

28 November 2023

Guy Beatson
General Manager, Governance Leadership Centre
Email: guy.beatson@iod.org.nz

cc: Kirsten Patterson, Chief Executive

RE: OECD Principles

Dear Guy,

At the previous quarterly meeting between the Institute of Directors (**IOD**) and the New Zealand Corporate Governance Forum (**NZCGF** or the "**Forum**") we discussed the G20/OECD Principles of Corporate Governance (**OECD Principles** or the "**Principles**").

The Forum is committed to promoting good corporate governance of New Zealand companies for the long-term health of the capital market. We believe that good governance improves company performance and increases shareholder value, which is a core focus for NZCGF members as custodians of capital.

The OECD Principles provide guidance on corporate governance to support "market confidence and integrity, economic efficiency, sustainable growth and financial stability"¹. The OECD considers the Principles to be the "main international benchmark for good corporate governance, ... [which] have a global reach and reflect the experiences and ambitions of a wide variety of jurisdictions with varying legal systems and at different stages of development." At the previous quarterly meeting, you queried the Forum's view of the OECD Principles.

In response, the Forum has set up a sub-group (**Working Group**) to compare the OECD Principles with the NZCGF Corporate Governance Code, as well as the NZX Corporate Governance Code, the FMA Corporate Governance Code and the Stewardship Code. Work is ongoing, and we would be pleased to update you on this at future quarterly meetings between the IOD and the Forum.

In addition, we offer the following initial and non-exhaustive comments from the Working Group on the OECD Principles, and their congruence with existing NZCGF work and advocacy:

1. The intentions of the OECD Principles are admirable; in particular, the desire to construct "a formal structure of procedures that promotes the transparency and accountability of board members and executives to shareholders [as this] helps build trust in markets." The notion that Boards (and Directors) and Management should be transparent and accountable to shareholders is a critical aspect of corporate governance. The Forum has repeatedly noted that the Board-shareholder and Board-management relationships are the most critical in the corporate governance of public companies, and that good corporate governance seeks to minimise the agency costs that arise in these relationships.
2. The first chapter, *Ensuring the basis for an effective corporate governance framework* concerns how corporate governance frameworks should interact with a country's legal system, market authorities and stock exchanges. Most of this was standard and the New Zealand public market is congruent with the outlined sub-principles as a developed market. We note that concepts about "artificial intelligence and algorithmic decision-making" could be, and in other jurisdictions possibly may already be, used in supervisory processes, and the OECD's view that the human element remains critical.

¹ OECD, *G20/OECD Principles of Corporate Governance*, (2023). All quotations in this letter reference this source.

3. In the second chapter, *The rights and equitable treatment of shareholders and key ownership functions* the OECD notes that a jurisdiction's "corporate governance framework should protect and facilitate the exercise of shareholders' rights and ensure the equitable treatment of all shareholders, including minority and foreign shareholders." This statement emphasises the *importance of general shareholder rights (not just those associated with capital raisings) and the equal treatment of minority shareholders*, that the NZCGF has also championed.
4. The Principles state that "all shareholders should have the opportunity to obtain effective redress for violation of their rights at a reasonable cost and without excessive delay" and go on to note that "one of the ways in which shareholders can enforce their rights is to be able to initiate legal and administrative proceedings against management and board members... the confidence of minority investors is enhanced when the legal system provides mechanisms for minority shareholders to bring lawsuits when they have reasonable grounds to believe that their rights have been violated." While the Working Group has sympathy for the counterpoint that "there is some risk that a legal system that enables any investor to challenge corporate activity in the courts can become prone to excessive litigation", it seems likely that shareholder rights will be tested in court in the future, especially as Kiwisaver Schemes become larger and have even greater resources to initiate legal and administrative proceedings.
5. The OECD states that "ownership of an equity share provides a right to information about the corporation and a right to influence the corporation, primarily by participating and voting in general shareholder meetings." It clarifies that "shareholders' rights to influence the corporation centre on fundamental issues, such as the election of board members, or other means of influencing the composition of the board, amendments to the company's organic documents, *approval of extraordinary transactions [emphasis added]*, and other basic issues as specified in company law and internal company statutes." In recent times the NZCGF has sought to improve shareholders pre-emptive rights with respect to major and material transactions.
6. The third chapter titled *Institutional investors, stock markets and other intermediaries* concerns the fiduciary duties of institutional investors, in particular exercising so-called 'ownership rights' such as voting and engagement. This area is naturally complex due to the difficulty in assessing the actual views held by institutional investors' underlying clients, and minority views are at risk of being subject to perceptions of the majority or fashionable views. The OECD covers the high-level aspects of these issues.
7. In chapter four, *Disclosure and transparency* the OECD states that the "corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, sustainability, ownership, and governance of the company." The Principles also support "simultaneous reporting of material or required information to all shareholders in order to ensure their equitable treatment, a fundamental principle that companies must uphold". The NZCGF agrees with the fundamental principle of equitable treatment of all shareholders, both generally and particularly on corporate disclosures, and support timely and accurate disclosure on all material matters to shareholders.
8. In agreement with the OECD, the NZCGF is cognisant that "disclosure requirements should not place unreasonable administrative or cost burdens on companies. Nor should companies be expected to disclose information that may endanger their competitive position unless disclosure is necessary to fully inform an investor's decisions and to avoid misleading the investor."

9. The OECD states that “investors require information on individual board members and key executives in order to evaluate their experience and qualifications and assess any potential conflicts of interest that might affect their judgement... this information may also refer to directors’ compliance with applicable independence criteria.” These opinions are shared by the NZCGF, which has supported narrowing the definition of director independence to focus on conflicts of interest and maintained that the factors that are used to determine director independence are not exhaustive (i.e. there could be additional factors which Boards should discover and then exercise judgement upon).
10. In chapter five, *The responsibilities of the board*, the OECD states that the “corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board’s accountability to the company and the shareholders.” The Working Group like the way this is worded and refers you to comments in the first bullet point regarding the Board-management and Board-shareholder relationships and their centrality to corporate governance.
11. The OECD states that in addition to “guiding corporate strategy, the board is chiefly responsible for monitoring managerial performance and achieving an adequate return for shareholders, while preventing conflicts of interest and balancing the demands of the corporation. In order for boards to effectively fulfil their responsibilities, they must be able to exercise objective and independent judgement. Another important board responsibility is to oversee the risk management system and mechanisms designed to ensure that the corporation obeys applicable laws, including relating to tax, competition, labour, human rights, environmental, equal opportunity, digital security, data privacy and personal data protection, and health and safety... The board is not only accountable to the company and its shareholders but also has a duty to act in their best interests. In addition, boards are expected to take account of, and deal fairly with, stakeholder interests including those of the workforce, creditors, customers, suppliers and affected communities.” The Working Group considers this to be an excellent summary of the role of the corporate Board and provides its purpose in a nutshell.
12. The OECD also states in this chapter that “independence from controlling and substantial shareholders will need to be emphasised, in particular if the ex ante rights of minority shareholders are weak and opportunities to obtain redress are limited. This has led to both codes and the law in most jurisdictions to call for some board members to be independent of controlling and substantial shareholders, independence extending to not being their representative or having close business ties with them.” Indeed, the classification of ‘independent directors’ from the majority or controlling shareholders (determined by a poll at a shareholder meeting) is another issue which the NZCGF has pursued concerning Director Independence Settings. We prefer some type of enhanced independence regime on a comply-or-explain basis.
13. In the final chapter on *Sustainability and resilience* the OECD states that “companies play a central role in our economies by creating jobs, contributing to innovation, generating wealth, and providing essential goods and services. Countries have made commitments to transition to a sustainable, net-zero/low-carbon economy in line with the Paris Agreement and the Sustainable Development Goals... A sound corporate governance framework would allow investors and companies to consider and manage the potential risks and opportunities associated with such transition pathways...” The NZCGF agrees that corporate governance frameworks should enable investors and companies to understand the impacts on corporate performance of the various transition pathways to the net-zero/low-carbon economy.

14. The OECD states that “corporate directors are not expected to be responsible for resolving major environmental and societal challenges stemming from their duties alone.” In general, this seems appropriate as this is primarily the domain of policymakers and the duty of the Board to the best interests of the company and shareholders.
15. Finally, while the Working Group is sympathetic to the OECD’s view in the Principles that “sustainability-related disclosure should be consistent, comparable and reliable, and include retrospective and forward-looking material information that a reasonable investor would consider important in making an investment or voting decision”, we argue that if such disclosure is important to shareholders then in providing it the Board is acting in the best interests of the company and shareholders (subject to the cost of providing such disclosure being reasonable).

* * *

Once again, we thank you and the IOD for your interest in the NZCGF’s views on the OECD Principles. We hope that the brief comments on the OECD Principles shed light on how the NZCGF’s Working Group sees some aspects of them, and we hope to keep updated on our work comparing the Principles to other codes and guidelines in the New Zealand market at future IOD/NZCGF quarterly discussions.

Please note that this letter may be published on our website (www.nzcgf.org.nz) and LinkedIn page.

Yours sincerely,

Sam Porath
Chair
NZ Corporate Governance Forum