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SEASONS GREETINGS FROM PHIL



Another busy year is coming to a close: one that has been clearly marked with an increased shareholder focus on environmental, social and well as governance issues that potentially impact on investments.

Also prominent has been the significant reaction from shareholders at general meetings on pay issues, corporate takeovers and management buyouts.

It is clear our individual and collective interest in all these issues is not about to dissipate. We don't believe that this is a fad that will come and go. What continues to be a challenge is matching our concerns on these issues with genuinely applying what we know in order to minimize risks and to find opportunities that will ultimately benefit our super fund members.

As our sector continues to get larger, having clicked just over \$1trillion and growing close to the capitalized value of the ASX, our community will be looking for tangible and meaningful responses to corporate governance challenges. One of these is reinforcing to companies and, in particular company directors, that as long-term investors we are interested in sustained performance and success. We have no interest in behaving or being treated like an obstructionist opposition group perceived to be supporting a narrowly focused approach

to governance that adds little value to a company's long-term prosperity.

At the moment, we are bracing ourselves for the full impact of the US induced credit squeeze on Australian companies. Hindsight is a great thing, but some basic questions will be asked with respect to the risks that boards had identified with respect to the short-term debt financing and whether they were satisfied that appropriate steps had been taken to mitigate these risks.

As to our continued focus on building on a sound governance base, there are still companies and directors who do not quite "get it" when it comes to our interest on these issues. Witness the reaction to a negative shareholder vote on remuneration reports from Telstra, particularly when considering that the company has still got a long way to go on building credibility and enhancing shareholder value.

This will be my final year as executive officer with ACSI. The search is on for a new CEO. As you all know, my association with ACSI will continue on a part-time basis with a slightly different - but no less committed - role. I remain grateful to the support of my colleagues and the Committee of Management who on every measure have been great advocates for ACSI and challenged me to find the best in myself over the last six years. In particular, I would like to thank Michael O' Sullivan, Michael Delaney and Ann Byrne together with my colleagues Ros McKay, Meredith Squires and Chris Panagiotopoulos with whom I have forged a trusted and close working relationship that has ensured that our small yet tight knit group punched 'above its weight'. I look forward to being part of an improved resourced unit going forward.

All the very best for the festive season and may the new year bring good health and prosperity to all of you.

See you in 2008.

NEW ACSI "ESG" GUIDELINES

On 19 November 2007, ACSI launched new guidelines to help superannuation funds consider environmental, social and corporate governance issues in investing.

The Guidelines provide a broad and consistent policy basis for ACSI members to approach ESG issues in investing. They contain a significant amount of the foundational work that ACSI members can build on when adopting and implementing their own ESG policies and practices.

The guidelines also contain:

- suggestions for funds on how to incorporate ESG issues into investment processes and to facilitate the broader and deeper consideration of ESG issues in across the investment industry.
- suggestions for fund managers and asset consultants to assist with the consideration of ESG issues, and outline the expectations that superannuation funds may have of their service providers in the future.
- broad expectations and suggestions for listed companies.
- a brief discussion of some of the key challenges in moving from "ideas to action" in this area.

ACSI anticipates that the guidelines will provide a catalyst for ACSI members to discuss with their fund managers, other service providers and investee companies how all parts of the investment chain can meaningfully consider ESG risks and opportunities in investment decision-making.

Copies have been sent to all member funds. Please contact Meredith Squires, Research Officer, ACSI on (03) 8677 3893 or msquires@acsi.org.au if you would like additional printed copies. Alternatively, a pdf is available from our website.

CLIMATE CHANGE

Invitation to join the sixth Carbon Disclosure Project

The Carbon Disclosure Project (CDP) is currently inviting institutional investors to become signatories to the sixth Carbon Disclosure Project in 2008.

In 2007, 315 investors representing over US\$ 41 trillion of assets under management were signatories to the CDP. Signatories to the CDP collectively seek information on the business risks and opportunities presented by climate change and greenhouse gas emissions data from the world's largest companies. In 2007, information was requested from 2,400 companies, including the ASX100 and NZ50. In 2008, the CDP request will be extended to the ASX200.

The CDP process encourages companies to measure, manage and reduce their emissions, their exposure to carbon risk and their physical climate change risks. Given the increasing importance of climate change as an investor issue, the CDP can provide signatories with access to information that may be useful in investment decision-making processes and engagement. There is no charge to become a signatory investor, and signatory investors have access to all CDP responses, including those that are not made publicly available.

To become a signatory investor, visit the CDP website and fill out the form: <http://www.cdproject.net/howbecomesignvestor.asp?menu=3&submenu=1> and email it to info@cdproject.net by **Friday 18 January 2008**.

For more information, visit the CDP website: www.cdproject.net

Climate Change & Investment

ACSI President Michael O'Sullivan and HESTA CEO Anne-Marie Corboy were invited to a meeting in London on 5-6 November to

discuss the role of pension funds in finding climate change solutions.

The "P8 Summit" – a meeting of large pension fund groups from the US, UK, Sweden, Australia, The Netherlands and the China Investment Corporation - was convened by The Prince of Wales Business and Environment Programme which is centred at Cambridge University.

The meeting received an update from Nobel Laureate, Al Gore, and leading scientist Sir David King (scientific advisor to the UK government), Professor John Schellnhuber (scientific advisor to the German government), Professor Robert Socolow (Princeton), Professor Daniel Kammen (Berkeley), Professor Jorgen Randers (Norway) and a number of others.

The key messages were:

- Global warming is occurring more rapidly than even the IPCC report predicted.
- A considerable shift in investment capital is needed to develop alternative energy, transport, construction and other technologies to reduce greenhouse emissions to a level necessary to limit global warming to an increase of 2°, beyond which the consequences are extreme.

The pension fund response was two fold:

- Pension funds had plenty of available capital to invest in private markets to fund new technology development, but that in most countries – UK, Europe, Scandinavia – there were few investible opportunities presented to the funds. The exception was the US where, despite poor political leadership on climate change, the three large funds at the P8, CALpers, CALsters and New York State Commission, said there were plenty of opportunities and investment had begun.
- Secondly, the pension funds said they could and should step up their

engagement with listed companies to ensure they were managing their climate change risks and opportunities in the most effective way possible.

The other key messages were:

- OECD and developed countries would have to make greater cuts to their emissions than developing countries if there was to be any prospect of holding global warming to 2°.
- A carbon cap and trade system was the essential and only practicable way to drive investment in new technology.

The experts were well aware that a change in government in Australia was likely, bringing Australia into Kyoto and establishing a national cap and trade system into operation by 2010.

You will have seen most of this reinforced by the prelude to, and the course of, the debate at the UN meeting in Bali.

Super Trustees Roundtable

On 23 November, the Climate Institute hosted a roundtable to look at Australian super funds' response to climate change – again both the risks and opportunities.

Michael O'Sullivan attended for ACSI along with members, David Atkin (ESSS) and Tim Hughes (Catholic Super).

Two issues received most attention:

- The design of Australia's carbon cap and trade system will be critical to Australia meeting necessary emission targets.
- It is possible for fund managers to take ESG into account in stock analysis, that it will become standard procedure, and that climate change risks and opportunities will accelerate deeper ESG valuations.

Joanne Saleeba representing the Investor Group on Climate Change, Pauline Vamos,

the new CEO of ASFA and Joseph Sorby, representing IFSA, all expressed a desire to work more closely with ACSI to ensure that super funds spoke with a single voice to government on carbon funding and other issues.

The meeting was valuable because it brought together the super funds' organisations and the ASX, those advising the BCA, actuaries and a number of fund managers seeking common ground.

ACSI will develop the fruits of these two important meetings and provide more information to members in the New Year. Meanwhile, we have established a close collaborative relationship with the Investor Group on Climate Change, which has led to consideration of some joint research on carbon trading.

IGCC Research On Earnings Impacts On Climate Change

The Investor Group on Climate Change recently launched a series of reports entitled Potential Earnings Impacts from Climate Change for Key Australian Sectors. The Reports outline the earnings impacts from climate change with a particular focus on emissions trading for key Australian Sectors: Energy Infrastructure, Steel, Construction Materials and Airport Infrastructure.

The research has been undertaken by Monash Sustainability Enterprises in conjunction with Goldman Sachs JBWere, Hastings Funds Management and Merrill Lynch. Copies of the reports can be downloaded from: www.igcc.org.au

INTERNATIONAL DEVELOPMENTS

US

Pay Consultants Under the Spotlight

A US congressional investigation has found pay consultants who do other work for

companies while helping them devise executive pay recommended significantly higher pay packages than consultants who had no such additional relationships.¹

During 2006, the committee's analysis showed, 179 of the largest 250 companies disclosed hiring at least one of six firms to advise them on executive pay. Of those companies, 113, or 63 percent, paid the same firm to provide other services to the company in 2006, creating the potential for conflicts.

It is also worth noting that 30 of those companies identified their compensation consultant in Securities and Exchange Commission filings as "independent."

For example MetLife described its consultant as independent even though it had paid the firm more than \$7 million for other services. PepsiCo similarly identified its consultant as independent, even though it had paid more than \$6 million for other work.

Interestingly at 25 companies whose pay consultants came from firms that also had lucrative contracts to provide actuarial or employee benefit services, chief executives were paid a median salary of \$12.5 million last year. That was 67 percent higher than the median salary paid by companies that did not use consultants that were potentially biased.

While executive pay levels in Australia are not in the main as egregious as in the US, it would potentially worthwhile undertaking a similar study in Australia.

Proxy access proposals

The U.S. Securities and Exchange Commission (SEC) voted on Wednesday 28 November 2007 to let companies exclude shareholder proposals for director nominations from

¹ New York Times, 'House Committee Finds Conflicts in Executive Pay Consulting', by Gretchen Morgenson, 6 December 2007.

corporate ballots but promised to reopen the issue at a later date.

The 3-1 vote backed the SEC's long-standing interpretation of its proxy access rules, which was cast into doubt by a 2006 federal appeals court decision.

The US still uses the plurality system, in which a single share voting 'yes' can elect an entire board even if every other ballot is marked 'withhold,' the only other option. Majority rule, by contrast, requires any director candidate failing to gain more than 50% 'yes' to resign. Some US companies are introducing majority rule through binding bylaw changes; others by non-binding policy. Some companies empower boards to retain a minority-elected director no matter what the vote.²

In the absence of majority rule and shareholder proposals for director nominations, in the U.S. investors have little say on who governs the companies in which they invest.

Proxy access has long divided investors and business groups. The commission said it received a record 34,000 comment letters on the issue.

Investors say it is their fundamental right as shareholders to be able to nominate board directors.³

SEC Chairman Christopher Cox said he hoped the SEC would revisit the issue in 2008 and work on crafting a rule to permit some access proposals. "Today is not the end, and I hope all stakeholders will continue to work with us," he said. "If we use the time between now and the next proxy season wisely, we can act on a new rule proposal next year

that does more than just perpetuate the status quo."

In an editorial before the SEC vote, the *Financial Times* was sceptical of the argument by U.S. corporate advocates that proxy access might drive some companies to move overseas. "There's a flip side to the competitiveness argument-international investors, too, can go anywhere," the London-based newspaper wrote. "Why would they choose a country where they have fewer rights?"⁴

EU

Draft Acting in Concert Laws in Germany

On 24 October 2007 the German Cabinet approved draft laws that tighten rules on investors 'acting in concert' in a bid to make takeover attempts more transparent.⁵

The draft laws attempt to broaden the definition of shareholders 'acting in concert' in such a way that curtails their ability to sway management. The law expands the definition to include discussions among shareholders before general shareholder meetings and coordinated votes on a single issue. Once found to be 'acting in concert', the shareholders would have to disclose their stakes in the company and, if their combined shareholdings reached 30%, they would be required to make a joint offer to all shareholders.⁶

In ACSI's view, this is a retrograde step in shareholder rights and is not an approach that should be emulated in Australia as it would discourage investors talking to each other.

⁴ RiskMetrics Group 'The SEC Denies Proxy Access' By L. Reed Walton, 30 November 2007.

⁵ FORBES.com 'Germany okays draft law to tighten rules on investors 'acting in concert'
<<http://www.forbes.com/markets/feeds/afx/2007/10/24/afx4255296.html>> at 27 October 2007.

⁶ 'Acting in Concert', *Wall Street Journal Online*, Review and Outlook, 26 October 2007
<<http://online.wsj.com/public/article/SB119334737928272014.html>> at 27 October 2007.

² Global Proxy Watch, 'Landslide' Vol XI No 41, 16 November 2007.

³ Reuters, 'UPDATE 2-US SEC restricts shareholder proxy access', 28 November 2007

<http://www.reuters.com/article/governmentFilingsNews/idUSN2861512520071128?pageNumber=3&virtualBrandChannel=0> at 5 December 2007.



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The ICGN has made a submission on the proposed new law because it is concerned that the proposed law makes no distinction between shareholders discussing normal corporate governance issues in advance of voting at a company general meeting and shareholders working together with the intention to change control of a company.⁷

Binding Vote on Severance Packages

In France in August 2007 it was announced that beginning in 2009 shareowners will have a binding vote on severance packages adopted by any listed company board for incoming chairmen, CEOs and deputy CEOs. Major changes in severance contracts for those posts would also go to a ballot. All such payouts are to be linked to performance. However, no guidance has been provided as yet as to the consequences if investors overturn a board-agreed CEO package.⁸

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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

⁷ Letter from Michelle Edkins, Acting Chairman, ICGN Shareholder Rights Committee to Herr Bundesminister, 10 October 2007

<http://www.icgn.org/organisation/documents/sri/german_law_change_october2007_en.pdf> at 10 November 2007.

⁸ Global Proxy Watch, 'Arrête!' Vol XI No 39, 2 November 2007.