



ICGN

International Corporate Governance Network

Ms Mavis Tan
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Australian Securities Exchange

By email: mavis.tan@asx.com.au

19th November 2013

Dear Ms Tan,

RE: Review of the ASX Corporate Governance Council Principles & Recommendations

The International Corporate Governance Network (ICGN) welcomes the opportunity to respond to the above consultation issued on 16th August 2013.

As an investor-led organisation of governance professionals, ICGN's mission is to inspire and promote effective standards of corporate governance to advance efficient markets and economies world-wide. We achieve this through three core activities: influencing corporate governance policy; informing dialogue through guidance and education; and connecting peers at international conferences. ICGN members are based in over 50 jurisdictions and include investors responsible for assets under management in excess of US\$18 trillion. For more information on the ICGN, please visit www.icgn.org.

The ICGN commends the Council and its 22 constituent members for having made significant further improvements to what was already a very impressive collaborative effort in codifying corporate governance best practices in Australia's listed securities market. ICGN, like the ASX CGC, is a broadly-based group of governance professionals representing a variety of professional domains and disciplines, but with a common interest in promoting effective standards of corporate governance to advance efficient markets and economies world-wide.

In this context, we note the Consultation Draft echoes principles that underpin ICGN's guidance in our core policy streams, being:

- Shareholder rights and responsibilities
- Corporate reporting and audit
- Corporate risk oversight and business ethics
- Board and shareholder communications

ICGN statements and guidelines developed by ICGN Policy Committees under the above headings are available on our website at <https://icgn.org/best-practice>. In broad terms these are complementary to those espoused in the ASX CGC Principles & Recommendations, although in some cases framed at a broader level to accommodate different regulatory approaches and disclosure cultures in different markets.

Accordingly, rather than provide detailed assessment of each of the ASX CGC Principles & Recommendations against its equivalent policy in ICGN's schema, our comments below are focused on a few particular highlights that we believe warrant special attention, and which ICGN sees as positive precedents for consideration in other jurisdictions as well.

Principle 1: Lay solid foundations for management and oversight

Board and senior executive gender diversity

ICGN commends the proposed migration of the gender diversity content out of Principle 3 (“Promote Ethical and Responsible Decision-Making”) and in to Principle 1 (“Lay Solid Foundations for Management and Oversight”). This is not merely a rhetorical change, but a very appropriate decision to recognise gender diversity as a fundamental value driver in business rather than as an ‘ethical’ consideration alone.

ICGN’s position on gender diversity is reflected in Principle 2.2 of the ICGN Global Corporate Governance Principles (2009) which states:

“Boards need to generate effective debate and discussion around current operations, potential risks and proposed developments. Effective debate and discussion requires...that there is a sufficient mix of relevant skills, competence, and diversity of perspectives within the board to generate appropriate challenge and discussion...”

In June 2013, ICGN members approved a more specific statement on gender diversity on boards (copy attached), which advocates a principles-based approach to improvement and acknowledges that diversity, of gender and more broadly, is a key strategic issue. The ICGN encourages companies to disclose their objectives in this respect and, in cases of non-compliance, encourages investors to hold companies accountable for justifying this.

Specifically, the ICGN recommends the following disclosure requirements:-

- (a) Every company should disclose specific and measurable targets for achieving greater female representation within its senior management and board, and appropriately measure and report on progress in achieving such targets.
- (b) Companies should maintain and disclose an up-to-date skill matrix used to assess the current board; to consider the need for recruitment; and against which director candidates are assessed.
- (c) Companies should disclose the process for board succession planning, and the timeframe over which this is considered.
- (d) Companies should disclose their gender diversity policies for the board, senior management and across all operations, which should include policies on flexible talent management and encouragement of female inclusion in hiring and promotion. This should be emphasised with a statement about why the board believes diversity is beneficial to the company and/or how it is part of the business strategy.
- (e) Boards should provide oversight on diversity throughout the organisation and ensure that there is a discussion of diversity strategy and reporting across the organisation. It would also be advantageous for companies to specify who is ultimately accountable for implementing steps to achieve greater gender balance on their respective boards.
- (f) Companies should communicate to shareholders their aims and achievements in implementing gender diversity policies. In each annual report to shareholders, companies should disclose their progress in effecting female inclusion across all operations, including stating what specific policies have been put in place to develop gender diverse talent at all ranks of the company.

In short, gender diversity is a competitiveness issue for a company as a whole and a critical dimension of governance, both in the board’s oversight of the enterprise and in the board’s

own composition and talent management. Increasing the representation of skilled and competent women on corporate boards will strengthen the corporate governance culture and ultimately contribute to value for all stakeholders.

Whilst phrased somewhat differently and referencing some specific regulatory requirements that naturally only apply in the Australian jurisdiction (e.g. the Australian Commonwealth *Workplace Gender Quality Act* reporting requirements), the proposed Recommendation 1.5 of the ASX CGC Principles & Recommendations strongly reflects these underlying principles and (along with parallel reforms in other key markets such as the Ontario Securities Exchange) is therefore welcomed as an exemplar in gender diversity disclosure practices globally.

Principle 2: Structure of the board to add value

Board member capacity and effectiveness

We welcome the focus on the word ‘effectiveness’ in relation to the functioning of the board. In this regard, ICGN’s Global Corporate Governance Principles (Principle 2.4.1) clarify that:

‘The board should consist of directors with the requisite range of skills, competence, knowledge, experience and approach, as well as a diversity of perspectives, to set the context for appropriate board behaviours and to enable it to discharge its duties and responsibilities effectively.’

We would add that emphasis on the ability of directors to dedicate sufficient time to board meeting preparation and attendance would be advantageous and we note ICGN’s Global Corporate Governance Principle 2.4.2 in this respect:

“All directors need to be able to allocate sufficient time to the board to perform their responsibilities effectively, including allowing some leeway for occasions when greater than usual time demands are made. They should assess on an ongoing basis if new activities may limit their ability to carry out their role at the company, and boards should make substantive disclosures regarding the results of these regular assessments.”

Principle 7: recognise and manage risk

Economic, environmental, social and governance risk disclosures

ICGN welcomes the proposed inclusion in Principle 7 of the ASX CGC Principles & Recommendations (concerning recognition and management of risk) of a specific recommendation concerning disclosure of economic, environmental and social sustainability risks (proposed Recommendation 7.4), as follows:

“A listed entity should disclose whether, and if so, how, it has regard to economic, environmental and social sustainability risks.”

This recommendation, and its inclusion in the risk management section of the document, reflects contemporary good practice in disclosure of environmental, social and governance investment risks, exemplified by the introduction in recent years of similar measures in other jurisdictions including South Africa, Hong Kong, the UK and Brazil. At the same time, the non-prescriptive nature of the Recommendation should provide sufficient flexibility for companies to make their own assessment of how (or indeed whether) these risks are material in their own business situations, and for investors to receive targeted and relevant disclosures that meet their information needs.

In these respects, the proposed Recommendation 7.4 is a good catalyst for listed companies in Australia to meet the “basic requirements from a shareholder and investor perspective” that are enumerated in ICGN’s Statement and Guidance on Non-Financial Business Reporting (copy attached), as well as important aspects of the more comprehensive reporting framework that is currently emerging through the International Integrated Reporting Council (IIRC) consultation process.

We also note that the IIRC reporting framework is itself likely to gain significant momentum over coming months with the imminent finalisation of the draft framework that has been the subject of intensive consultation over the course of 2013. As this will occur during the timeframe envisaged by the Council’s updated Principles & Recommendations, it is important that the ASX CGC document has a sufficient ‘anchor’ for their implementation, both for ESG reporting and other aspects. The proposed Recommendation 7.4 does appear to achieve this goal, and is therefore supported.

General considerations

As noted earlier, there are many other areas in which the Council’s Principles & Recommendations are similar to ICGN guidelines, particularly in areas such as board composition, financial reporting integrity, remuneration policy and risk management. We have not attempted to undertake a detailed reconciliation of each policy item at a granular level, other than to make the observation that the ASX CGC Principles & Recommendations are broadly consistent with those espoused by the ICGN and we view this as an excellent example of collaboration among industry players and articulation of sound governance practices.

We also support the “if not, why not” status of the ASX CGC standards. Members of the ICGN are strong supporters of the flexible application of standards (known variously around the world as ‘apply or explain’, ‘comply or explain’ or ‘if not, why not’), and expect that the ICGN’s own best practice guidelines will be applied with flexibility and understanding of the specific circumstances of individual companies and their markets.

We are grateful for the opportunity to comment on the Council’s consultation and should you wish to discuss any of the points that we have raised, please feel free to contact Kerrie Waring, the ICGN’s Head of Secretariat, by email at kerrie.waring@icgn.org or by telephone on +44 (0) 207 612 7098.

Yours faithfully,



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ICGN

International Corporate Governance Network

ICGN Statement and Guidance on Gender Diversity on Boards

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ICGN Statement and Guidance on Gender Diversity on Boards

About ICGN

An investor-led organization of governance professionals, ICGN's mission is to inspire and promote effective standards of corporate governance to advance efficient markets and economies world-wide. Established in 1995 and present in over 50 countries, the ICGN membership includes global investors with assets under management in excess of US\$18 trillion. For more information, contact the ICGN Secretariat by telephone: +44 (0) 207 612 7098, email: secretariat@icgn.org or visit www.icgn.org.

Preamble

In recent years, the public discussion of Board diversity has focused principally on gender. Boards around the world are overwhelmingly comprised of men, and the small percentage of female directors has increased only modestly despite the extraordinary gains of women in the workplace.

For many years, women have represented a large proportion of the tertiary-educated workforce and female representation continues to grow as a proportion of graduates with advanced degrees. Women occupy an increasing percentage of leadership positions in business, government and the professions.

Companies that fail to draw from the ever-deepening talent pool of well-educated and high achieving women will fall behind in an increasingly competitive world. This is as true for the boardroom as it is for employee recruitment and retention. The challenge and opportunity of embracing gender diversity extends to all levels of the corporation.

This paper focuses on the roles of both shareholders and companies in promoting and supporting gender diversity on Boards. It should be viewed in the context of the ICGN Global Corporate Governance Principles (2009) and other ICGN guidance (see Annex 6.3). It sets out the ICGN's view on gender diversity as an important governance issue in contributing to the effectiveness of Boards and, ultimately, the long-term sustainability of companies.

The guidance has been structured into two primary sections: (a) investor responsibilities; and (b) Board responsibilities. The aim of the guidance is to enhance dialogue between companies and investors on the subject and therefore most likely to help improve gender diversity on Boards.

Gender diversity is a competitiveness issue for a company as a whole and a critical dimension of governance, both in the Board's oversight of the enterprise and in the Board's own composition and talent management. Increasing the representation of skilled and competent women on Boards will strengthen the corporate governance culture and ultimately contribute to value for all stakeholders.

This paper has been developed by a working group of the ICGN Shareholder Responsibilities Committee and takes into account ICGN members' views as expressed through a survey on the subject conducted in October 2012 and through a formal consultation of the ICGN membership carried out in March and April 2013, in addition to other sources. Going forward, the ICGN, through its Shareholder Responsibilities Committee, will begin work on developing a paper on the broader issue of diversity on Boards, extending the approach outlined in this paper beyond the gender issue.

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1.0 ICGN statement on gender diversity on Boards

The ICGN position on diversity relates to Principle 2.2 of the ICGN Global Corporate Governance Principles (2009) which states:

“2.2 Boards need to generate effective debate and discussion around current operations, potential risks and proposed developments. Effective debate and discussion requires:

(c) that there is a sufficient mix of relevant skills, competence, and diversity of perspectives within the Board to generate appropriate challenge and discussion...”

The principle expresses the ICGN view that diversity, broadly defined, and independence are important attributes of a highly functioning Board.

A recent survey of ICGN members found that the majority believe that Boards have a role to play in overseeing human capital strategy which embeds diversity and inclusiveness within a company's operations and approach. Boards that aim for effectiveness, with diversity being seen as an element to help deliver that effectiveness, are likely to perform better than those constructed with compliance in mind.

ICGN advocates a principles-based approach to improving gender diversity on Boards and acknowledges that diversity, of gender and more broadly, is a key strategic issue. The ICGN encourages companies to disclose their objectives in this respect and, in cases of non-compliance, encourages investors to hold companies accountable for justifying this.

Boards which draw on a wide range of relevant skills, competence, and diversity of perspectives are better able to generate appropriate challenge and discussion, thereby generating and preserving enhanced value for investors.

It is the role of the chairman to ensure that such diverse Boards contribute effectively to an active debate. Board diversity is as much about the culture within the boardroom and acceptance of a diversity of views, as it is about having diversity (of gender or otherwise) around the boardroom table.

2.0 Background

2.1 Boardroom reforms and diversity

Countries around the world have enacted reforms to set higher standards of accountability for Boards, to strengthen the authority of independent directors, and to increase the transparency of Board recruitment processes and assessments of the skills required to meet evolving company needs. Many of these reforms were driven, to an extent, by failures in corporate governance practices which in turn contributed to significant investor losses in the early years of the last decade, and more recently during the financial crisis of 2008-2009.

Some Boards were criticised for their failures of attitude and effectiveness due to a propensity towards 'group think' and an inability effectively to rein in management and oversee risk. Such criticisms have been bolstered by the fact that Board composition remains highly homogeneous, raising questions about whether Boards enjoy the range of different perspectives and degree of challenge that will make them most effective.

Diversity of thought and experience are essential contributions towards constructive debate and independence within boardrooms, allowing Boards better to fulfill their expansive oversight responsibilities. These objectives can be accomplished more effectively by recruiting a Board which is diverse in the broadest sense of gender, race, national origin, culture, expertise and thought. Diversity is fundamentally an issue about building the most effective and forward-looking Board possible, and delivering quality governance in the broadest understanding of that term.

2.2 Regulatory and market-led reforms

In the European Pact for Gender Equality 2011-2020 (March 2011), the European Council acknowledged that gender equality policies are vital to economic growth, prosperity and competitiveness and appealed for action to promote equal involvement of men and women in decision-making at all levels and in all fields, so as to utilise all talents. Accordingly, the European Commission (EC) has introduced a Directive on improving the gender balance among non-executive directors of companies listed on stock exchanges.

The purpose behind the EC Directive is to significantly increase the number of women on corporate Boards throughout the European Union by setting a binding minimum objective of 40% presence of the under-represented sex among non-executive directors of companies, focusing on public limited companies, in an effort to promote gender equality in economic decision-making, and to take full advantage of the talent pool of candidates for a more equal gender representation on company Boards.

A number of other countries have introduced legislation imposing gender quotas for Boards of publicly traded companies or relevant disclosure rules. For example, Norway enacted a law in 2003 requiring companies to have 40% female directors by 2008. Spain has also introduced the same quota, to be reached by 2015. The French Parliament passed a law in January 2011 imposing 20% gender quotas on Boards within three years, and 40% after six years. In Italy a hybrid system is in place with a temporary three year period where mandatory action is required and thereafter, it is hoped that this impetus will continue to drive change.

Other countries have adopted a 'comply or explain' approach, encouraging development and disclosure of diversity policies and objectives and ensuring that explanations are provided for any non-compliance. For instance, Australia has introduced a regime for extensive disclosures on diversity policies for the Board, management and the workforce with stated objectives and an explanation of progress made, if any, to meeting those objectives.

In parallel with regulatory reforms, there are a number of market-led initiatives committed to improving gender balance on Boards. For example, in the UK, the 30% Club, is committed to achieving better gender balance at all levels of organisations in order to make businesses and Boards more effective, by taking voluntary steps towards the goal of 30% women on Boards by 2015.

Several initiatives are under way in Canada to help companies increase diversity. Catalyst Canada has issued a call for action for companies to increase the proportion of women directors to 25% by 2017ⁱ. The Canadian Board Diversity Council is publicising 50 "board-ready" candidates each year who are diverse in terms of gender and other attributesⁱⁱ.

The Chartered Secretaries Australia issued the 'Guidelines for gender balance performance and reporting Australia' (the Guidelines). The Guidelines are intended to support Australian entities to make progress on the employment, retention and promotion of women in the workplace, particularly at senior executive level, by providing a best practice framework on the steps and measures necessary for improving gender balance within organisations.

2.3 Academic research

According to several prominent research studies, greater gender diversity in senior executive and Board ranks is correlated with measures of organisational excellence and stronger stock price appreciation than that exhibited by less diverse peers.

Research studies associating gender diversity with financial performance support the view that investors should focus attention on diversity at investee companies. For example, studies conducted by McKinsey & Co (such as that sampling 101 large companies around the world and another sampling 89 European-listed companies)ⁱⁱⁱ, found that companies with the most significant level of gender diversity in top management positions scored higher on measures of organisational excellence, showed more distinct returns on equity, more attractive operating results and stronger stock price appreciation than the average of their respective sectors.

The American non-profit, Catalyst, has conducted two similar studies^{iv}. In both cases, companies with three or more women on the Board outperformed their peer companies in terms of returns on sales, returns on invested capital and returns on equity. The Credit Suisse Institute published a study that found that a sample of companies with women on their Boards outperformed peers that lacked female directors by 26% over a period of six years^v. In 2011, the law firm Eversheds published a study^{vi} examining the relationship between Board composition and share price performance for a sample of 241 large global companies during the financial crisis. The study found a powerful correlation between overall performance and the percentage of female directors.

More recently, in a 2013 Canadian study^{vi}, an empirical testing of a cohort of over 600 companies directors found that female directors achieved significantly higher scores than their male counterparts on the dimension of 'Complex Moral Reasoning', compared to more even scores on other defined reasoning methods of 'Personal Interest' and 'Normative Reasoning'. These results suggest that women may generally be likely to offer superior skills in making key decisions in situations where competing interests are at stake – an attribute that would seem vital at the governance level of today's complex corporations.

Such studies highlight the fact that although the correlation between female directors and firm performance does not imply causation, it does support the proposition that companies which promote women to top management and governing roles may have a number of attributes that lead to organisational excellence and to better share price performance. Conversely, an absence of diversity may signal ineffective management. As the US-based National Association of Corporate Directors has remarked, "*...a lack of diversity can be an apparent sign that the Board is not engaging in a rigorous search for the most qualified people*".

3.0 Board responsibilities

3.1 Disclosure

- Every company should disclose specific and measurable targets for achieving greater female representation within its senior management and Board, and appropriately measure and report on progress in achieving such targets.
- Companies should maintain and disclose an up-to-date skills matrix used to assess the current Board; to consider the need for recruitment; and against which director candidates are assessed.
- Companies should disclose the process for Board succession planning, and the timeframe over which this is considered.
- Companies should disclose their gender diversity policies for the Board, senior management and across all operations, which should include policies on flexible talent management and encouragement of female inclusion in hiring and promotion.
- Boards should provide oversight on diversity throughout the organisation and ensure that there is a discussion of diversity strategy and reporting across the organisation.
- Companies should communicate to shareholders their aims and achievements in implementing gender diversity policies. In each annual report to shareholders, companies should disclose their progress in effecting female inclusion across all operations, including stating what specific policies have been put in place to develop gender diverse talent at all ranks of the company.

3.2 Skills and experience

- When recruiting non-executive directors, competence and fit with the skills and experience the Board is seeking should be the conclusive components. However, within the skills-based framework, Boards should strive for greater gender diversity. It is a Board's responsibility to ensure that it possesses and maintains the right balance of independence, skills and diversity, including gender.
- Boards should be comprised of directors with the knowledge and experience to discharge the Board's responsibilities and the independence of judgment to do so free of any external influence.
- The skills and experience necessary to oversee a company's strategy and risk will evolve along with the company's business. The Board should periodically update its desired skills matrix as the company's business develops.
- Boards should acknowledge that Board composition may need to be refreshed on a regular basis to achieve the optimal mix of director experience. To this end, Boards should consider director tenure and limiting terms of service.

3.3 Evaluation and recruitment

- The Board should include an annual assessment of its own performance in achieving greater female representation within its own ranks as well as within senior management. Given the important strategic value of gender diversity, the Board should also assess the performance of management in implementing gender diversity policies not just within senior management but across the company's entire operations.
- The Nomination Committee should conduct a structured evaluation of the Board of directors on an annual basis to identify ways to strengthen the Board's effectiveness, to assess gender balance, and to highlight gaps between the skills and background of existing directors and their optimal mix. This exercise will help inform the recruitment of new directors whose diversity of skills and experience should address any gaps.
- The Nomination Committee should also develop a succession plan for the Board, recognising that new director recruitment should be conducted strategically to help replace the skill-sets of retiring directors.
- The committee should report to the full Board on how it takes gender diversity into account when nominating candidates to the Board.
- The Nomination Committee should identify and recommend candidates for new Board members and the committee should seek a gender-diverse candidate slate, alongside age, background and experience. This will ensure that new directors are chosen from the widest possible group of qualified candidates.
- The Board should consider requiring the relevant Board committee to address gender diversity and talent management as an explicit element of its oversight work, and to report to shareholders specifically on this.

3.4 Implementation and culture

- Companies should establish programmes to address any failures to deliver levels of diversity that reflect the relevant wider society. Programmes to enable and encourage gender diversity throughout the organisation should encompass:
 - Appropriately tailored recruitment policies
 - On-going skills development and mentoring
 - Human capital strategy development
 - Flexible working and telecommuting opportunities
- A gender diverse Board established over the head of a non-gender diverse company is unlikely to be wholly effective. Investors will certainly be somewhat cynical about gender diversity grafted on only at the very highest level of a company as this may appear cosmetic and management's ability to listen effectively to a full range of views may be in doubt.
- In order to be an effective and open organisation which draws on the skills and talents of all members of society, companies need to have in place approaches to gender diversity throughout their business. Doing so will deliver confidence to investors that this is an issue which management takes with genuine and appropriate seriousness. This will make it more likely that investors will also have confidence that a gender diverse Board is actually able to be effective.

- The natural development of gender diverse staff through the organisation will help lead in due course to gender diversity at executive Board and full Board levels. This will provide further skilled and able non-executive women directors for other Boards.
- Making female executives available for non-executive roles on other companies' Boards should be part of their development programme to accelerate the visibility and board-level skills of these executives.

3.5 Role of advisors

- Recruitment agencies should be challenged by Nomination Committees to look outside the common channels and existing networks to source female candidates.
- Nomination Committees should favour professional agencies with proven abilities to generate genuinely diverse long- and short-lists of potential candidates.
- Nomination Committees should ensure that there are suitably qualified women on the short-lists of candidates that they consider. As such, recruitment advisors should take advantage of the numerous, databases of board-qualified women and they should expect recruiters to broaden their own proprietary databases to include more female candidates. These candidates should include women with senior operating and executive backgrounds, even though they may not have served as CEOs.

4.0 Shareholder responsibilities

4.1 Dialogue with companies

- Shareholders should include discussions around gender diversity in their regular engagement with Boards and management of investee companies, with discussions covering Boards as well as the workforce as a whole. Shareholders have a key role in expressing their views on the implementation of diversity policies and should hold Boards to account for delivering on it.
- Shareholders should seek the development and implementation of gender diversity policies among investee companies, and require investee companies to disclose these policies and the degree of adherence to them in their annual reports.
- Shareholders should encourage companies to consider the way in which human resources are being developed with their organisations and how this incorporates gender diversity. This includes encouraging companies to communicate their aims and achievements in developing and implementing gender diversity policies.
- Shareholders should advocate high standards of governance practice among the companies in which they invest and ensure that consideration of these standards is integrated into investment decision-making processes.

4.2 Voting guidelines

- Shareholders should articulate their expectations in relation to gender diversity on Boards and include these within their own governance and voting guidelines and in relation to appointment and election/re-election of Board members.
- Shareholders should openly disclose their voting guidelines to investee companies. By way of example, the Australian Council of Superannuation Investors includes the following statement in relation to gender diversity in its Governance Guidelines^{viii}:

“4. Board structure

The Board should be comprised of individuals who are able to work together effectively to lead a viable, profitable and efficient company with diverse backgrounds (e.g. age, gender, core expertise) who have a high degree of competency, integrity, skill, capacity, experience and commitment to discharge their duties and responsibilities. Companies must ensure that these factors are considered in the director nomination processes.”

Similarly, the National Association of Pension Funds in the UK recognises the importance shareholders should place on gender diversity in its Corporate Governance Policy and Voting Guidelines^x, recommending that:

“B.2.2. Shareholders will expect companies to explain what steps they are taking to bring diversity to their boardroom, particularly gender diversity. This section should include a description of the Board’s policy on diversity – including professional, international and especially gender diversity – any measurable objectives that it has set for implementing the policy, and progress on achieving the objectives.”

4.3 Exercising voting rights

- Shareholders should utilise tools to monitor companies in their efforts to encourage the improvement of gender diversity at Board level as well as within the corporation, thereby creating an environment for better performing companies and investments.
- Shareholder should recognize that their participation in the nomination and election of the Board is a key responsibility and, where appropriate, they should make use of their voting rights to promote change in gender diversity practices at investee companies. This may, among other things, include the nomination of directors to Boards where gender diversity is found to be lacking and the companies concerned have not embraced the gender diversity agenda.
- Where it is not possible for shareholders to nominate directors to Boards, a first step may be seeking to have this right to have a more active say in the nominations process with relevant regulators and standard-setters.

4.4 Public policy

- Shareholders should communicate the importance of gender diversity to regulators and exchange providers, encouraging them to establish their own policies regarding gender diversity on Boards.
- Regulators and exchange providers should establish a reporting policy on the number of women on Boards. At a minimum, this policy should encourage companies to develop and disclose their own benchmark targets for achieving gender diversity on Boards and in senior management, as well as relevant policies across their operations, including on career and work-life flexibility, management development processes, and mentoring and networking.
- Beyond engaging with individual companies, shareholders should also, where appropriate (either individually or in collaboration with others) make a constructive contribution to market-wide research and benchmarking studies that monitor trends in gender diversity within their particular jurisdiction.

Publication of this information at a trend level can be highly effective in securing the engagement of directors and other stakeholders in companies, without crossing the boundary into the realm of the Board's own discretion to seek the best candidates for its own particular circumstances.

5.0 End Notes

- i Catalyst Accord: Women on Corporate Boards in Canada: <http://www.catalyst.org/catalyst-accord-women-corporate-boards-canada>
- ii Canadian Board Diversity Council: <http://www.boarddiversity.ca/>
- iii Women Matter: Gender diversity, a corporate performance driver (2007): http://www.mckinsey.de/downloads/publikation/women_matter/Women_Matter_1_brochure.pdf AND Women Matter 2: Gender diversity, a competitive edge for the future (2008): http://www.mckinsey.de/downloads/publikation/women_matter/Women_Matter_2_brochure.pdf
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- vi The Eversheds Board Report: Measuring the impact of Board composition on company performance (2011) http://www.eversheds.com/global/en/what/articles/index.page?ArticleID=en/Financial_institutions/Eversheds_Board_Report_080711
- vii Bart & McQueen, (2013), Why Women Make Better Directors – International Journal of Business Governance & Ethics, Vol. 8, No. 1, 2013, pp. 93-99
- viii ACSI Governance Guidelines, July 2011, p11
- ix NAPF Corporate Governance Policy and Voting Guidelines, November 2012, p23

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7.0 Annexes

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7.3 ICGN Guidance

ICGN Statement and Guidance on Gender Diversity on Boards (2013)

ICGN Statement of Principles for Institutional Investor Responsibilities (2013)

ICGN Executive Remuneration Principles and Policy Disclosure Guidance (2012)

ICGN Guidance on Political Lobbying and Donations (2012)

ICGN Model Contract Terms Between Asset Owners and Managers (2012)

ICGN Corporate Risk Oversight Guidelines (2010)

ICGN Non-executive Director Remuneration Guidelines (2010)

ICGN Position paper: What Investors Want from Financial Reporting (2010)

ICGN Global Corporate Governance Principles (2009)

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ICGN Statement and Guidance on Non-financial Business Reporting (2008)

ICGN Securities Lending Code of Best Practice (2007)



ICGN

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Non-financial
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ICGN Statement and Guidance on Non-financial Business Reporting

About ICGN

The ICGN is a global membership organisation of around 550 leaders in corporate governance based in 50 countries with investors collectively representing funds under management of around US\$18 trillion. The breadth and expertise of ICGN members from investment, business, the professions and policymaking extends across global capital markets and our mission is to raise standards of corporate governance worldwide. For more information about the ICGN contact the Secretariat by telephone: +44 (0) 207 612 7098, email: secretariat@icgn.org or visit www.icgn.org.

Preamble

The aim of the ICGN Statement and Guidance on Non-financial Business Reporting is to emphasise its importance within the overall context of company reporting and promote better understanding by setting out disclosure criteria that will assist companies in meeting the expectations of investors. As such, the ICGN Statement and Guidance aims to generate substantive dialogue between investors and company boards about the content and timing of non-financial business reporting.

The ICGN Statement and Guidance has been developed by the ICGN Non-financial Business Reporting Committee in consultation with ICGN members. The first draft was published on 31st March 2008 and a consultation paper on the subject was sent to ICGN members for comment. A wide range of responses were received and contributed towards the final draft.

There was further consultation at an open meeting of the Non-financial Business Reporting Committee with ICGN members at the 2008 ICGN Annual Conference and AGM in Seoul, Republic of Korea. ICGN members attending the AGM voted to approve the draft document, after which the final draft was ratified by the membership by email. In December 2008 the ICGN

Statement and Guidance on Non-financial Business Reporting was published and launched at an ICGN meeting in Wilmington, Delaware.

The ICGN Non-financial Business Reporting Committee recognises the work of existing bodies seeking to advance non-financial business reporting and will engage with such bodies to promote consistency and broad stakeholder acceptance. The aim is to co-ordinate existing efforts and thereby, in due course, lead to a single reference point for companies. This will promote a cohesive view of investor needs, and provide a more compelling incentive for companies to embrace the key principles of non-financial business reporting.

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1. ICGN Statement on Non-financial Business Reporting

1.1 Introduction

The ICGN considers that it is part of the fiduciary duty of institutional investors, such as pension fund trustees and fund managers who are agents for beneficiaries, to take into account all of the information which assists in identifying and mitigating risk on the one hand, and assists in identifying sources of wealth creation on the other. To perform that duty adequately shareowners and investors require comprehensive financial and non-financial disclosure by investee companies.

The ICGN position on disclosure and transparency is set out in the 2005 'ICGN Statement on Global Corporate Governance Principles' as follows:

"Corporations should disclose relevant and material information concerning the corporation on a timely basis, in particular meeting market guidelines where they exist, so as to allow investors to make informed decisions about the acquisition, ownership obligations and rights, and sale of shares."

The ICGN believes that reporting of relevant and material non-financial information is an essential part of the disclosure required to enable shareowners and investors to make informed investment decisions. We use the term 'non-financial' to refer to information relevant to the assessment of economic value, but which does not fit easily into the traditional accounting framework. Other terms such as 'extra-financial' are also sometimes used to describe this information (see Annex 1 regarding terminology).

In a fast-changing, globalising world, information material to investor decision-making is becoming increasingly diverse and dynamic. Long term success in managing a business in today's complex economic, environmental and social landscape is increasingly dependent on factors not reflected in financial statements and in some instances thought to be outside the corporation's sphere of concern.

The same is true for investors when assessing a company's present and future valuation and ability to understand its opportunities and risks. For example, until recently, climate change drew little attention among investors and financial analysts. Today, the confluence of accepted scientific evidence, the pricing of environmental impacts (e.g. through carbon trading schemes), more rigorous financial models and the surging volume of venture capital

investments in climate-friendly technologies attest to the rapid penetration of climate change into financial markets. Similarly, a company's approach to intellectual and human capital may have material consequences for reputation, capacity to innovate, brands, alliances and other intangible assets that are critical to value creation in the contemporary knowledge and information based economy.

These and other issues, including supply chain management, human resources, and environmental management systems, represent a growing class of variables that drive company performance and valuation. All can have an impact directly on short and long-term value creation and destruction. They can have an impact indirectly through effects such as reputation loss or enhancement and customer satisfaction and loyalty. Non-financial business information, when combined with financial information, can provide valuable insight into the overall quality of management, a critical variable in the appraisal of the firm's financial prospects.

1.2 Disclosure and transparency

The ICGN encourages companies to report the information necessary for responsible investment decision making. This is based on a proper understanding of the company's strategic objectives,

as well as the financial and non-financial risks and opportunities which may affect its ability to meet those objectives.

Companies in different industries, sectors and social contexts will face different material and relevant issues. Shareholders and investors should seek, and companies should provide, information about the factors which enable investors to judge future prospects as well as past performance.

Non-financial business reporting contributes to achieving the objectives of disclosure and transparency as described in the 'ICGN Statement on Global Corporate Governance Principles.' However, it should not be considered in isolation. It is important that all disclosure integrates consideration of financial and non-financial risks and factors which may affect the company's ability to achieve its strategic objectives.

Sustainability reports serve a useful purpose for multiple stakeholders in informing the wider community, but issues material to investors should be set out succinctly in the annual report prepared and/or approved by the board itself, and addressed to shareholders. This will demonstrate that directors regularly take non-financial issues into account.

Non-financial issues that may be material include: the impact of environmental risk, such as climate change; matters affecting employees, customers, suppliers and

host communities; the development and protection of intellectual property and other intangible assets which are crucial to success; ethics, and governance arrangements. Other non-financial matters which are relevant may be company or sector-specific. For example, reporting by pharmaceutical companies may include information about the multi-year drug development pipeline, while retail companies may report on same-store sales.

1.3 The quality of reporting

Standardised reporting within and between companies greatly assists investor decision making and comparative analysis. The ICGN welcomes efforts to develop acceptable common understanding, standards and guidance for disclosure and reporting to support the financial statements which are being pursued by international standards-setting bodies such as the International Accounting Standards Board (IASB) and the wider corporate reporting community. The value of qualitative and quantitative reporting alongside the financial statements should not be underestimated, nor the importance of judgement in ensuring the relevance of non-financial business reporting.

The ICGN considers that non-financial business reporting should:

- be genuinely informative and include

forward-looking elements where this will enhance understanding;

- be material, relevant and timely;
- describe the company's strategy, and associated risks and opportunities, and explain the board's role in assessing and overseeing strategy and the management of risks and opportunities;
- be accessible and appropriately integrated with other information that enables investors to obtain a whole picture of the company;
- use key performance indicators that are linked to strategy and facilitate comparisons;
- use objective metrics where they apply and evidence-based estimates where they do not;
- be strengthened where possible by independent assurance that is carried out having regard to established disclosure standards applicable to non-financial business reporting, such as those issued by the IASB.

The above examples used to illustrate these guidelines are not by any means an exclusive list. They are designed only to illustrate the need for high standards of non-financial business reporting which, when combined with conventional financial reporting, will enable well-informed investment decision making.

2. ICGN Guidance on Non-financial Business Reporting

2.1 Background

Conventional financial reporting primarily describes what has already occurred, for example, revenues, net earnings and depreciation of assets during a specified time period. These are essential to understanding a company's financial results and condition at a point in time. However, traditional accounting is generally transaction focused and ill-equipped to capture intangible drivers which in the modern economy increasingly underpin value creation. The so-called 'value gap' between more traditional financial accounting measures of value, such as book value on the one hand and market capitalisation on the other, suggests a need to go beyond conventional accounting. Investors need to understand what drives value.

Non-financial business reporting can help to inform the investment process by revealing in both quantitative and qualitative terms those drivers that increasingly shape company performance. The existence of the 'value gap' suggests that investors understand the potential importance of non-financial business reporting in making investment decisions, and the

issue is whether this process can be made more efficient and whether it might benefit from comparable metrics. Efficient asset allocation depends on the ability to compare companies within sectors and ultimately across sectors and this requires a degree of standardisation of definitions.

To complement the information provided by traditional accounting, non-financial business reporting should provide information that helps put historical performance into context, and portrays the risks, opportunities and prospects for the company in the future, be that two, five or ten years or even longer in certain industries. It has an important role in mitigating the short-termism that currently afflicts financial analysis and other approaches to valuation and in helping investors understand a company's strategic objectives and its progress towards meeting them.

Non-financial business reporting should seek to reflect the complexities inherent in a contemporary business - the interdependence of financial and non-financial factors on its prospects; management's understanding of this interdependence; its ability to harness this for value creation; and awareness of the risks and opportunities that flow from non-financial factors.

While failure to recognise these risks and opportunities may not immediately translate into financial outcomes, this is

unlikely to be true in the long-term, which is the time horizon of greatest concern to institutional investors and their beneficiaries.

2.2 Expectations of non-financial business reporting

Different stakeholder groups and interested parties have different needs and expectations about the nature of information relevant to their decision making, depending on the issues of particular concern to them. Investors seek information about how a company creates financial value and deals with issues including governance, environmental, social and ethical issues that can affect its financial performance and value over time.

It is increasingly recognised that relationships with key stakeholder groups including customers, employees, and communities can affect the company's financial performance and future value. In other words, an intangible business value, positive or negative, may be attributed to a company's relationships with its stakeholders.

Care needs to be taken to make sure that measures selected are relevant to the specific circumstances of the business. It is useful for investors seeking to compare the performance of different companies in a sector if

businesses provide information on performance against measures that are widely accepted in the sector concerned. It is also generally helpful for information to be provided on how the measures have been developed and for a consistent approach to be adopted from one year to another so that changes in performance over time can be evaluated.

Critically, businesses need to recognise the link between improvements in non-financial areas and in cash flow or the share price. Such improvements can occur after a time-lag which highlights the importance of relevant non-financial measures as they may act as a lead indicator of future performance. It is also important to avoid measuring too many things leading to a wild profusion of peripheral, trivial or irrelevant measures.

2.3 Basic requirements from a shareowner and investor perspective

The ICGN recognises that there is a need to balance corporate disclosure with protection of commercially sensitive information. The purpose of setting out guidance on non-financial business reporting from a shareowner and investor perspective is to indicate to companies the type of reporting which is useful and to encourage the investment community to solicit such information.

Bearing in mind that non-financial business reporting should be both quantitative and qualitative in nature, disclosures that are valuable to long term investors will:

- be genuinely informative and include forward-looking elements where this will enhance understanding.

Non-financial business reporting should support and enhance the information in the financial statements. It will set historic performance in the context of a company's strategy and market conditions and will offer insight into the potential for future success. Such forward-looking elements include trend data that can help investors to assess the company's strategy and prospects. Where forward-looking and historical non-financial business reporting is provided, it should explain how it helps to form an assessment of the company's strategy and prospects. For example, does it indicate significant trends that are not evident from the financial statements and, if so, how these trends are likely to affect the company?

- be material, relevant and timely.

Non-financial business reporting is material if it might reasonably be expected to affect investors' decisions about the acquisition and sale of shares or the exercise of ownership rights and obligations. Non-financial business reporting should be timely, in particular meeting market guidelines

and it should be made available as soon as reasonably possible so that investors are able to make informed decisions based on it and the likelihood of a false or distorted market is diminished.

Information should be focused in order for it to be genuinely useful. Too much information that is not relevant will dilute the message. The materiality (or not) and relevance of the issues covered will be determined by the company's circumstances and the sector within which it operates, rather than being determined by a prescriptive approach to what should be reported.

- describe the company's strategy, and associated risks and opportunities, and explain the board's role in assessing and overseeing strategy and the management of risks and opportunities.

The explanation should focus on the key points necessary to help investors understand not only the strategy, risks and opportunities but also form a view of the appropriateness and effectiveness of the governance approach adopted by the board in its oversight of these matters.

- be accessible and appropriately integrated with other information that enables investors to obtain a whole picture of the company.

Non-financial business reporting should be in a form which shareowners and investors can reasonably be expected to understand. For example, complicated technical terms should be explained and care should be taken to ensure that the information is clearly written and presented. It should be appropriately integrated with and presented alongside financial information in companies' reports to shareowners.

- use key performance indicators that are linked to strategy and facilitate comparisons.

An indicator is likely to be important and relevant to strategy if it is used by the board in monitoring the company's performance in achieving its strategy and if it is therefore likely to affect board decisions. However, for non-financial business reporting to achieve its potential to assist in efficient capital allocation, it could be argued that consistent definitions and industry norms may be needed for certain metrics even if they are not used by management.

Indicators disclosed in non-financial business reporting should facilitate comparisons with other companies and for the same company over time. Where sector-specific practices have emerged for indicators, companies should follow them unless they have reasons for considering them inappropriate. Companies should disclose indicators that are

comparable over time, unless circumstances change and they cease to be appropriate.

- use objective metrics where they apply and evidence-based estimates where they do not.

Where objective measures of intangibles are relevant and can be obtained, such measures should be used. In the absence of relevant objective measurements, estimates and commentary should be provided. Narrative discussion and judgement can be useful in conveying information. Both metrics and judgement are valuable in non-financial business reporting.

- be strengthened where possible by independent assurance that is carried out having regard to established disclosure standards applicable to non-financial business reporting, such as those issued by the IASB.

Independent assurance about the extent to which non-financial business reporting has followed established measurement and reporting standards can be useful to enhance the credibility and reliability of the reported information. Companies should adopt a clear and disclosed policy towards obtaining assurance.

Annex 1: Terminology

Non-financial business reporting is a wide-ranging term which can include both regulated and voluntary disclosure by companies. From a shareholder and investor perspective, it is information, other than financial statements, which is relevant and material to investment decision making. This may include descriptive information around a company's operation and strategy or other disclosures which may bear on intangible assets and value drivers, and the company's "social license to operate". Other terms such as 'extra-financial' and 'narrative reporting' are sometimes used to describe such information.

The United Nations' Principles for Responsible Investment (UNPRI) encompass a significant subset of the terms covered by non-financial business reporting. In this regard, the UNPRI has adopted the term, Environmental, Social and Governance (ESG) which covers factors that investors, who wish to be seen as 'Responsible Investors', should take into account and equally, ESG disclosures expected of companies. 'Corporate Social Responsibility' or simply 'Corporate Responsibility' are widely used terms encouraging positive corporate social and environmental practices and, inter-alia, their disclosure as part of non-financial business reporting.

Some companies have responded to these various demands for additional disclosure by producing "Sustainability Reports" either as part of their annual reports to shareholders or as stand alone reports.

In recent years, many companies have embraced various forms of non-financial business reporting, notably in terms of their environmental and social impacts. In Europe and Japan, there has also been experimentation with various types of intellectual capital statements. However, there is as yet no generally accepted definition of what constitutes non-financial business reporting, though significant progress has been achieved.

In a welcome initiative, the IASB in 2008 began to develop non-mandatory guidance for a narrative report described as 'Management Commentary'. The IASB aims to develop the principles, qualitative characteristics and essential content elements necessary to make Management Commentary useful to investors. This is an important step towards achieving global consensus on non-financial business reporting whilst recognising diverse legal, cultural and regulatory environments in different jurisdictions.

Annex 2: Metrics

Credible and verifiable measurement of non-financial business reporting is vital. However, the development of valid metrics is challenging due to a variety of factors including the measurement of intangibles, claims of proprietary information, and comparability across qualitative data elements. The metrics for non-financial business reporting will frequently be determined by the specific characteristics of a company and the sector in which it is operating. However, there is a growing consensus on a number of components that will have widespread relevance across multiple sectors.

The ICGN Non-financial Business Reporting Committee's own deliberations, as well as the work of other interested groups, highlight a number of broad subject areas as being integral components of non-financial business reporting. These include not only corporate governance, which is a central focus of the ICGN's mission, but also areas such as intellectual capital, human capital, the environment, customer goodwill, reputation, human rights, anti-corruption, suppliers and community relations.

These areas may themselves be redefined or reshaped over time as the field of non-financial business reporting evolves often in line with developments in legal and regulatory requirements

and emerging views about topics such as workplace, social and ethical practices in the field of non-financial business reporting. The impact of global and economic trends should be also taken into account. Often the impact of such trends is immediate on the financial reporting side, but they also have a long term impact on corporate sustainability and value.

The ICGN aims to encourage companies to develop and use metrics which suit their particular circumstances while pointing to the value of developing consensus around components which allow for comparison. It aims to help foster such a consensus without prescribing any particular solutions.

Annex 3: Resource list

Some examples of useful guidance documents, standards and studies relating to non-financial business reporting, including those recommended by ICGN members who responded to the consultation on the subject, are listed below. Further examples will be available in due course on the ICGN website at www.icgn.org.

International references

- CFA Institute, 'Environmental, Social, and Governance factors at Listed Companies: a Manual for Investors' (2008)
- Global Reporting Initiative, 'G3 Sustainability Reporting Guidelines' (2006)
- International Accounting Standards Board, 'Management Commentary Discussion Paper' (2005)
- International Auditing and Assurance Standards Board, 'ISA 720 Other Information in Documents Containing Audited Financial Information'
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- UNEP Finance Initiative, Asset Management Working Group, 'Show me the money – linking environmental, social and governance issues to company value' (2006)
- Canadian Institute of Chartered Accountants, 'MD&A Guidance on Preparation and Disclosure'
- Deloitte, 'Added value, long term: non-financial sustainability key performance indicators on their way into financial reports of German companies'
- DVFA – Society of Investment Professionals in Germany, Committee on Non-financials, 'Key performance indicators in the telecommunications sector'
- Institute of Chartered Accountants in Australia, 'Extended performance reporting: an overview of techniques'
- Institute of Chartered Accountants in England and Wales, 'Sustainability: the role of accountants' (2004)
- The Norwegian Society of Financial Analysts, 'Recommended guidelines for the reporting of additional information on value creation'
- Universities Superannuation Scheme, James O'Loughlin and Raj Thamootheram, 'Enhanced analytics for a new generation of investor'

National references

- AccountAbility, 'AA1000 AccountAbility Principles Standard' (2008)
- Accounting Standards Board (UK), 'Operating and Financial Review'
- Australian Institute of Company Directors & PricewaterhouseCoopers, 'Shareholder friendly report'
- US Securities and Exchange Commission, 'Management's Discussion and Analysis of Financial Condition and Results of Operations'

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Other ICGN Best Practice guidance available:

ICGN Guidance on Political Lobbying and Donations (2012)

ICGN Model Contract Terms Between Asset Owners and Managers (2012)

ICGN Corporate Risk Oversight Guidelines (2010)

ICGN Non-executive Director Remuneration Guidelines (2010)

ICGN Position paper: What Investors Want from Financial Reporting (2010)

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ICGN Guidance on Anti-Corruption Practices (2009)

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ICGN Statement of Principles on Institutional Shareholder Responsibilities (2007)

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