CORPORATE GOVERNANCE IN AUSTRALIA: IMPLICATIONS OF RECENT INTERNATIONAL DEVELOPMENTS

by

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The financial failures in the United States and the revelations which were subsequently made about the deficiencies which contributed to such failures have once again focussed international interest on the most appropriate manner by which effective corporate governance can be achieved. The legislative responses to these failures have provided the regulators in the United States with ample opportunity to require improvement of corporate governance practices aimed to rectify the shortcomings. Similar developments in Australia, though not as well known outside the antipodes, have had similar effect, with major corporate collapses of HIH and One.Tel resulting in legislative proposals in Australia which are not too dissimilar to those legislated in the United States in June, 2002.

In both the United States and Australia, prescriptive standards for certain aspects of corporate governance have been proposed. In the United States, the passage of the *Sarbanes-Oxley Act*[1] in July, 2002, was primarily intended to redress accounting and audit practice deficiencies revealed by recent United States corporate failures. Nevertheless, the changes brought about by this legislation also have broader implications, including the constitution of the board of directors and the role of professional advisors. The corporate governance aspects of this legislation have now begun, with international implications being felt throughout the world. Even for those corporations not directly regulated by the legislation or the corporate governance listing rules which it requires, the *Sarbanes-Oxley Act* has acted as a model for change.

In Australia, Mr. David Knott, Chairman of the Australian Securities and Investments Commission ('ASIC'), perhaps heartened by the quick passage of the American legislation, proposed in a speech delivered to the opening of the Monash Governance Research Unit in July, 2002,[2] that more prescriptive standards be imposed on listed entities in Australia by the Australian Stock Exchange (the 'ASX'). Although initially received with no great enthusiasm by the ASX, the ASX indicated in an announcement by its CEO, Richard Humphry on 1 August 2002 that it had come to accept that some change was necessary.

For Australian companies and their legal and accounting advisors, the new corporate governance landscape now requires Australian companies and their advisors to consider a number of new developments. These include the new obligations which may be applicable as a result of the passage of the *Sarbanes–Oxley Act*, newly proposed Australian legislative requirements, and new corporate governance principles upon which specific disclosure is now required under the listing rules of the ASX.

UNITED STATES DEVELOPMENTS

The Corporate Failures in the United States

The two major corporate collapses in the United States which precipitated the changes to corporate governance practices were those of Enron and World Com. Both of these collapses raised fundamental questions about the corporate governance systems which operated at the time.

At the time of Enron Corporation's collapse in December 2001, it was listed as the seventh largest company in the United States with over US$100 billion in gross revenues. It had created an online energy trading facility which treated contracts to deliver energy products like marketable commodities. In order to increase cash flow, lower its debt, and smooth its earnings (to flatter its financial performance), Enron developed a number of strategies, including securitizing energy contracts and syndicating its assets. These strategies required counterparties willing to invest in the energy contracts and syndicated assets. Enron relied upon increasingly complex transactions, including transactions with special purpose vehicles which were unconsolidated entities. In addition to the "high risk" treatment of these transactions, the vehicles used for such transactions often involved related parties and frequently involved collateralized Enron shares. Further, remuneration policy for executives was "excessive" and involved factors influenced by the financial position as reported. When these transactions unravelled, the share price dropped, leading to an acceleration in the demise of Enron's capital value.

A number of factors contributed to Enron's failure; however, chief among them was the lack of institutional assurance of the independence of the auditor and the audit committee. Involving the same accounting firm in provision of both auditing

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and consulting services meant that the auditor might fear not only the loss of his audit engagement, but also the loss of substantial consulting income if the audit reports were not favourable to management. The inclusion of former partners on the audit committee meant that the audit committee itself was less likely to be disruptive.

Also contributing to Enron's failure was the lack of an over-riding obligation on United States auditors to present financial statements which, in addition to complying with generally accepted accounting principles, presented a true and fair view of the financial position of the corporation. The accounting practices in the United States complied with the specific requirements while completely disguising the true circumstances. Enron's use of unconsolidated partnerships to place potential liabilities off balance sheet was an example of that practice.

Encouraging the use of these dubious practices was the determination of executive bonuses based upon maintenance of share price. In the case of Enron, this need to maintain high share values was accentuated by the provision of company shares to related entities in circumstances which meant that liabilities would not be attributed to Enron itself. When the share price dropped, the entire artifice imploded.[3]

WorldCom was the second-largest long distance carrier in the United States, as a result of which it had invested heavily in fibre optic technology. Because of excess capacity in fibre optic line availability, WorldCom's earnings were eroded by a softening price for such services. In order to meet market expectations, the operations of WorldCom were reported so as to re-construe expenses to permit WorldCom to report profits over the two-year period prior to bankruptcy. When these practices began to be known, share values fell and employees were laid off. Nevertheless, the corporation still was able to pay $ 287 million in a bonus scheme for executives.[4]

The Deficiencies in Corporate Governance Revealed

The corporate collapses in the United States revealed a number of deficiencies in the systems of corporate governance. Specific deficiencies identified by the Enron failure were ineffective measures to assure audit independence, problems with accounting systems, and general issues with the role of the board of directors in preventing conflicts of interest. Many of these issues also arose with WorldCom, but the appropriateness of paying executive bonuses in circumstances such as those found with WorldCom were also a matter of concern.

While many of these deficiencies may have been rectified by specific remedial action, the approach to enforcement of corporate governance norms has also been the subject of re-consideration in the United States. After *Sarbanes-Oxley*, public corporations in the United States will need to comply with corporate governance norms which are required by legislation, regulation, or exchange listing rules. At least in this regard, the responses of Australia and the United States are somewhat different, as Australia has adopted a model similar to that of the United Kingdom which relies upon disclosure and market pressure rather than direct imposition of obligations to accomplish desired aims.

The United States Response

Although it is quite easy to summarise the provisions of the *Sarbanes-Oxley Act*, the implications of its passage may be somewhat more difficult. In addition to the specific measures taken, it is also clear the United States has moved in a fairly decisive way toward a more prescriptive regulation of corporate governance.

The important features of the Act are:

(1) The establishment of the Public Company Accounting Oversight Board to: (a) oversee the audit of public companies that are subject to the securities laws; (b) establish audit reporting standards and rules; and (c) investigate, inspect, and enforce compliance relating to registered public accounting firms, associated persons, and the obligations and liabilities of accountants.[5]

(2) The prohibition of registered public accounting firms from performing specified non-audit services contemporaneously with a mandatory audit and requires pre-approval for non-audit services not expressly forbidden by statute. It also mandates: (a) audit partner rotation on a five-year basis; and (b) auditor reports to audit committees of the issuer. The Act also prevents a registered public accounting firm from performing statutorily mandated audit services for an issuer if the issuer's senior management officials had been employed by such firm and participated in the audit of that issuer during the one-year period preceding the audit initiation date.[6]

(3) The provision to the audit committee of an issuer the responsibility for the appointment, compensation, and oversight of any registered public accounting firm employed to perform audit services. The Act requires audit committee members to be members of the board of directors of the issuer, and to be otherwise independent.[7]

(4) A requirement for the chief executive officer and chief financial officer of an issuer to: (a) certify that periodic financial statements filed with the United States Securities and Exchange Commission (SEC) fairly present, in all material respects, the operations and financial condition of the issuer; and (b) forfeit certain bonuses and compensation received

following an issuer's accounting restatement owing to non-compliance with securities laws. These were intended to reverse the "avoidance mentality" which over concern with specific rules had engendered.

(5) Imposition of an SEC requirement that financial statements disclose all material off-balance sheet transactions and relationships that may have a material effect upon the financial status of an issuer.[8]

(6) Requires the presentation of pro forma financial information to the SEC in a manner that is not misleading, and which reconciles it with the financial condition of the issuer under generally accepted accounting principles.[9]

(7) Adoption of rules for the SEC designed to address conflicts of interest in securities research.[10]

(8) The introduction of new criminal offences such as knowingly destroying, altering, concealing or falsifying records with intent to obstruct or influence an investigation in a Federal matter or in bankruptcy.[11]

(9) Enhancement of the criminal penalties for fraud;[12] and

(10) Imposition of a requirement on senior corporate officers to certify in writing that financial statements and the disclosures therein fairly present in all material aspects the operations and financial condition of the issuer.

The Act also generally prohibits a corporation from making personal loans to its corporate executives; reduces the mandatory period for senior executives and principal stockholders to disclose changes in ownership of securities) to two business days; and directs the SEC to promulgate a code of ethics for senior financial officers of an issuer.[13]

SEC Initiatives and NYSE Response

Prior to the passage of the *Sarbanes- Oxley Act*, the Securities and Exchange Commission had already considered that changes in relation to its listing requirements were necessary. In its review of the obligations to be imposed upon those corporations which were subject to its oversight, the SEC had indicated in June, 2002 that it would seek to implement the following:

1. Requiring independent directors to comprise a majority of a listed company's board and tightening of the definition of "independent director;"
2. Requiring non- management directors to meet regularly without management;
3. Mandating that all companies must have an audit committee, a nominating committee and a compensation committee, each comprised solely of independent directors;
4. Requiring listed companies to adopt corporate governance guidelines, as well as charters for their audit, compensation and nominating committees;
5. Requiring listed companies to adopt a code of business conduct and ethics; and
6. Giving shareholders the opportunity to vote on all equity-based compensation plans.

On June 6, 2002, the New York Stock Exchange Corporate Accountability and Listing Standards Committee filed its report indicating that the NYSE Listing rules should be modified in a way which would accomplish many of the objectives desired by the SEC. On August 1, the changes which were proposed were approved by the Board of Directors of the New York Stock Exchange, and the changes were filed with the SEC on August 16, 2001. The NYSE modified its filing on April 4, 2003.[14]

After passage of the Sarbanes-Oxley Act, the SEC has proceeded to "flesh out" a number of the Sarbanes Oxley requirements through regulation released in February, 2003. Of most interest to Australia are requirements concerning the concept of "independence" in relation to board members and the obligations imposed upon lawyers who represent clients before the SEC. Both of these will impact Australian companies listed on United States markets, as discussed below.

Direct Australian Impact of *Sarbanes-Oxley* and Exchange Rules Changes

The passage of the *Sarbanes-Oxley Act* itself would have had minimal impact upon corporations outside the United States were it not for the fact that a number of Australian and other foreign corporations have sought to raise capital on the stock exchanges of the United States. As a result of this, the United States legislation and the rules for corporate governance implemented by American exchanges in response to the requirements of *Sarbanes-Oxley Act* necessitate that Australian corporations which are listed on United States exchanges comply with such listing rule requirements.[15]

Because the Australian listing rules (of the ASX) implemented in March 2003 are similar to the requirements imposed upon listed corporations in the United States, many of the requirements applicable to dual listed companies would have applied eventually by operation of the ASX listing rules. Nevertheless, the introduction of a requirement that a majority of directors be independent and the expanded definition of independence did not occur simultaneously in the United States and Australia, with the result that Australian companies with United States listings were more quickly required to comply with

the new corporate governance norms so as to maintain their American listing. Further, the more prescriptive nature of the American system (as compared to the Australian system, described below) left less room for manoeuvre to avoid compliance. As a result of this, a number of Australian accountants and solicitors were effectively required to vacate their seats on the Board of Directors of client corporations, being faced with the choice of serving as a director or forfeiting professional fees. Many elected to forego the directorships rather than the professional relationship, thereby depriving such corporations of significant expertise (although increasing the proportion of independent directors).

In contrast to the indirect effect of the changes affecting United States listed Australian companies, the adoption by the SEC of rules to implement section 307 of the *Sarbanes-Oxley Act* (proposing standards of professional conduct for legal practitioners) had potentially quite significant direct impact in Australia. On November 6, 2002, the SEC voted to propose standards of professional conduct in a new Part 205 of Title 17 of the Code of Federal Regulations. These regulations affect the attorney-client relationship by indicating what responsibilities an attorney has when they become aware of a material violation and by allowing attorneys to reveal confidential information without the consent of the client in certain instances to prevent the commission of a material violation. While these changes have been the subject of significant discussion in the United States (both because of the direct impact upon State law and because of the alteration of the attorney client relationship), those changes were particularly worrying in the international context (where Congress's ability to alter the foreign substantive law relating to lawyer-client relationships is yet to be recognized). Thus, if the regulations as originally formulated were applied to foreign practitioners, they were faced with the prospect of being required to comply with applicable federal regulations which would result in the contravention of their locally required obligations as legal practitioners. Fortunately, submissions from foreign legal practitioners resulted in a clarification which should be satisfactory to all.

AUSTRALIAN DEVELOPMENTS

The Corporate Failures

In Australia, similar events to those which occurred in the United States with Enron and WorldCom have transpired with the failures of HIH (a general insurance company) and OneTel (a telecommunications company) in circumstances remarkably similar to those in the United States.

HIH was the one of the largest general insurance companies in Australia, having been run nearly from its inception by its Chief Executive. In order to maintain appropriate balance sheet and profitability, the company had invested in insurance businesses in the United Kingdom, the United States and had acquired another large Australian insurer, FAI. Because of inexact accounting requirements, HIH continued to show profits even though claims often eventually proved larger than accounting reserves which had been factored into the company's performance. On 15 March 2001 the major companies in the HIH Insurance group were placed in provisional liquidation. Formal winding-up orders were made on 27 August 2001with deficiencies of the group estimated to be between A$3.6 billion and A$5.3 billion, making it the largest corporate failure Australia has endured.

The Royal Commission into the HIH failure concluded:

> HIH is not a case where wholesale fraud or embezzlement abounded. Most of the instances of possible malfeasance were borne of a misconceived desire to paper over the ever-widening cracks that were appearing in the edifice that was HIH.
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> Where did the money go? Some of it was wasted by extravagance, largesse, paying too much for businesses acquired, and questionable transactions. There were some trading losses. But in the main the money was never there. The deficiency of several billion dollars has arisen because claims arising from insured events in previous years were far greater than the company had provided for. Past claims on policies that had not been properly priced had to be met out of present income. This was a spiral that could not continue indefinitely. In the language of the industry, the failure to provide adequately for future claims is called 'under-reserving' or 'under-provisioning'. This, in my view, is the primary reason for HIH failing—and not only failing but doing so in such an egregious way.[16]

Unlike HIH and Enron, but much like World.Com, One.Tel was a telecommunications company caught by negative economic circumstances rather than poor accounting practice. One.Tel , a company listed on the Australian Stock Exchange, was placed into voluntary administration in May 2001 and then into liquidation in July 2001. While the internal corporate governance practices of the company were called into question by ASIC (particularly the role of the Chairman of the Board of Directors), the major implication of One.Tel's failure was the community outrage at the payment to the directors of performance bonuses prior to the collapse. Although circumstance might have allowed for recovery of such bonuses in bankruptcy, the fact that performance criteria could have provided for such bonuses even though the company was poorly performing has resulted in the introduction of legislation to control such payments.[17]

Lack of audit independence, inappropriately constructed executive bonuses and poor financial reporting all contributed to the collapses. In the Australian cases, the failures also resulted from activity which did not meet even the minimal

standards imposed by the *Corporations Act*. Nevertheless, as in the United States, changes in corporate governance practice (particularly in relation to accounting and audit practice) were seen to be required.

Ramsay Report

The problems with audit independence were raised by the corporate collapses of HIH and OneTel in Australia; however, the full extent of the problem with audit independence was truly highlighted by the failures in the United States, particularly that of Enron. In October 2001, Professor Ian Ramsay of the University of Melbourne released a report on audit independence intended to improve the safety and security of investments.

In suggestions which proved to be consistent with the approach adopted both by SEC Rules and by the United States Congress months later, Professor Ramsay's report[18] made the following recommendations:[19]

1. Imposition through the *Corporations Act* of a general requirement that auditors be independent;
2. Incorporation into the *Corporations Act* of best international practice concerning the employment of auditors and the financial relationships between the audit firm and its clients to assure appropriate independence;
3. Requiring improved disclosure of the non-audit services provided by the audit firm so that the type of service and dollar value of such service would be apparent;
4. Prohibiting the those partners of an audit firm who were directly involved in an audit from becoming directors of the audited company within two years of their resignation from the audit firm;
5. Prescribing that all listed companies have audit committees;
6. Establishment of an auditor independence supervisory board; and
7. Implementation of measures to improve the operation of the Companies Auditors and Liquidators Disciplinary Board.

While the Ramsay Report could be viewed as a measured response in light of some Congressional responses (rotation of audit firms every five years); many of the proposals have yet to be implemented. Nevertheless, audit independence is a main feature of appropriate corporate governance, and many of the recommendations of the Ramsay report are included within legislative proposals introduced late in 2002. In light of the successful implementation of similar reforms in the United States with the *Sarbanes-Oxley Act*, it is likely that greater protections of that auditor independence will also occur through legislative action (CLERP 9, discussed below) in Australia in 2003.

ASIC/ASX Debate

Whether corporate governance practices could ever be properly encouraged only through use of general disclosure requirements (as had been the case in Australia until 2002) was raised by Mr. David Knott, Chairman of the Australian Securities and Investments Commission in his Inaugural Lecture to the Monash Governance Research Unit in July, 2002. In this lecture, entitled "Corporate Governance – Principles, Promotion and Practice," Mr. Knott, after reviewing the American developments, challenged the current system (particularly the role of the ASX) in the following terms:

> In the light of these developments there have been increasing calls of late for the ASX to adopt a more assertive role in this area. The ASX listing rules do, of course, include mandatory rules that are related to corporate governance. For example, those rules which require shareholder consent whenever the corporation enters into particular transactions that are prone to abuse, are clearly related to corporate governance. The ASX listing rules also require that listed entities must include, in their annual reports, a statement of their main corporate governance practices.
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> However, unlike many other exchanges, the ASX has specifically disavowed any intention to endorse best corporate governance practices. It argues that the diversity of entities that it lists, the existence of alternative solutions to address particular governance problems and the development of corporate governance ideas over time, mean that it is inappropriate for it to require particular practices to be adopted.
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> In seeking to assess this difference of approach, we should be mindful that, unlike the NYSE, ASX is a 'for profit' corporation; and regulatory responsibility often sits uncomfortably alongside the profit motive. The Corporations Act imposes a responsibility on ASX to ensure that its market is fair, orderly and transparent; it must supervise its market, including compliance with its listing and business rules; and it must have listing rules that comply with the relevant regulations. However, any additional regulatory role is a matter of choice for ASX – that is, it is up to ASX to decide whether it wishes to combine such a role with its 'for profit' business model. This is an important dynamic created by the de-mutualised, for-profit exchange structure which is growing around the world. Responses to the new environment differ. In the United Kingdom, for example, the government responded to the demutualisation of the London Stock Exchange by transferring the listing responsibility from the Exchange to the UK Financial Services Authority (ASIC's equivalent).

Time will tell whether the current Australian arrangements are sustainable, or whether the ASX will accept extended responsibilities in this area. It is always possible, of course, that additional governance obligations will be legislated or that ASIC will be charged with increased responsibilities in the area.

Whereas initially this statement met with resistance from the ASX, in a media release on 1 August 2002, Mr. Richard Humphry, Managing Director and Chief Executive Officer of the ASX stated:

- To further broaden this disclosure regime, ASX will lead a renewed initiative to develop an agreed set of corporate governance standards of best practice for Australian listed companies.
- ASX will convene a Corporate Governance Council tasked with the development, on the basis of consultation with the business community, of a set of consolidated and up-to-date standards.
- Further, ASX will enhance current Listing Rule disclosure requirement where appropriate to ensure that listed companies fully report to the market and shareholders on their adherence to these standards.[20]

Shortly after this statement was made in August, the ASX convened the ASX Corporate Governance Council. The Council included representatives of a number of industry bodies with an interest in promoting good corporate governance.[21] The Corporate Governance Council was intended to serve ass a central reference point for companies to understand stakeholder expectations, in order to promote and restore investor confidence. Its stated purpose was to develop recommendations which would reflect international best practice. The deliberations of the Corporate Governance Council continued until early 2003, when its recommendations were released (discussed below). During this time, however, the Government of Australia responded to the Ramsay report with a paper proposing legislative reform, known in Australia as "CLERP 9" due to the fact that it is the ninth proposal from the Corporate Law Economic Reform Program, first commenced after the governmental enquiry into the Australian financial services industry undertaken by Mr. Stan Wallis 1997.[22]

CLERP 9

On 18 September, the Australian Treasurer released a discussion paper[23] on corporate disclosure incorporating many of the changes suggested by the Ramsay report and some of the legislative solutions adopted in the United States. A number of the proposals relate to auditor independence and the reliability of the financial reports which they audit (similar to enactments of the *Sarbanes-Oxley Act* in the United States), but there are also a number of developments which are peculiarly Australian.

Accounting/Audit Proposals

The most obvious features of the CLERP 9 proposals are those relating to auditor independence. In order to safeguard the independence of auditors, CLERP 9 proposes the following:

- Expanding the responsibilities of the Financial Reporting Council to oversee the setting of auditing standards, advise on auditor independence, monitor the adequacy of the systems and processes used by audit firms to assure audit independence, promote the teaching of professional and business ethics, monitor the adequacy of disciplinary procedures, and maintain responsibility for the oversight of the accounting standard setting process;[24]
- Including a general statement of principle in the Corporations Act to require auditor independence;[25]
- Requiring auditors to declare annually to the board of directors of an audited company that the auditor has maintained its independence as required by legislation and professional standards;[26]
- Prohibiting a former partner of an audit firm from becoming a director or other responsible officer of the audited company within two years of resignation as auditor; [27]
- Restricting financial relationships (investments and loans) between the auditor and the audit client; [28]
- Requiring immediate application of Professional Standards on Independence requiring the auditor to identify threats to independence and safeguards to be employed. Where non-audit services pose too great a risk to independence, such services would be prohibited;[29]
- Imposing disclosure requirements on non-audit services and requiring explanations of why certain services (preparing accounting records, valuation services, internal audit services, It services, legal services, recruitment services, etc.) do no compromise auditor independence;[30]
- Requiring the top 500 ASX listed companies to have audit committees[31]
- Imposing a requirement that audit partners be rotated after five years; [32]
- Requiring the auditor to attend the AGM to answer questions submitted by members; [33] and
- Streamlining auditor disciplinary procedures. [34]

In order to deal with the issue of auditor liability, CLERP 9 includes proposals to:

- to allow auditors to incorporate;[35] and
- to replace joint and several liability of auditors with proportionate liability. [36]

In addition to the proposals dealing directly with auditors, CLERP 9 also deals with a number of general accounting proposals, including:

- application of international accounting standards; [37]
- requiring the expensing of share options; [38]
- maintaining the requirement that accounts present a "true and fair" view. [39]

General CLERP 9 Proposals

In addition to the proposals intended to impose greater reliability on the accounting and auditing systems, several of the CLERP 9 proposals will assist the proper functioning of the market but may have little direct impact upon corporate governance. For example, a number of the CLERP proposals are intended to assure the independence of those who provide financial analysis. More noteworthy than most of the CLERP proposals have been two which relate to penalties:

- increasing the civil penalty provisions of the Corporations Act to provide a maximum civil penalty for corporate offenders of up to $1 million (from the current $200,000); [40]
- applying penalties for continuous disclosure breaches against individuals involved in the breaches; [41] and
- allowing ASIC to impose an administrative penalty (similar in effect though not in scale to a speeding ticket) which may be paid to avoid court action in relation to the continuous disclosure requirements. [42]

These increases in ASIC powers and in the severity of penalties are undoubtedly intended (as are developments in the United States) to provide a strong message about governmental attitudes to corporate crime.

Finally, CLERP 9 also makes a number of pro-active proposals intended to improve corporate governance in a general sense. These include:

- Requiring shorter and more comprehensive notices; [43]
- Elimination of bundled resolutions to assure member agreement with each matter put to a vote; [44]
- Facilitating electronic meetings and electronic participation;[45]
- Requiring directors to disclose all of their directorships in annual reports; [46] and
- Providing qualified privilege for company employees who report breaches to ASIC. [47]

Although these proposals are less prescriptive than equivalent proposals in the United States, they attempt to achieve similar objects. These proposals have yet to be enacted: however, the response of the business community appears to be positive.

Australian Question: United States or United Kingdom Model

The legal framework of the United Kingdom towards corporate governance has many similarities to that employed in Australia, and has consequently provided a more natural model of comparison than that of the United States. Basic legal obligations (directors' duties, meetings requirements, etc.) are directly regulated by legislation or common law. In addition, the encouragement of best corporate governance principles for publicly listed companies has been based upon the adoption in the 1990s of codes of practice enforced by market pressure through disclosure obligations.

In 1991, the Financial Reporting Council, the Stock Exchange and the Accounting profession set up the Cadbury Committee to report on a code of best practice on corporate governance. In 1992, the Cadbury Committee released its findings and conclusions in the Cadbury Report, accompanying that report with a Code of Best Practice.[48] The Cadbury Report indicated that the primary responsibility for compliance with its Code of Best Practice was with companies themselves.[49] In 1993, the Listing Rules of the London Stock Exchange referred to the Code of Best Practice, and required corporations to indicate whether they had complied with its requirements.[50]

In 1995, the Code was reviewed and revised by the Greenbury Committee. While this committee made of number of recommendations in relation to executive remuneration and shareholder participation, it did not support the use of legislation to enforce these practices upon companies, asserting that companies themselves should take steps to implement its proposals.[51] It did propose, however, that the Code of Practice should be enforced through disclosure required by the listing rules.[52] The London Exchange did so by adding certain of the recommendations as an appendix to its Yellow Book and requiring disclosure of compliance thereto.[53]

In 1998, a Committee on Corporate Governance, Chaired by Sir Ronald Hampel, was established to review and modify the Cadbury and Greenbury Codes. The Hampel Committee took the view that the objective of a code of practice:

> …is not to prescribe corporate behaviour in detail but to secure sufficient disclosure so that investors and others can assess companies' performance and governance practice and respond in an informed way.[54]

Not only did the Hampel Code state principles of corporate governance, but it also detailed specific best practice. Implementation through the London Stock Exchange of the Hampel Code was accomplished through required disclosure of the way in which the principles of corporate governance were applied in general terms and whether there was compliance with the specific principles and a justification of significant variances.[55]

In response to international corporate governance failings in the United States and the regulatory responses which those failings brought about there, the Financial Reporting Council in the United Kingdom released its code of audit practice on January 20. Presented as part of the Smith Report on Audit Independence,[56] the code sets the following requirements of the audit committee:

- that it have a have a minimum of three suitably trained members;
- that it monitor financial statements, review the internal control system and internal audit function; and
- that it makes recommendation about external audit appointments and reviews the independence and non-audit work of the external auditor.

The Smith Report also indicated that that the board of directors should provide the audit committee with sufficient resources to perform its task, even if this involves getting independent advice. The FRC set a consultation period on 12 weeks, and finalised the code on 14 April. Companies will be required to implement the code by 1 July 2003.

In addition to the Smith Report on Audit Practice, the role of independent directors in provision of good corporate governance was subject to consideration by a committee chaired by Derek Higgs. On 20 January 2003, the Higgs review into the use of independent directors was published.[57] The code of practice released as part of that review asserted that directors be appointed as a 'meritocracy' and that the experience in United Kingdom boardrooms be widened. Key findings of the report were that:

- non-executive directors should come from a wider pool of candidates, get more training and take a more important boardroom role;
- at least half of board members should be independent of management;
- the role of chairman and chief executive should remain separate.

These proposals are likely to be implemented and incorporated into the Combined Codes in the United Kingdom in the near future. Although the proposals and the studies supporting them may have influenced Australian developments, much of the Australian work on corporate governance changes had already been well advanced by the release of this material.

ASX Corporate Governance Principles

In March, 2003, the ASX Corporate Governance Council released its report on corporate governance. The report provided ten corporate governance principles and a number of recommendations for implementing those principles. Unlike the requirements found in the United States, the best practice recommendations are not prescriptions. Like the Combined Codes in the United Kingdom, they are guidelines, designed to produce an efficiency, quality or integrity outcomes.

The report of the Corporate Governance Council does not require a "one size fits all" approach to corporate governance. Instead, it provides guidance to best practice for optimising corporate performance and accountability in the interests of shareholders and the broader economy. Like the Combined Codes in the United Kingdom, a company which considers that a recommendation is inappropriate to its particular circumstances has the flexibility not to adopt it – a flexibility tempered by the requirement to explain why.

Companies are encouraged to use the guidance provided by this document as a focus for re-examining their corporate governance practices and to determine whether and to what extent the company may benefit from a change in approach, having regard to the company's particular circumstances. There is little value in a checklist approach to corporate governance that does not focus on the particular needs, strengths and weaknesses of the company.

The Council recognises that the range in size and diversity of companies is significant and that smaller companies may face particular issues in attaining all recommendations from the outset. Performance and effectiveness can be compromised by material change that is not managed sensibly. Where a company is considering widespread structural changes in order to meet best practice, the company is encouraged to prioritise its needs and to set and disclose best practice goals against an indicative timeframe for meeting them.

Under ASX Listing Rule 4.10, companies are required to provide a statement in their annual report disclosing the extent to which they have followed these best practice recommendations in the reporting period. Where companies have not followed all the recommendations, they must identify the recommendations that have not been followed and give reasons for not following them. Annual reporting does not diminish the company's obligation to provide disclosure under ASX Listing Rule 3.1.[58]

The ten broad corporate governance principles and twenty-eight specific recommendations provided by the Corporate Governance Council which a company should, according to the ASX, are as follows:

ASX Corporate Governance Principles

1. Lay solid foundations for management and oversight
   This principle requires companies to recognise and publish the respective roles and responsibilities of board and management.
   Recommendation
   1.1. Formalise and disclose the functions reserved to the board and those delegated to management.

2. Structure the board to add value
   This principle requires companies to have a board of an effective composition, size and commitment to adequately discharge its responsibilities and duties.
   Recommendations
   1.1. A majority of the board should be independent directors.
   1.2. The chairperson should be an independent director.
   1.3. The roles of the chairperson and chief executive officer should not be exercised by the same individual.
   1.4. The board should establish a nomination committee.
   1.5. Provide the information indicated in Guide to reporting on Principle 2, which would require disclosure in the annual report of:
   - the skills, experience and relevant expertise of each director at the date of the annual report;
   - the names of the directors of the board considered to be independent and the materiality thresholds;
   - a statement as to whether there is a procedure agreed by the board for directors to take independent professional advice at the expense of the company;
   - the term of office held by each director in office at the time of the annual report;
   - the names of members of the nomination committee and their attendance at meetings of the committee; and
   - an explanation of any departure from recommendations 2.1 to 2.5;

   A description of the procedure for the selection and appointment of new directors, the charter of the nomination committee (or a summary of its role, rights, responsibilities and membership requirements), and the nominations committee's policy for appointment of directors should be made publicly available, ideally on the company's website.

3. Promote ethical and responsible decision-making
   This principle requires companies to actively promote ethical and responsible decision-making.
   Recommendations
   3.1. Establish a code of conduct to guide the directors, the chief executive officer (or equivalent), the chief financial officer (or equivalent) and any other key executives as to:
   - the practices necessary to maintain confidence in the company's integrity; and
   - the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

   3.2. Disclose the policy concerning trading in company securities by directors, officers and employees.
   3.3. Provide the information indicated in Guide to reporting Principle 3, which would require:
   - an explanation in the annual report of any departure from recommendations 3.1 to 3.5; and
   - an applicable code of conduct or a summary of its main provisions and the trading policy or a summary of its main provisions be made publicly available, ideally on the company's website.

4. Safeguard integrity in financial reporting
   This principle requires companies to have a structure to independently verify and safeguard the integrity of the company's financial reporting.
   Recommendations
   4.1. Require the chief executive officer (or equivalent) and the chief financial officer (or equivalent) to state in writing to the board that the company's financial reports present a true and fair view, in all material respects, of the company's financial conditions and operational results and are in accordance with relevant accounting standards.
   4.2. The board should establish an audit committee.

4.3. Structure the audit committee so that it consists of
- only non-executive directors;
- a majority of independent directors;
- an independent chairperson who is not chairperson of the board;
- at least three members.

4.4. The audit committee should have a formal charter.

4.5. Provide the information indicated in Guide to reporting on Principle 4, which would require disclosure in the annual report of:
- details of the names and qualifications of those appointed to the audit committee (or if no audit committee, those who fulfil that function)
- the number of meetings of the audit committee the names of the attendees; and
- an explanation in the annual report of any departure from recommendations 4.1 to 4.5;

A summary of the audit committee charter and information on procedures for the selection and appointment of the external auditor and of the rotation of external audit engagement partners should be made publicly available, ideally on the company's website.

5. Make timely and balanced disclosure

This principle requires companies to promote timely and balanced disclosure of all material matters concerning the company.

Recommendations

5.1. Establish written policies and procedures designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior management level for that compliance.

5.2. Provide the information indicated in the Guide to reporting on Principle 5, which would require:
- an explanation in the annual report of any departure from recommendations 5.1 to 5.3;
- a summary of the policies and procedures designed to guide compliance with the Listing Rule disclosure requirements be made publicly available, ideally on the company's website.

6. Respect the rights of shareholders

This principle requires companies to respect the rights of shareholders and facilitate the effective exercise of those rights.

Recommendations

6.1. Design and disclose a communication strategy to promote effective communication with shareholders and encourage effective participation at general meetings.

6.2. Request the external auditor to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report.

7. Recognise and manage risk

This principle requires companies to establish a sound system of risk oversight and management and internal control.

Recommendations

7.1. The board or appropriate board committee should establish policies on risk oversight.

7.2. The chief executive officer (or equivalent) and the chief financial officer (or equivalent) should state to the board in writing that:
- the statement given in accordance with best practice recommendation 4.1 (the integrity of financial statements) is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the board; and
- the company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

7.3. Provide the information indicated in the Guide to reporting on Principle 7, which would require:
- an explanation in the annual report of any departure from recommendations 7.1 to 7.3;
- a description of the company's risk management policy and internal compliance and control system be made publicly available, ideally on the company's website.

8. Encourage enhanced performance

This principle requires companies to fairly review and actively encourage enhanced board and management effectiveness.

Recommendation

8.1. Disclose the process for performance evaluation of the board, its committees and individual directors, and key executives.

9. Remunerate fairly and responsibly

This principle requires companies to ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to corporate and individual performance is defined.

Recommendations

9.1.1. Provide disclosure in relation to the company's remuneration policies to enable investors to understand the costs and benefits of those policies and the link between corporate performance and remuneration paid to directors and key executives.

9.1.2. The board should establish a remuneration committee.

9.1.3. Clearly distinguish the structure of non-executive directors' remuneration from that of executives.

9.1.4. Ensure that payment of equity-based executive remuneration is made in accordance with thresholds set in plans approved by shareholders.

9.1.5. Provide the information indicated in the Guide to reporting on Principle 9, which would require disclosure in the annual report of:

- the company's remuneration policy;
- the names of the members of the remuneration committee and their attendance;
- the existence and terms of any scheme for retirement benefits (other than statutory superannuation) for non-executive directors; and
- an explanation of any departure from recommendations 9.1 to 9.5.

The charter for the remuneration committee should be publicly available, ideally on the company's website.

10. Recognise the legitimate interests of stakeholders

This principle requires companies to recognise legal and other obligations to all legitimate stakeholders.

Recommendation

10.1. Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders. (Such a code should be posted on the company's website).

A Convergence of Corporate Governance Principles

The methods which have been adopted in the United States and Australia to assure that good corporate governance occurs are undoubtedly different. The United States now relies upon direct legislation, regulations by its federal regulator (the SEC), and rules imposed by exchanges (as mandated by the legislation or regulation) which have direct effect upon listed corporations. Australia, by contrast, retains a disclosure model which is similar to that of the United Kingdom, with some legislative requirements supplemented by exchange listing rules requiring disclosure of the way each company either complies or does not comply with the Corporate Governance Principles accepted by the exchange (eg. the ASX Principles).

A great deal of recent academic debate has focussed upon the convergence of corporate governance practice throughout the world.[59] While much of the discussion about convergence of international corporate governance principles concerns the application of corporate governance principles designed for application in systems where a dispersed ownership model of corporations predominates into systems in which the concentrated ownership model of corporations predominates,[60] the convergence of corporate governance within the common law world appears to be proceeding apace.

The implications of corporate governance convergence may be significant both for corporations from civil law countries and for world dominant markets, such as the United States; however, these issues are less relevant to Australian based companies. Rather than providing United States-style protections for concentrated ownership firms through cross listing (often characterized as a bonding device or renting of United States law), the Australian response is a more typical application of comparative law convergence. With similar structures, ownership patterns, legal systems and cultures, solutions which prove to be successful in the United States may also prove successful in Australia. Rather than "rent" United States law, Australia has merely implemented modifications to its own laws to enhance protection of investors in its own commercial enterprises. This is consistent with the desired aim of the Australian government to make Australia a provider of financial services which adopts world best practice (including best practice in relation to financial markets and corporate governance). Due to the timing of the Australian changes, one might assert that the Australian response to its corporate governance failures are not derivative or borrowed, but rather are indicative of the fact that similar systems will respond in a similar fashion to the discovery of common weaknesses.

Despite the differences in implementation strategies, the actual principles of corporate governance which have been adopted in the United States and Australia exhibit convergence in the substantial principles which are to be applied. This is not surprising in the context of the United States and Australia in view of the underlying similarities of the commercial and legal systems in these countries.[61] Australian has, however, relied upon developments in the United Kingdom, which has also developed corporate governance concepts with significant common features to those of Australia. The extent of these

similarities can be seen by reference to the following table, which compares the applicable concepts in each of the three countries.

Table of Comparisons
Corporate Governance Developments

	United States	United Kingdom	Australia
Composition of Board of Directors	A majority of the Board is to be independent directors.	The Combined Code currently requires one third of the Board to be non-executive and a majority of those to be independent. The proposed changes will require that at least half the Board be independent.	The ASX Principles require a majority of the Board to be independent directors.
Independence	Board must determine independence of director (and disclose that determination). Director must have no material relationship with company, which includes commercial and professional relationships. Cannot (within the past five years) have been: 1. Director who receives more than $100,000 in direct compensation; 2. Employed by present or former internal or external auditor; 3. Director employed as an executive of another company if executives serve on that other company's compensation committee; 4. A director who is an executive officer of another company that accounts for greater of 2% or $1 mill of gross revenue or to which greater than 2% or $2 mill of gross revenue is provided. Each of the above also applies if an immediate family member is in any of the above classes.	The modified Combined Code will require the board to determine whether a non-executive director is independent and that there are no relationships which would affect or appear to affect the director's judgement, such as: 1. Former employee (within five years); 2. A material business relationship (within three years) either directly or indirectly; 3. Recipient of additional remuneration, participant in share option or performance- related scheme or member of pension scheme; 4. Close family member of company's advisors, directors or senior employees; 5. Holds cross-directorships with other directors; 6. Represents significant shareholder; 7. Director for ten years.	ASX Principles indicate that an independent director: 1. is not a substantial shareholder or associate; 2. was not within the last three years an executive; 3. was not within the last three years a principal of a material professional adviser or consultant (or an employee who provided the service); 4. was not a material supplier or customer (or its officer); 5. has no material contractual relationship; 6. has not served on the board for a period which could materially interfere with the ability to act in the best interests of the company; 7. is free from any interest or other relationship which could materially interfere with the ability to act in the best interests of the company.
Chairman of Board	Currently no obligation to be separate from CEO, but best practice is that they should.	The Combined Code does not currently prevent the Chair and CEO from being the same person, but if so, it should be justified. The proposed changes require that these offices be kept separate.	The ASX principles require the chair to be an independent director.
Key Committees	SEC and NYSE require audit, nomination and compensation committees consisting solely of independent directors.	The Combined Code requires a remuneration committee and a nomination committee with a majority of independent directors and an audit committee consisting solely of independent directors.	The ASX Principles require a nomination committee, a remuneration committee and an audit committee, each with a majority of independent directors..

Certification of Financial Reports	CFOs and CEOs to certify that SEC report does not contain any untrue statement or omission of material fact and "fairly present" financial position, etc.	There is no equivalent requirement in the United Kingdom	CLERP 9 will require CFOs and CEOs to certify to board that accounts present a "true and fair" view
Public Company Audit Committees	The audit committee of public companies must: be responsible for the appointment, compensation and oversight of auditors; be composed of independent members of the board of directors; establish procedures for treatment of accounting complaints; have authority and funding to engage independent advisors. Required to approve accounts and meet separately with auditors.	An audit committee, consisting of at least three non-executive directors, all of whom should be independent, is required under proposed changes to the Combined Code. Its duties include monitoring the integrity of the financial reporting system; reviewing the company's internal financial control and (unless there is a risk committee) risk management system; reviewing the scope, results and cost effectiveness of the audit; monitoring the independence and objectivity of the auditors; and reviewing non-audit services provided by the auditors.	The ASX Principles require an audit committee consisting of at least three non-executive directors, a majority of which should be independent. It should have an independent chairperson who is not chairperson of the board. Its duties include reviewing the scope, results and cost effectiveness of the audit; the independence and objectivity of the auditors; and reviewing non-audit services provided by the auditors. It does not approve accounts (done by board). CLERP 9 will require audit committee for ASX top 500.
Loans to Directors/Executives and other related party transactions	Personal loans, with some exceptions, may not be given by a public company to directors and executives of that company	A public company is restricted from making or guaranteeing a loan to directors and persons connected with them unless exempted under the ss. 332-338 of the *Companies Act.*	A public company must obtain member approval for loans to a related party unless permitted under the exceptions (eg. arms length terms) in ch. 2E of the *Corporations Act.*
Financial Expert Disclosure	A public company is required to disclose whether its audit committee consists of at least one member who is a 'financial expert.' The NYSE indicates that the chair of the audit committee must have accounting or financial management expertise.	The Combined Code requires members of the audit committee to be named in the financial report and accounts. The proposed changes recommend the audit committee has at least three suitably trained members and at least one member of the audit committee have significant, recent and relevant financial experience.	The ASX Principles require disclosure of the names and qualifications of audit committee members. It is recommended that at least one member of an audit committee has accounting or related financial expertise.
Insider Trading Disclosure	Officers, directors and 10% shareholders are required to report changes in ownership of securities or the purchase/sale of a security-based swap agreement.	Directors, 3% shareholders with a material interest and 10% shareholders without a material interest must notify the company in writing of changes in ownership of securities under the *Companies Act*. The company must notify a Regulatory Information Service of the change.	Substantial shareholders (5% shareholding or more) must comply with the notice provisions in Part 6C.1 of the *Corporations Act*. Listed companies are required to notify the ASX of directors' holdings. The ASX principles require formulation and disclosure of policy concerning trading in company securities by directors, officers and employees.
Assessment of Internal Control	An 'internal control report' must be filed annually which states the responsibilities of management for establishing and maintaining internal control.	The Combined Code states that the directors should conduct at least annually a review of the effectiveness of the internal control system and report to shareholders that they have done so.	The ASX Principles require companies to establish a sound system of risk oversight and management and internal control.

Code of Ethics	Public companies must disclose in periodic reports whether or not they have adopted a code of ethics for senior financial officers.	The Combined Code has no requirement of this nature.	The ASX Principles require a code of conduct for the directors, the chief executive officer, the chief financial officer, and any other key executives as to the practices necessary to maintain confidence in the company's integrity; and the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.
Securities based remuneration Bonuses, etc. to CEO, CFO	To be approved by shareholders. CEOs and CFOs of public companies must forfeit any bonuses and profits received by them from the sale of company securities during the 12 month period following the filing of a financial report, where an accounting restatement was required for misconduct with reporting requirements. Bonuses to be expensed.	The Combined Code, as modified, indicates that shares granted or other forms of deferred remuneration should not vest within three years. New long term schemes should be subject to shareholder approval and should be conditioned upon challenging performance criteria. Such remuneration should not be excessive. Disclosure of the remuneration policy should be disclosed by the board in the annual report to shareholders.	The ASX Principles require disclosure in relation to the company's remuneration policies to enable investors to understand the costs and benefits of those policies and the link between corporate performance and remuneration paid to directors and key executives and to ensure that payment of equity-based executive remuneration is made in accordance with plans approved by shareholders. Unreasonable bonuses will be covered by new legislation. Bonuses to be expensed.
Disqualification of Directors, Officers	SEC may prohibit any person from serving as an officer or director if they have violated certain anti-fraud provisions and their conduct demonstrates 'unfitness' to serve.	Under the *Company Directors Disqualification Act*, a court may make an order to bar a person from being a director of a company for 5-15 years for general misconduct in connection with companies and for unfitness. (ss. 2 – 12).	A person can be disqualified under Part 2D.6 of the *Corporations Act* from managing corporations for convictions; for certain serious offences; for involvement in failed corporations; for undischarged bankruptcy; and repeated contraventions of the *Corporations Act.*
Civil Penalties	Civil penalties from SEC enforcement actions will be diverted to accounts to compensate victims of related securities law violations.	Under the *Financial Services and Markets Act* the FSA must prepare a scheme for ensuring that the amounts paid to the Authority by way of penalties imposed under the Act are applied for the benefit of issuers of securities admitted to the official list.	CLERP 9 will alter the civil penalty provisions (Pt 9.4) of the *Corporations Act* to provide a maximum civil penalty for corporate offenders of up to $1 million (from the current $200,000). Compensation for losses may already be provided.
Periodic Disclosure	Companies lodging periodic reports with the SEC must disclose all material off-balance sheet transactions and factors.	As required by accounting standards, generally annually.	Periodic reports (quarterly or semi-annual) providing a "true and fair view" of financial position already required by the ASX Listing Rules and *Corporations Act*.
Continuous Disclosure	Each reporting public company must disclose to the public on a 'rapid and current basis' any additional information concerning material changes in its financial condition which is necessary or useful for the protection of investors and is in the public interest.	A listed company must, under the Rules, notify a Regulatory Information Service of any major new developments which may lead to substantial changes in share price 'without delay'.	The ASX listing rules require that a listed company inform the ASX 'immediately' if it becomes aware of information which a reasonable person would expect to have an effect on the price or value of its securities. Certain unlisted companies must inform ASIC in similar circumstances.

Prohibited Services	Registered accounting firms are prohibited from providing non-auditing services contemporaneously with an audit' unless the services are not forbidden by the Act and are pre-approved by audit committees. Firms may provide non-auditing services to a company if the services do not exceed 5% of the total fees paid by the company to the auditor during the year.	The Combined Code indicates that where the auditors supply a substantial volume of non-audit services, the nature and extent of such services shall be kept under review seeking to balance the maintenance of objectivity and the value for money. The proposed changes to the Combined Code recommends that the audit committee develop and implement policy on the engagement of the external auditor to supply non-audit services.	CLERP 9 will apply Professional Standards on Independence requiring the auditor to identify threats to independence and safeguards to be employed. Where non-audit services pose too great a risk to independence, such services would be prohibited. CLERP 9 will also impose disclosure requirements on non-audit services and require explanations of why certain services do no compromise auditor independence.
Audit waiting period	A registered public accounting firm may not audit a public company if: a senior finance executive of the company was employed by the firm; and that person participated in the audit of the company during the preceding year.	The external auditor of a listed company must provide the audit committee (at least annually) with a written statement about the firm's independence and the objectivity of the audit partner and staff. The proposed changes to the Combined Code specify that the audit committee monitor and review the external auditor's independence, objectivity and effectiveness.	CLERP 9 will prohibit a former partner of an audit firm from becoming a director or other responsible officer of the audited company within two years of resignation as auditor.
Audit rotation	A registered public accounting firm may not audit a public company if the lead audit partner or partner responsible for reviewing the audit has performed audit services for the company in each of the 5 previous financial years.	Shareholders are required to appoint auditors annually and the Combined Code requires the audit committee to constantly review the independence of the auditor.	CLERP 9 will require audit partners to be rotated every five years.
Audit record retention	Auditors must retain all audit and review work papers for at least 7 years.	No direct requirement. Reports to be lodged at annual meeting. Professional standards apply to auditor.	No direct requirement. Reports to be lodged at annual meeting and contraventions reported to ASIC under *Corporations Act*. Professional standards apply to auditor.
Audit influence	An officer or director of a public company Is prohibited from fraudulently influencing, or coercing, any independent public auditor that is performing an audit on the company.	The Combined Code requires the audit committee to keep under review the objectivity and independence of the auditor.	CLERP 9 will insert a general statement of principle in the Corporations Act to require auditor independence; it will require auditors to declare annually to the board of directors of an audited company that the auditor has maintained its independence as required by legislation and professional standards; it will restrict financial relationships between the auditor and the audit client; and will immediately apply the Professional Standards on Independence requiring the auditor to identify threats to independence and safeguards to be employed.

Audit reports	Registered public accounting firms are required to make timely reports to the audit committee on matters including critical accounting policies and practices to be used.	The audit committee is required under the Combined Code to keep under review the scope and results of the audit.	Audit committee should report to the board whether external reporting is consistent with members' knowledge and is adequate for shareholder needs. Auditor must report *Corporations Act* contraventions to ASIC.
Accounting oversight	A five-member board independent of the accounting profession and overseen by the SEC will set auditing, quality control and independence standards.	Accounting standards are issued by the Auditing Practices Board, part of the Accountancy Foundation which is independent of the accountancy profession	CLERP 9 will expand the responsibilities of the Financial Reporting Council to oversee the setting of auditing standards, advise on auditor independence, monitor the adequacy of the systems and processes used by audit firms to assure audit independence, promote the teaching of professional and business ethics, and monitor the adequacy of disciplinary procedures.
Accounting standards	An 'accounting standard setting body' will establish accounting principles and procedures with consideration of emerging accounting issues	The Accounting Standards Board (ASB) is a private body run by a board appointed by the Financial Reporting Council (FRC). The ASB issues principle-based accounting standards. With the application of the *International Accounting Standards* (IAS) by 2005, affected companies will have to prepare their consolidated accounts on the basis of accounting standards issued by the International Accounting Standards Board.	CLERP 9 will maintain the responsibility of the Financial Reporting Council for the oversight of the accounting standard setting process. *International Accounting Standards* (IAS) are to apply.

Conclusion: Where to from here?

This review of the legal framework of corporate governance in the United States and Australia reveals a number of things. Perhaps the primary lesson from events of the last few years indicate is that best practice in good corporate governance transcends international boundaries. Each of United States and Australia impose basic corporate governance requirements through their legislation and common law. The exact method by which these legal requirements are imposed differs slightly between these countries due in part to constitutional differences; however, the essential nature of corporation and the legal system in each of these countries means that similar basic obligations and legal strategies occur for all corporate entities (no matter what size). The common law systems provide similar approaches to such issues as corporate structures; membership participation; transparency of procedures; directors' duties and accountability; and (to a lesser extent) members' remedies. These commonalities mean that corporate governance concepts are likely to be as effective in Australia as in the United States.

Because Australia and the United States have seen similar commercial development and uses of corporate entities (as congregators of capital), each has relied upon regulation of the capital markets to impose further corporate governance requirements in order to access the capital markets (through the listing rules of the ASX or the various American exchanges). The contractual obligations which require particular corporate governance practices are often complemented by legislation or regulation giving legislative or semi-legislative effect to the requirements. In Australia, the method of implementation is similar to the Combined Codes used in the United Kingdom.

In addition to direct requirements, corporate governance principles of best practice have developed as a result of legal and non-legal study of corporate dynamics. Such things as audit committees, selection committees, remuneration committees, reliance upon independent directors have evolved as a means of assuring proper governance without legal

prescription. The imposition of full disclosure of these practices from the pressure of institutional investors or market listing rules aligns market demand for good corporate governance with perceptions of the practice of particular corporations.

While best corporate governance practice may not be truly of universal application (for there are some differences in societies, legal cultures, and corporate structures), in the common law world there is a convergence of thought on many of the best corporate governance practices which should be employed. As these practices become more generally accepted, they appear to migrate from less prescriptive legal form ('best practice" disclosed to the market) to more prescriptive legal form (directly required by a listing rule or, ultimately, required by statute). The events of the last year have seen corporate governance best practice in relation to audit move in such a way in the United States. Australian developments have yet to be imposed in such a prescriptive way; however, the greater specificity in disclosure obligations indicates that greater compulsion could eventuate.

Footnotes

[1] *Public Company Accounting Reform and Investor Protection Act of 2002.* PL 107-207 (HR 3763) Title 8 (the '*Sarbanes-Oxley Act'*).
[2] David Knott, *Corporate Governance Principles Promotion and Practice* (16 July 2002) which can be found at: http://www.asic.gov.au/asic/asic.nsf/lkuppdf/ASIC+PDFW?opendocument&key=Monash_spch_160702_pdf
[3] Report of the Permanent Subcommittee of Investigations to the Senate Governmental Affairs Committee (S. Prt. 107-70) (July 8, 2002), *The Role of the Board of Directors in Enron's Collapse*. Also found at http://www.gpo.gov/congress/senate/senate12lp107.html. See also Larry Ribstein, *Market v. Regulatory Responses to Corporate Fraud: A Critique of Sarbanes-Oxley Act 2002,* 28 IOWA J. CORP. L. 1 (2002)
[4] See Jennifer Recine, *Examination of the White Collar Crime Penalty Enhancements in the Sarbanes-Oxley Act,* 39 AM. CRIM. L. REV. 1535 (2002).
[5] The *Sarbanes-Oxley Act,* Title I.
[6] *Id*. Title II.
[7] *Id.* Title III.
[8] *Id*. Title IV.
[9] *Id*. § 302.
[10] *Id*. Title V.
[11] *Id*. Title VIII
[12] *Id*. Titles IX, XI.
[13] *Id*.§§ 403, 404.
[14] The substance of these proposals can be found at: http://www.nyse.com/about/1045516490394.html.
[15] As of April 2001, over 970 non-U.S. firms were listed on the NYSE, Nasdaq, or the Amex. See J C Coffee, *Racing towards the Top? The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance* 102 COLUM. L. REV. 1757 (2002) fn 43. Eleven Australian companies were listed on the NYSE as at December 31, 2003. See http://www.nyse.com/pdfs/forlist030512.pdf. On May 27, 2003, there were ten Australian companies listed on the Nasdaq. See http://www.nasdaq.com/asp/NonUsOutput.asp?page=A&previousCount=0&region=asia.
[16] HIH Royal Commission (Justice Neville Owen), REPORT OF THE HIH ROYAL COMMISSION (2003) pp. viii. Also found at: http://www.hihroyalcom.gov.au/finalreport/Front%20Matter,%20critical%20assessment%20and%20summary.HTML#_Toc37086537. See also, P. Lipton, *The Demise of HIH: Corporate Governance Lessons* (forthcoming in KEEPING GOOD COMPANY), available at: http://www.australian-corporate-governance.com.au/hih_royal_commission.pdf.
[17] F. CLARKE, G. DEAN AND K. OLIVER, CORPORATE COLLAPSE: ACCOUNTING, REGULATORY AND ETHICAL FAILURE (CUP, 2003).
[18] Ian Ramsay, INDEPENDENCE OF AUSTRALIAN COMPANY AUDITORS: REVIEW OF CURRENT AUSTRALIAN REQUIREMENTS AND PROPOSALS FOR REFORM (October, 2001 and reprinted March 2002)(the "Ramsay Report").
[19] These are found in Parts 4-6 of the Ramsay Report.
[20] R. Humphry, *Corporate Governance Council to Broaden Disclosure* (1 August 2002), found at http://www.asx.com.au/shareholder/pdf/CorpGovCouncil010802.pdf. Contrast this to R Humphry, *ASX Business is Market Integrity* (24 July 2002), at http://www.asx.com.au/shareholder/pdf/RGH240702.pdf.
[21] These included the following:

- Association of Superannuation Funds of Australia Ltd
- Australasian Investor Relations Association
- Australian Council of Superannuation Investors
- Australian Institute of Company Directors
- Australian Institute of Superannuation Trustees

- Australian Shareholders' Association
- Australian Stock Exchange Limited
- Business Council of Australia
- Chartered Secretaries Australia
- CPA Australia
- Group of 100
- Institute of Actuaries of Australia
- Institute of Chartered Accountants in Australia
- Institute of Internal Auditors Australia
- International Banks and Securities Association of Australia
- Investment and Financial Services Association
- Law Council of Australia
- National Institute of Accountants
- Property Council of Australia
- Securities & Derivatives Industry Association; and
- Securities Institute of Australia

[22] Wallis S. (Ch.), FINANCIAL SYSTEM INQUIRY FINAL REPORT (Canberra, AGPS, 1997) (the 'Wallis Report').
[23] CORPORATE DISCLOSURE: STRENGTHENING THE FINANCIAL REPORTING FRAMEWORK (Commonwealth of Australia 2002) ('CLERP 9').
[24] *Id*. Proposal 1.
[25] *Id*. Proposal 2.
[26] *Id*. Proposal 3.
[27] *Id*. Proposal 4.
[28] *Id*. Proposal 5.
[29] *Id*. Proposal 6.
[30] *Id*. Proposal 7.
[31] *Id*. Proposal 8.
[32] *Id*. Proposal 9.
[33] *Id*. Proposal 10.
[34] *Id*. Proposal 34
[35] *Id*. Proposal 12.
[36] *Id*. Proposal 13.
[37] *Id*. Proposal 14.
[38] *Id*. Proposal 15.
[39] *Id*. Proposal 16.
[40] *Id*. Proposal 21.
[41] *Id*. Proposal 23.
[42] *Id*. Proposal 24.
[43] *Id*. Proposal 37.
[44] *Id*. Proposal 38.
[45] *Id*. Proposal 39.
[46] *Id*. Proposal 40.
[47] *Id*. Proposal 35.
[48] Committee on the Financial Aspects of Corporate Governance (Sir Adrian Cadbury, Chair), REPORT OF THE COMMITTEE ON THE FINANCIAL ASPECTS OF CORPORATE GOVERNANCE (Gee Publishing, 1992) (the 'Cadbury Report').
[49] Cadbury Report Para. 3.14.
[50] The London Stock Exchange Listing Rules Para 12.43(j) (deleted in January 1999)
[51] DIRECTORS REMUNERATION: REPORT OF A STUDY GROUP CHAIRED BY SIR RICHARD GREENBURY (Gee Publishing, 1995) (the 'Greenbury Report') Para. 1.13, 1.14.
[52] The Greenbury Report Para. 1.19, 3.3.
[53] The London Stock Exchange Listing Rules Para 12.43(w), (x) (1999).
[54] Committee on Corporate Governance (Sir Ronald Hampel, Chair), COMMITTEE ON CORPORATE GOVERNANCE: FINAL REPORT (Gee Publishing, 1998) (the 'Hampel Report") Para. 1.25.
[55] The London Stock Exchange Listing Rules Para 12.43A (1999).
[56] Sir Robert Smith, REVIEW ON COMBINED CODE GUIDANCE FOR AUDIT COMMITTEES (Financial Reporting Council,2003)
[57] D Higgs, REVIEW OF THE ROLE AND EFFECTIVENESS OF NON-EXECUTIVE DIRECTORS (U.K. Stationary Office 2003)
[58] This listing rule states:

> Once an entity is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities, the entity must immediately tell the ASX that information.

[59] L A Bebchuk and M J Rowe, *A Theory of Path Dependence In Corporate Ownership and Governance* 52 STAN. L REV. 127 (1999); A N Licht, *The Mother of All Path Dependencies Toward a Cross-Cultural Theory of Corporate Governance Systems* 26 DEL. J OF CORP L 147 (2001); L E Ribstein *Politics, Adaptation and Change* 8 AUSTL. J. OF CORP L 246 (1998); J Farrar, *In Pursuit of an Appropriate Theoretical perspective and Methodology for Comparative Corporate Governance* 13 AUSTL J OF CORP L 1 (2001); and R Romano, *A Cautionary Note on Drawing Lessons from Comparative Corporate* Law 102 YALE L J 2021 (1993).

[60] This distinction roughly coincides with the civil/common law divide. See P G Maloney, *The Common Law and Economic Growth: Hayek Might be Right* 30 J LEG STUD. 503 (2001). This is, of course, a generalization, and major differences in cultural and ownership concentration exist among such common law jurisdictions with Hong Kong, Malaysia and Singapore exhibiting different patterns from Australia, the United States and the United Kingdom See also Rafael La Porta, Francisco Lopez-de-Silanes, Andrei Shleifer and Robert Vishny, *Corporate Ownership Around the World,* 54 J. FIN. 471 (1999).

[61] See J. Hill, *Visions and Revisions of the Shareholder*, 48 AM. J. COMP. L. 39 (2000); J Farrar, *In Pursuit of an Appropriate Theoretical perspective and Methodology for Comparative Corporate Governance* 13 AUSTL J OF CORP L 1 (2001).