

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ACSI ANNUAL CONFERENCE

“Bridging the Expectations Gap!”

The fifth annual ACSI Conference will take place on **Friday 16 June 2006** at the Arthur Streeton Auditorium, Hotel Sofitel, Collins Street Melbourne.

The theme of the conference reflects the fact that shareholders increasingly expect more from boards as to how they should protect their interest. These expectations will increase as superannuation funds assets under management continue to grow. Boards also have expectations about shareholders. Many still assume that they know what shareholders want or should want from the company and directors.

ACSI's fifth annual Conference aims to challenge all shareholders, Boards, executives, and institutional investors to narrow the gap of each other's expectations.

Attendance at this Conference will count for 3 Continuing Professional Development (CPD) for AIST's Member Accreditation Program.

ACSI members (trustees, their boards, fund executives and staff) attend the conference for **FREE**.

If you haven't received a registration form visit www.acsi.org.au and go to the Conference page and download the form.

REGISTRATIONS CLOSE 9 JUNE 2006.

FOREIGN CO'S BACK IN THE AUSSIE INDEX

Now that the dust has settled after News Corp has been removed from the ASX/S&P 200 the ASX and S&P have come full circle and are considering including foreign domiciled companies into their indices.

As a result of including foreign-domiciled entities in S&P/ASX indices, it would be necessary for the S&P/ASX Index Series to operate independently of S&P's global index suite. Such a change in policy will result in the S&P/ASX 50 index being removed from the Global 1200 index suite. Consequently, S&P/ASX have issued a consultation paper which also introduces a "pure" S&P Australia & New Zealand 50 Index (SPANZ 50) for the Global 1200.

Michael O'Sullivan, President of ACSI warned in a recent AFR article¹ that the US based S&P did not have the interests of Australian shareholders at heart when making global decisions. "We would be happier with the ASX running its own index rather than outsourcing it to a foreign company and being subject to its decisions." He went on to say that if the S&P must manage the index, the least it could achieve for investors was consistency. He said back flips on index composition had cost investors money, because funds were forced to sell – not on the basis of making investors money, but because of index changes. While many funds would have to buy back what they sold last year in the case of News Corp, the situation was better than excluding stocks with a foreign domicile.

"If (these companies) have a strong following in Australia, it's appropriate that they are indexed. There was no profound reason for removing them in the first place." he said.

Summary of proposals

Foreign secondary listings will be considered for inclusion in the S&P/ASX indices where:

- The company is not a foreign-exempt listing;
- A company must have a broad spread of shareholdings through the Australian market-Australian Registered

Shareholders (ARS) must be greater than 300 (by number), with no dominant shareholders, for example no greater than 33% of ARS.

- The company will be evaluated for index inclusion on the basis of its ARS, both for the purposes of assessing market capitalisation and measuring liquidity;
- Index capitalisation (and index weight) will be the lower of the free float capitalisation, or the minimum ARS capitalisation in the previous six months;
- The company will be allocated to S&P/ASX size indices on the basis of full equity capital (not adjusted market capitalisation) to capture the true risk/return profile of the company;
- The index treatment of foreign secondary listings currently included in the S&P/ASX indices will be grandfathered; and
- The All Ordinaries index will continue to be constructed, comprised of the S&P/ASX 300 plus an additional 200 domestic stocks based on market capitalisation.

The consultation closes on 14 June 2006. The consultation paper can be found at

http://www2.standardandpoors.com/spf/pdf/index/20060518_ForeignDomicileCompanies.pdf

NAB – TRYING TO EASE THE PAIN!

The AFR has reported that the National Australia Bank is preparing an ambitious legal action to recover more than \$500 million from two global currency broking houses for their alleged role in the bank's rogue-trading affair.²

¹ 'ASX backflip on index sparks a fear of foreigners', AFR, 30 May 2006.

² 'Rogue trading: NAB chases \$500m from forex firms', AFR, 29 May 2006

Late last week the last two former foreign currency traders responsible for the scandal were convicted. The close of the criminal trial gives NAB the green light to pursue Cantor Fitzgerald spin-off BGC International and ICAP for their alleged roles.

As per the AFR article it is understood that the bank has given the broking houses until this week to respond to a demand for \$539 million in compensation.

David Bullen, was found guilty of 18 out of 20 charges and Vincent Ficarra, 27, was found guilty of all 13 charges for their roles in the scandal. Both men were remanded in custody and will appear at a pre-sentencing hearing next month.

PROPOSED CHANGE TO THE BUSINESS JUDGEMENT RULE

On 7 April 2006, Treasury released a consultation paper 'Corporate and Financial Services Regulation Review'. Comments on the paper closed on 19 May 2006. The consultation paper focused on the following areas:

- further refinements to FSR;
- company reporting obligations;
- auditor independence;
- corporate governance;
- fundraising;
- takeovers;
- collective investments;
- dealing with regulators.

The only area of concern that ACSI had related to the extension of the Business Judgement Rule.

ACSI has queried why there has not been a proper canvassing of the potential and relevant issues relating to the Business Judgement Rule, through a detailed discussion paper. There also appears to be some overlap on this issue and the matters that were recently considered at a Joint

Parliamentary Committee Hearing with respect to duties of directors.

ACSI has registered its concern with respect to the potential extension of the business judgement rule.

For a copy of the consultation paper visit <http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=1068>

2005 ANALYSIS OF CORPORATE GOVERNANCE PRACTICE DISCLOSURE

On 22 May 2006 the ASX Corporate Governance Council released '2005 Analysis of corporate governance practice disclosure'. This report presents an analysis of corporate governance disclosure and compliance by listed companies with ASX Listing Rules for the 2005 reporting period. It also provides commentary on the trends in disclosure and adoption-reporting levels of various Recommendations between the 2004 and 2005 reporting periods as identified in the recent review of 2005 annual reports.

The ASX review of disclosures in 2005 annual reports showed:

- The overall reporting level for all Recommendations has increased to 88% from 84% in 2004.
- 14 out of 28 Recommendations had reporting levels over 90%
- An additional 9 out of 28 Recommendations had reporting levels over 80%
- This compares with the 2004 review where 8 out of 28 Recommendations had reporting levels over 90% and an additional 9 out of 28 Recommendations had reporting levels over 80%
- The overall reporting level increased at a faster rate among companies outside the Top 500.

- The adoption reporting level for all Recommendations increased to 74% from 68%

The review found that companies have improved reporting on their practices in a number of areas:

- Recommendation 3.1: Establish a code of conduct – the reporting level increased to 90% in 2005 from 78% in 2004, an increase of 12%
- Recommendation 5.1 - Establish policies and procedures to ensure compliance with the Listing Rules – the reporting level increased to 92% in 2005 from 79% in 2004, an increase of 13%
- Recommendation 6.1- Design and disclose a strategy for communicating with shareholders and encouraging participation at meetings – the reporting level increased to 91% in 2005 from 82% in 2004, an increase of 9%
- Recommendation 8.1 – Disclose the process for board and executive performance evaluation – the reporting level increased to 85% in 2005 from 73% in 2004, an increase of 12%.

The ASX also found that there continues to be a strong 'if not, why not' exception reporting level in relation to:

- Recommendation 2.1 - A majority of the board should be independent directors, an 'if not, why not' exception reporting level of 47%
- Recommendation 2.4 - The board should establish a nomination committee, an 'if not, why not' exception reporting level of 57%.

The complete report can be found at http://www.asx.com.au/about/pdf/corporate_governance_2005_disclosure.pdf

ASX COUNCIL POST IMPLEMENTATION REVIEW RESULTS

On 6 March 2006 the ASX Corporate Governance Council released key findings of a survey aimed at understanding the relevance of corporate governance to the investment and analyst community.

The key findings covered the following areas

- Usage of Corporate Governance information
- Sources of Corporate Governance information
- Decisions based on Corporate Governance information
- Focus on annual reports

The findings will assist the Council to improve the usability of the information reported by companies. To promote the "if not, why not" principles and improve the flow of information for investors and shareholders.

The survey can be found at http://www.asx.com.au/supervision/pdf/asx_corporate_governance_summary_march06.pdf

CHAIRMAN OF THE BOARD – A ROLE IN THE SPOTLIGHT,

The Australian Institute of Company Directors (AICD), released 'Chairman of the Board – A Role in the Spotlight' on 21 April 2006. The publication details how chairs approach their task of board leadership, with advice and personal insights from Coca Cola Amatil's David Gonski, Australia Post's Linda Nicholls and former Telstra Deputy Chairman John Ralph.

The publication provides chairmen's views on building partnerships with chief executive officers, improving company performance

from the boardroom, the qualities of chairmen who make a difference, communicating with shareholders, and why the role does not suit everyone.

The aim of this work is twofold: it provides an overview of chairmanship as practised in Australia today and it touches on current issues that are shaping the way in which chairmanship is evolving in Australia.

Order forms for the publication can be found at

<http://www.companydirectors.com.au/Bookshop/Book+Categories/Chairman+of+the+Board+A+Role+in+the+Spotlight.htm>

GREAVES RULING DOESN'T LET DIRECTORS OFF THE HOOK

Interestingly on 30 May 2006 the AFR³ included a letter from Jeffrey Lucy, Chairman, ASIC regarding the impact that the NSW Supreme Court Ruling has in relation to the responsibilities of not just chairman but also other directors.

Mr Lucy highlighted that the NSW Supreme Court Ruling found that Mr Greaves, former Chairman of One-Tel had extra responsibility because of his position. However, this finding should not mean that fellow non-executive directors will not be culpable in the event of corporate failure.

The letter went on to state that "Directors, whether executive or non-executive, who fail to perform their duties should take no comfort from the premise that if a chairman is found to have breached his duty, it somehow lets other directors off the hook. All directors have the responsibility to be probing and diligent. Good corporate governance demands this responsibility to be taken very seriously."

³ 'Misguided take on Greaves ruling', AFR, 30 May 2006

PROPOSED AUDITOR ROTATION POLICY

ASIC has recently sought comment on a new policy proposal paper regarding ASIC's power to give relief from the auditor rotation obligations in the Corporations Act 2001 (the Act).

Auditor rotation is part of the auditor independence requirements introduced into the Act by the Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004 (CLERP 9). The auditor rotation obligations will apply to an audit for a financial year that begins on or after 1 July 2006.

The issues raised in the paper include:

- the expectation that auditors will undertake a self-assessment of eligibility;
- how ASIC expect to be notified of any contraventions;
- when ASIC consider that the auditor rotation obligations will create an unreasonable burden justifying some relief; and
- what ASIC expect to see in an application for relief from the auditor rotation obligations.

For a copy of the consultation document visit http://www.asic.gov.au/asic/asic_pub.nsf/byheadline/IR+06-11+ASIC+seeks+comments+on+proposed+auditor+rotation+policy?openDocument

NEW PRUDENTIAL GOVERNANCE STANDARDS

On 5 May 2006 APRA released new prudential standards on governance for authorised deposit-taking institutions and for life and general insurance companies. The new standards have been developed after industry consultation. The new standards

build on existing requirements in two main ways:

- they seek to promote greater independence on the part of the board, its chair and the board audit committee; and
- they require boards to have a formal policy on board renewal and procedures for assessing their own performance.

For more information visit http://www.apra.gov.au/media-releases/06_26.cfm

ENVIRONMENT, SUSTAINABILITY AND GOVERNANCE ISSUE A CORE FIDUCIARY DUTY

The UN Secretary General Kofi Annan recently marked the start of an historic partnership between the global investment community and the **United Nations** by launching the Principles for Responsible Investment (PRI). These were also launched in Europe in Paris recently.

The initiative represents the first time mainstream funds have jointly labelled analysis of environmental, social and governance (ESG) issues as material to investment risk and part of core fiduciary duties for long-term value. A number of commentators are suggesting that the PRI could become a central pillar of institutional investment, triggering global changes in money management, brokerage and corporate behaviour.

There have been endorsements from 33 funds in 16 markets speaking for US\$2.4 trillion in assets. The Paris launch will reportedly usher in another 18 first-round signatories, including big Japanese money managers, bringing total money behind PRI to more than US\$3 trillion.

Framed as six pledges with 35 action options, the PRI says signatories will now:

1. *Incorporate ESG into portfolio analysis and trading.* Expect funds to press brokers to do ESG homework.
2. *Step up shareowner activism on ESG issues.* With engagement branded a routine responsibility, expect more of it on issues such as climate change.
3. *Call on corporates for more ESG disclosure.*
4. *Ensure investment service providers address ESG.* Expect funds to insist that financial service providers demonstrate capacity to offer ESG analysis.
5. *Work collectively to implement the PRI.*
6. *Disclose to beneficiaries how they bring ESG concerns into share ownership operations.*

Work on the PRI opened a year ago when Annan asked the **UN Environment Programme Finance Initiative** and the **UN Global Compact** to probe shareowner appetite for guidelines promoting responsible investment. The agencies convened a two-track drafting process involving 20 funds and 70 experts, meeting in Paris, New York, Toronto, London and Boston. Ceres, the environmental coalition, and **Mercer Investment Consulting** were key advisors; France's **Caisse des Dépôts** was the main outside underwriter.

Signatory funds have recently opened talks on next steps. **Among plans: a compact PRI secretariat to coordinate recruitment of endorsers, information sharing, training, benchmarking of implementation and a website.** Proponents envisage a board dominated by funds, plus UN and independent members. That structure would formalize the unfamiliar alliance between investors and the UN.

A copy of the principles can be found at http://www.unglobalcompact.org/docs/new_events/9.1_news_archives/2006_04_27/pri_brochure.pdf

INTERNATIONAL NEWS

UK Developments

USS' take on Extra-Financial Factors

The Universities Superannuation Scheme Limited published an interesting paper in May titled 'Enhanced Analytics For a New Generation of Investor – How the Investment Industry Can Use Extra-Financial Factors in Investing'. The purpose of the paper is to provoke and stimulate a constructive debate about the use and consideration of extra-financial factors in investing.

The paper can be found at http://www.usshq.co.uk/special_interest_group_index.php?name=special_interest_group_rules_and_finance_corporate_governance&content=ri_enhanced_analytics

Company Law Reform Bill

A press notice was issued on 3 May 2006 in relation to Government amendments to the Company Law Reform Bill laid before Parliament. The developments are part of the UK Government's wish to respond to debates in the House of Lords as well as detailed engagement with interested parties. The measures include changes to: Directors' Duties; Narrative Reporting; and Derivative Claims. As part of the package, the Government will also clarify the position on liability for disclosures under the Companies Act and for implementation of the EU Transparency Obligations Directive.

Two new draft clauses on a proposed regime for liability have been issued for a consultation in relation to the Liability of directors for false and misleading statements in reports and liability for false and misleading statements.

This consultation has now closed and we'll keep you abreast of any further developments. Further details can be found at <http://www.dti.gov.uk/bbf/co-law-reform-bill/index.html>

US Developments

United Health Group being sued for backdating options

The AFR report on Monday 22 May 2006⁴ that the CEO and directors of the second largest US health insurer were being sued for allegedly backdating options. The suit alleges that option grants were backdated with the share price as at a record low.

Options provide recipients with the option to purchase shares at a preset price, known as the exercise or strike price, with the expectation that market prices will rise before the option is exercised, allowing the holder to benefit from the rise in the market price of the stock. The strike price is usually the stock's market price on or close to the day the option is granted.

The US securities regulator is also investigating the stock option programs of several companies and have sought records from Vitesse Semiconductor Corp and at least 10 other companies that may have backdated options.

An ISS study has also found that potential dilution resulting from stock-based incentive plans continues to decline at the largest U.S. companies, while voting opposition to such plans rose markedly in 2005. Investor support for traditional stock plans, while still considerable, was far less strong in 2005 than in past years. In 2005, 17 of approximately 383 stock plan proposals--or 4.4 percent--voted on by shareholders (and tracked in the ISS study) failed to gain shareholder approval. Those 17 companies with failed plans include: **Administaff, Autodesk,**

⁴ 'US health insurer sued for backdating options', AFR, Monday 22 May 2006



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Broadcom, Connetics, Cyberonics, D. R. Horton, ESS Technology, Gallagher (Arthur J.), Hain Celestial, Kulicke & Soffa Industries, Littelfuse, Macrovision, Mesa Air Group, NDCHealth, New Century Financial, RehabCare Group, and Tetra Technologies.

A copy of ISS' 2006 "Stock Plan Dilution" report (along with the underlying data) can be purchased from

<http://www.irc.org/bookstore/specials.htm>

Former Enron Chiefs Convicted

On May 25 2006 former Enron chief executives Kenneth Lay and Jeffrey Skilling were convicted on charges that they lied to investors during the 2001 collapse of what was once was the seventh-largest U.S. company.

"The government's successful prosecution of Kenneth Lay and Jeffrey Skilling is a victory for the shareholders and employees of Enron and the American public,"

"The verdict makes clear that high level corporate executives who deceive the investing public for personal gain will be held fully accountable. The result in the Enron criminal trial is a victory for all Americans, whose jobs and economic security depend on the integrity of our capital markets." said Christopher Cox, chairman of the Securities and Exchange Commission.

A federal judge in Houston has also given approval for a \$6.6 billion securities class action settlements reached by Enron investors with several of the company's former underwriters for alleged assistance in hiding debt to inflate the energy company's earnings.

SEC Announces Next Steps for SOX Implementation

On 17 May 2006 the Securities and Exchange Commission (SEC) announced a series of actions it intends to take to improve the

implementation of the Section 404 internal control requirements of the Sarbanes-Oxley Act of 2002.

In recent months, the Commission has obtained comment from a variety of sources concerning the operation and effects of Section 404.

"The actions the Commission is announcing today represent key steps toward addressing issues raised by participants involved in the critical process of reporting to investors on the effectiveness of companies' internal control over financial reporting," said John White, Director of the Commission's Division of Corporation Finance. "We will be working on our own, and with the PCAOB, to improve the implementation of Section 404 so that it will work efficiently and effectively for companies and auditors of all sizes and types while still maintaining the important investor protections it provides."

Details of the actions the Commission expects to take can be found in the press release at

<http://www.sec.gov/news/press/2006/2006-75.htm>

Board Elections Bill Introduced

On 16 May 2006, legislation was introduced in the Delaware General Assembly that would help investors seek bylaw changes to establish a majority-voting standard in director elections.⁵

The bill is based on recommendations from the Corporate Law Section of the Delaware State Bar Association. The proposed amendments to the Delaware General Corporation Law are noteworthy because a majority of U.S. public companies are incorporated in the state.

The legislation would amend the law to provide that a company bylaw adopted by a vote of stockholders that prescribes a

⁵ ISS Governance Weekly, 26 May 2006



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required vote (e.g., majority) for director elections cannot be altered by the board without shareholder consent.

QWEST Binding Majority Vote Proposal

On 24 May 2006 a binding majority-voting proposal received 53% of votes cast at Qwest Communications International (US' largest telephone company)⁶.

The vote on the bylaw proposal is the highest so far for a binding shareholder resolution in this area. However, the significant support for this resolution was not enough because 80% of Qwest's total outstanding shares were required.

After the vote the CEO said that the board would consider the issue.

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This newsletter is correct to the best of our knowledge and belief at the time of going to press. It is, however, written as a general guide so it is recommended that specific professional advice is sought before any action is taken

⁶ ISS Governance Weekly, 26 May 2006