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NZX Limited

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Submission on NZX Corporate Governance Code Review 2021

The Institute of Directors (IoD) appreciates the opportunity to comment on NZX's review of its Corporate Governance Code (the NZX Code) as outlined in its initial [discussion document](#).

Summary of IoD submission

The IoD welcomes the review of the NZX Code to ensure it is current, effective for good corporate governance reporting and aligned with best practice. The IoD submitted on the first review of the NZX Code in [2016](#) and subsequently in [2018](#).

The IoD's supports the review and the proposed areas of reform. Our submission comments on a number of points raised in the consultation document:

- The IoD supports the 'comply or explain' approach to implementing the Code. It's important to keep the Code as simple as possible to ensure that it remains effective as a way of encouraging greater uptake of governance best practice amongst listed companies. The Code's recommendations should drive strategic thinking and change within organisations while providing meaningful disclosure to owners and stakeholders. The reporting requirements should align with other codes and practices issued by standard-setters and regulators, including the incoming climate disclosure standards issued by the External Reporting Board (XRB). We encourage NZX to work closely with the XRB to ensure NZX guidance is consistent and aligned with the work the XRB is doing.
- The review should take into account global trends around growing awareness of an entity's social license to operate and the expectation that the needs of stakeholders and society at large receive greater attention
- The IoD considers the end goal of board diversity is diversity of thought and capability. Board diversity brings a broader range of skill and experienced perspectives to the boardroom and increases the potential for success, effective risk oversight and long-term business sustainability. The IoD is committed to supporting diversity on boards and we are actively doing this through our Future Directors and Mentoring for Diversity programmes. We continue to support boards setting and reporting on diversity targets. Some boards may also wish to add an additional director or Future Director to their board.
- The IoD supports the establishment of the proposed NZX Corporate Governance Institute and we would welcome the opportunity to contribute to the Institute, including in respect of contributing governance expertise as well as being a conduit for the IoD's members.

About the Institute of Directors

The IoD has over 10,000 members and is New Zealand's pre-eminent organisation for directors and is at the heart of the governance community. We believe in the power of governance to create a strong, fair and sustainable future for New Zealand. Our role is to drive excellence and high standards in governance. We support and equip our members who lead a range of organisations from listed companies, large private organisations, state and public sector entities, small and medium enterprises, not-for-profit organisations and charities.

The IoD's Code of Practice for Directors (IoD's Code) provides guidance to directors to assist them in carrying out their duties and responsibilities with professional standards. All IoD members must sign up to the Code. Our Chartered Membership pathway aims to raise the bar for director professionalism in New Zealand, including through continuing professional development requirements.

Overview of NZX's Corporate Governance Code Review

The NZX Corporate Governance Code (Code) provides NZX issuers with guidance on NZX's expectations in relation to corporate governance practices. NZX's Listing Rules require issuers to publicly report the extent to which the issuer has followed the recommendations set out in the Code on a 'comply or explain' basis.

The settings for the Code were last amended in 2018 as part of a holistic Listing Rule review and NZX is now reviewing certain settings within the NZX Corporate Governance Code to assess their effectiveness.

The initial discussion document seeks feedback in relation to the scope of the matters that NZX has identified for inclusion in the review, which will be used as a basis from which to develop more detailed proposals for a second round of consultation in early 2022. We note NZX will be sample testing issuers' disclosure practices in relation to the 2018 Code and we look forward to seeing the insights from this analysis.

NZX has identified the following objectives for the review:

- Undertake a targeted review of issuers' reporting practices, and certain aspects of the settings of the Code, now that issuers have completed three reporting cycles using the settings that were implemented in 2018
- Facilitate the successful operation of New Zealand's capital markets by enabling issuers to access capital on a competitive basis, through settings that deliver appropriate costs of capital
- Ensure that the Code's settings enable access for investors and other stakeholders to information about issuers' corporate governance practices to facilitate efficient allocation of capital; and
- Promote good governance practices that support the generation of long-term benefits for issuers' shareholders and other stakeholders, and contribute to a sustainable and productive economy for New Zealand.

The review is also intended to promote the confident and informed participation of businesses, investors and consumers in the financial markets and be consistent with the other purposes of the Financial Markets Conduct Act 2013.

NZX has indicated that following a second round of consultation in early 2022, the final Code amendments are scheduled to be finalised and made effective in the latter half of 2022.

IoD commentary

General comments and specific comments on review areas

The IoD welcomes the NZX's initiative to revise the NZX Corporate Governance Code to ensure it is fit for purpose, and up to date with developments and trends in corporate governance.

Good governance focuses on adherence to relevant codes and principles, with a clear understanding of roles, relationships and accountabilities of the key stakeholders of an organisation. The corporate governance landscape continues to change and the NZX Corporate Governance Code plays an important part in improving corporate governance in New Zealand and assisting directors in carrying out their roles and responsibilities.

We generally support NZX's approach to the review and the proposed areas of reform. We look forward to seeing the results of the sample testing of issuers' disclosure practices and how this will inform the Code review.

It's important that disclosures are clear, useful and meaningful, and we therefore support keeping the Code as simple as possible. Having a large number of requirements can reduce the effectiveness of the Code, for example, by creating a culture of tick-box compliance. It also wouldn't be helpful to see a code with recommendations that weren't being used.

Consistency in corporate reporting is important to the market, issuers operating in New Zealand and other markets, shareholders and stakeholders. We encourage ensuring that any amendments align with other standard-setters and regulators. The Code needs to fit within the wider reporting framework, both in New Zealand and with other major trading partners, for example, by ensuring alignment and using consistent language/terminology as other guidance and standard where appropriate.

We note that although the ASX Corporate Governance Principles and Recommendations go beyond those in the NZX Corporate Governance Code, New Zealand entities can still choose to adopt the ASX standards on a voluntary basis as part of good corporate governance.

We commented in 2016 that we were concerned that the proposed amendments to the Code diluted the importance of stakeholder interests and ran contrary to global trends where stakeholder interests were receiving increasing attention in corporate governance.

We are in an environment now where there is even greater public awareness around an entity's social licence to operate. To succeed in the long-term, directors and the companies they lead need to build and maintain successful relationships with a wide range of stakeholders. Effective stakeholder engagement is fundamental to good governance in the modern age.

A whitepaper published in 2021 by the IoD and MinterEllisonRuddWatts [Stakeholder Governance: A call to review directors' duties](#) outlines the evolving corporate governance landscape in relation to stakeholders. It includes significant developments and trends around the world and in New Zealand, relevant law in New Zealand and also provides guidance for boards.

Review Area One: 'Comply or Explain'

We continue to support a 'comply or explain' approach to implementing the Code. Such an approach supports good governance and provides flexibility and proportionality for organisations to report in a way that is appropriate, relevant and meaningful to their circumstances. For 'comply or explain' to work effectively, there needs to be genuine commitment to good governance and meaningful, open explanations. A constructive culture needs to be fostered where explanations are assessed on their merit rather than assuming

non-compliance is inherently negative. Explaining why the entity has not complied and providing sound reasons for why not is important for transparent corporate reporting.

Review Area Two: Director Independence

Benefits to appointing independent directors include a fresh and independent viewpoint on issues before the board. For example, the ability to access specific expertise, experience, networks and relationships with other organisations.

The Listing Rules define an 'Independent Director' as a director who has no 'Disqualifying Relationship'. 'Disqualifying Relationship' is defined as any director or indirect interest, position, association or relationship that could reasonably influence, or could reasonably be perceived to influence, in a material way, the director's capacity to: (a) bring an independent view to decisions in relation to the issuer, (b) act in the best interests of the issuer, and (c) represent the interests of the issuer's financial product holders generally. The Code then notes a number of factors that may impact on a director's independence.

We agree with these current settings for determining the independence of directors under the NZX Listing Rules and the Code.

NZX is interested in the extent to which tenure should be regarded as a fetter on director independence. The IoD makes no firm recommendation on what is an appropriate mandatory retirement age or length of service (other than as a result of rotation) and how it may affect a determination of independence. However, it is important that boards ensure sufficient independence on the board as a whole, while balancing the need for wisdom from time with the business and bringing in new skills and expertise for evolving needs.

Review Area Three: Remuneration

Consistent and open reporting on director and officer remuneration helps build trust and confidence in corporate governance. Director and officer pay is increasingly in the spotlight and boards can continue to expect greater scrutiny and heightened debate about levels of remuneration and corporate income disparities.

We support clear and transparent reporting of organisations' remuneration policies and procedures, including the reasoning behind the approach to remuneration paid to directors and senior executives. For example executive remuneration policies should explain how the remuneration practice supports company strategy and performance.

Expectations of institutional investors and the public are continuing to increase and it is important that companies look to meet these expectations by considering other opportunities for transparency such as reporting on diversity or pay gap matters.

Reporting director remuneration

In 2017 the IoD, with input from members who were experienced listed company directors, developed a [Guide to Disclosing Director Remuneration in Annual Reports](#). The guide aims to support transparent and consistent disclosure of director remuneration. The framework includes disclosing details on all board and committee fees received, plus any other benefits or payments received and associated explanations.

The Financial Markets Authority references the IoD guide in their Corporate Governance Handbook. We encourage the NZX to reference it in its Code to aid consistent and transparent disclosure of director remuneration.

Review Area Four: Shareholder meetings

Sound corporate governance holds shareholder participation as a key factor in successful shareholder meetings. Shareholders must be able engage with the board and attend and vote at shareholder meetings on an equal basis to maintain the integrity of corporate governance in New Zealand. Traditionally this has been through being physically present at

meetings but this has now extended to virtual meetings, particularly over the last two years due to pandemic restrictions.

We are supportive of NZX's proposal to prefer hybrid meetings over physical meetings. Offering virtual meetings allows for greater attendance and by promoting hybrid meetings, which by definition include a physical meeting, shareholder participation is encouraged by whatever form of engagement suits them best.

Review Area Six: Environmental, Social and Governance Reporting

Transparent and clear reporting on financial and non-financial information, including on environmental, social and governance (ESG) matters is critical to building and maintaining trust and confidence in corporate governance and financial markets.

It is vital that reporting is useful and meaningful, and goes beyond compliance, to help drive strategic thinking and performance. One of the challenges for listed companies is the myriad of reporting expectations and frameworks. It's essential that there is as much as alignment as possible, in particular with any mandatory requirements such as the incoming climate disclosure standards.

In October 2021 the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill passed into law, broadening non-financial reporting by requiring certain 'climate reporting entities' to make climate-related disclosures. This includes all NZX issuers, other than issuers with a market capitalisation of \$60 million or less. Reporting will be made against reporting standards issued by the External Reporting Board (XRB) and will be aligned with the recommendations of the Taskforce on Climate-Related Financial Disclosures (TCFD).

XRB is currently consulting in stages on the development of the climate standards and expects to issue a final standard in December 2022, to apply to financial years beginning in 2023, so reporting in 2024.

As noted in the discussion document there has been a steady increase in voluntary reporting on climate and ESG related matters. IoD research also supports this. In our *2021 Director Sentiment Survey* 68% of respondents of publicly listed companies (up from 42% in 2020) said that their latest annual report included disclosures on climate-related risks and/or the impact of climate change on their organisation.

Although reporting has increased, because it has evolved voluntarily and against a range of frameworks, for example, to meet investor and other stakeholder expectations, there is a significant range of reported information, and also of organisational reporting maturity and capability. Cohesive and consistent guidance is therefore even more important.

We also note the XRB's new mandate is broader than climate changes and extends to issuing guidance on ESG matters. We encourage NZX to work closely with the XRB to ensure NZX guidance is consistent and aligned with the work the XRB is doing.

Review Area Seven: Diversity Practices

The IoD has long held that the real goal of board diversity is diversity of thought and capability. Board diversity brings a broader range of skills and experienced perspectives to the boardroom and increases the potential for success, effective risk oversight and long-term business sustainability.

We note the NZX discussion document refers to various diversity practices in other jurisdictions. In 2021 the UK's Financial Reporting Council published a report on [Board Diversity and Effectiveness in FTSE350](#). The research highlights that it is the responsibility of the board to drive inclusion. It highlights that in order to maximise the benefits of diversity, the board should recognise that change takes time and that diversity without inclusion is

unlikely to encourage new talent to the board. Additionally the research identifies that diversity, over time, improves the performance of boards and the businesses they lead.

The IoD's guide [Getting on Board with Diversity](#) was first published in 2016. It provides practical steps to help boards improve board capability, attract and retain the best talent, and lead an inclusive culture that lets diverse thinking thrive. It also encourages boards to set targets, for example, between 30 to 50 percent for women on their board. Setting transparent board targets are important as they help drive change through driving accountability and actions for progress.

The New Zealand public sector is making good progress against its targets. Manatū Wāhine Ministry for Women's [2020 Stocktake of Gender, Maori, Pacific, and Ethnic Diversity on public sector boards and committees](#) shows that the Government achieved its 50 percent target of women on state sector boards and committees in 2020 (one year earlier than planned) after setting its target in 2018. The Government was also able to report on the ethnic makeup of New Zealand's sector boards and committee. While there is still much work to do, the report shows that appointments to boards are becoming more diverse.

NZX's latest report on [Gender Diversity Statistics](#) (for the year to September 2020) shows that there were 22.5% female directors on all NZX issuers, and 31.6% female directors for S&P/NZX 50 companies. Although this is up on 12% first reported in 2013, it is still very slow progress.

The IoD is committed to supporting diversity on boards including through our [Future Directors](#) and [Mentoring for Diversity](#) programmes. We also continue to support that boards set and report on diversity targets (for example, a gender target of between 30 and 50 percent). Shifting the dial on board diversity can take a long time, especially for smaller boards. To help enable more diversity some boards may wish to consider adding an additional director or Future Director to their board.

Review Area Eight: NZX Corporate Governance Institute

The IoD has been a long standing supporter of establishing an NZX Corporate Governance Institute, supporting the concept in 2016, and we would welcome the opportunity to contribute to the Institute.

The IoD is New Zealand's pre-eminent director organisation, with over 10,000 members and is committed to raising corporate governance standards in New Zealand. This includes in publicly listed companies, for example, by training directors in the Company Directors Course, raising standards through the Chartered Membership pathway and supporting directors through our programmes such as Mentoring for Diversity and Future Directors.

A significant proportion of New Zealand based NZX directors are members of the IoD, including:

- 78% of NZX 50 directors and 70% of NZX 100 directors
- 92% of NZX 50 chairs and 88% of NZX 100 chairs

The IoD would bring significant value to the Institute in respect of contributing governance expertise and as a conduit for our members. We are also at the forefront of global governance developments including through our membership of the Global Network of Director Institutes. We also note the Australian Institute of Company Directors is a member of the Australian Securities Exchange (ASX) Corporate Governance Council.

Conclusion

The NZX Corporate Governance Code plays an important part in improving corporate governance in New Zealand and assisting directors in carrying out their roles and responsibilities. We support the review of the Code to help ensure its efficacy and impact on good corporate governance practices.

A successful review should result in a Code that aligns with global and local trends in governance best practice, drives strategic thinking and change and provides for a greater level of meaningful disclosure to owners and stakeholders. It's therefore important to get the settings right and ensure the requirements are not overly burdensome while ensuring sufficient guidance and encouragement for improvement is provided.

We appreciate the opportunity to comment on behalf of our members, and we would be happy to discuss our submission and the review more broadly as it progresses.

Yours sincerely,



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