

Government Corporate Social Responsibility Inquiry

Dr Ian Woods and Nick Edgerton of the Sustainable Funds Team recently took the opportunity to contribute to Corporate Responsibility policy development and public debate by providing a submission to the Australian Government's Corporations and Markets Advisory Committee (CAMAC) inquiry. CAMAC recently released its Corporate Social Responsibility Discussion Paper after it was asked by the Parliamentary Secretary to the Treasurer, the Hon Chris Pearce MP, for consideration and advice about the extent to which the duties of directors under the *Corporations Act 2001* (the Corporations Act) should include corporate social responsibilities or explicit obligations to take account of the interests of certain classes of stakeholders other than shareholders.



In their role as Research Analysts in the Sustainable Funds Team, Ian and Nick examine the minimum social and environmental standards required by companies and have developed an appreciation for mainstream company trends in corporate responsibility. As investors, we are particularly interested in the actions and reports by responsible corporate leaders who see corporate responsibility as an opportunity and recognise the importance of wider stakeholders as part of their social contract with society and their aim to provide maximum return to shareholders. Identifying corporate responsibility leaders and laggards is an essential step in our investment process.

Based upon the knowledge generated from their work in the Sustainable Funds Team, the submission included five critical issues for consideration, shaped largely around matters raised by the Parliamentary Secretary.

A summary of our response follows:

1. Directors should have regard to the interests of specific classes of stakeholders and/or the broader community when making corporate decisions because having regard to these stakeholders is necessary to:
 - a. manage the crucial intangible assets of the organisation; and
 - b. minimise the risk of additional regulatory and compliance costs.

Given the disparate views expressed in submissions to an inquiry into corporate responsibility by the Parliamentary Joint

Committee on Corporations and Financial Services, current expectations placed on directors require clarity about the extent that they account for the interests of specific classes of stakeholders or the broader community when making corporate decisions. Clarity can be achieved through the following, or similar, revision to the Corporations Act:

S180(2)(d) rationally believe that the judgement is in the best long-term interest of the corporation, taking into consideration the interest of legitimate stakeholders and the environment.

2. In addition, to meet the implied social contract obligations to the community implicit from allowing companies limited liability and being a legitimate party in civil society, companies need to act in a manner acceptable to society's expectations.

A suggested revision to the Corporations Act should be:

S180(2)(e) have considered community, and legitimate stakeholder expectations, on appropriate corporate behaviour.

3. Australian companies should be encouraged to adopt socially and environmentally responsible business practices to ensure enlightened shareholder value. A variety of industry initiatives and best practice social and environmental reporting are available to assist the transition to these business practices and should be encouraged by government and industry groups.
4. Given that meeting legal requirements is the minimum standard set by the community for a company's corporate responsibility it is proposed that the Director's Report provides details on all non-compliances within the financial year. This could replace the requirements currently provided under s299(1)(f).
5. To facilitate effective disclosure of material non-financial issues, further guidelines are required to assist companies meet the intent of s299A of the Corporations Act. The disclosure should be of issues that directors are already aware of and considering within their current responsibility "of discharging their duties with the degree of care and diligence that a reasonable person would exercise." The requirement for directors to be considering these issues is not placing an additional responsibility on directors.

For those readers interested in the full submission made by Ian and Nick, please access the CAMAC website¹. CAMAC is expected to report later in 2006.

1 Submission no.58 – <http://www.camac.gov.au/CAMAC/camac.nsf/byHeadline/SubmissionsCorporate+social+responsibility>

stock story

Babcock & Brown

Babcock & Brown Environmental Investments Limited (BEI) is involved in the development and production of sustainable energy. BEI's main operations are Southern Oil Refineries, Natural Fuel Limited, Denco Pty Ltd and through its 91% owned subsidiary, EarthPower Technologies Sydney Pty Ltd.

Southern Oil Refineries, based in Wagga, produces a range of quality base oil products all manufactured from previously used lube oils, rather than from crude oil as at the traditional oil refineries. The re-refinery also produces a range of fuel oils as by-products.

In July 2005, BEI started constructing a \$45 million biodiesel manufacturing facility in Darwin. The plant will have the capacity to deliver a substantial proportion of the Australian Government's renewable fuel targets in the future. The completion is targeted for August 2006 and production is expected from September 2006.

In November 2005, BEI bought a US ethanol producer, Diversified Energy Company (DENCO). DENCO produces approximately 120 million litres of ethanol, using corn as prime feedstock and also has 12.5% interest in a US ethanol marketing company, primarily into the petrol substitute/biofuel market.

Earthpower Technologies Sydney Pty Ltd is an anaerobic digester facility that recycles organic waste from food manufacturing, retailing and hospitality industries into biogas, which is converted into electricity, and fertiliser. The company has signed a three year agreement to provide Country Energy with the full capacity (3.5 Megawatts) of electricity from a waste to energy production plant.

Over the last 12 months BEI share price has increased by over 60%.

research & engagement

The Sustainable Funds Team's (the Team) research focus during the past 12 months continued to be on 'industry specific sustainability' issues to complement our strong top-down sustainability and corporate social responsibility assessment. Industry specific sustainability analysis completed by the Team included companies in the Engineering Contractors and Services sector, and the Property sector with an environmental management focus. The Team also commenced research in the Commercial Services and Property Development sectors.

Strategic Research included a paper by Ian Woods entitled 'Lessons from the European Union Emissions Trading Scheme and Emission Intensity Permit Allocation' which identifies and explains four useful lessons from the experience of the European Union Emissions Trading Scheme for the development of an Australian scheme. The study concluded that lessons regarding the style of permit allocation can minimise the potential impact of an emissions trading scheme and thereby assist in the transitioning of the economy to a low emissions future.

On the engagement front the Team has kept busy with:

- **Sustainability:** Ian Woods was one of the judges for the Association of Chartered Certified Accountants Sustainability Report Awards. He provided written feedback to participating companies and presented and contributed to the discussion at the awards presentation.
- **Climate Change:** Ian provided written comments to the Australian Greenhouse Office regarding the Intergovernmental Panel on Climate Change Geosequestration (CO2 capture and storage) draft report as input into Australia's comments. Ian presented at the Climate Change and Finance Sector Conference (organised by BT and The Climate Group) on the institutional investors' view on climate change. In addition, Ian presented at meetings with various stakeholders (Australian Conservation Foundation, HESTA Superannuation, Victorian Department of Sustainability and Environment, Victorian Department of Infrastructure, Victorian Department of Premier, Adviser to the Premier, WWF Australia, and Energy Supply Association of Australia) about his paper on Implications of Climate Change Policy on Power Sector Investment and the subsequent Emission Trading Scheme Permit Allocation Paper. Also, Ian participated in the Workshop on Greenhouse and Energy Reporting in Canberra held by the Australian Government Department of the Environment and Heritage and provided a submission on behalf of AMP Capital Investors.
- **Human Rights:** Ian provided BHP with feedback on their disclosure of Human Rights within their operations.
- **Social and Environment:** Ian was a part of the panel discussing Community Consent with a range of stakeholders for the Christian Centre of Socially Responsible Investment Annual Investment Conference – Community Consent Workshop. Ian presented to the Australian Government Department of the Environment and Heritage and Advisors to the Minister and Shadow Minister for the Environment about Matthew Rey's research paper – Financial Payback from Environmental and Social Factors in Australia. Michael Anderson presented at the National Business Leaders' Forum on Sustainability about socially responsible investment, our fund, and the results of Matthew's research paper.
- **Industries of the Future:** Mike Murray visited various health care related companies in the US, including Ventana (competitor to Vision Systems), Actsys Medical (plasma and generics distribution), Supercare (Sleep distributor), Apria Healthcare, Fisher & Paykel Healthcare distribution, Cochlear implant centre in San Diego, ResMed, Citigroup US Healthcare Team, Ansell, Vision Systems, and Domantis (Peptech).
- **Reporting and Disclosure:** Ian presented at the Radcliffe Lecture (UNSW Accounting Department) about non-financial reporting issues. Sarah and Ian engaged with the Mineral Policy Institute of Australia and Publish What You Pay (UK) about transparency in the extractive industry and what AMP Capital Sustainable Funds can do for transparency in Australian mining companies.
- **Uranium Industry:** Ian wrote a submission to the Australian Government House of Representatives Standing Committee on Industry and Resources about the Development of the Non-Fossil Fuel Energy (i.e. Uranium) in Australia and presented to the Inquiry in September.





AMP Capital Corporate Governance

AMP Capital invests money on behalf of many Australians and as an active institutional shareholder we aim to take corporate governance seriously. We believe that it is not only our responsibility to make the best investment decisions we can on behalf of our clients, but also to ensure that the companies we invest in are managed effectively.

The AMP Capital Sustainable Fund has its own Corporate Governance and Proxy Voting Policy available on the website at www.sustainablefuturefunds.com. It builds on the AMP Capital policy and strong commitment to vote at every meeting and actively engage with companies on corporate governance issues. AMP Capital has a dedicated Corporate Governance Manager, Karin Halliday, who facilitates all our proxy voting and research on governance issues. This section summarises the corporate governance issues and voting outcomes from the recent Proxy Voting season in September/October 2005.

As an active shareholder, we believe that improved communication will usually contribute to better results. For this reason, when we cannot support current resolutions, we write to companies to explain why, and also to outline suggestions to ensure that resolutions are supportable in future. These letters have often led to constructive conversations, and many company Chairpersons now make it a habit to 'touch base' with us and other major shareholders annually. Companies that AMP Capital has had constructive engagement on corporate governance issues in the past six months include Westpac, Australian Wealth Management, Origin Energy, Transfield Services, and David Jones.

Voting Issues

In 2005 AMP Capital voted on 1,824 resolutions at 381 company meetings. The bulk of resolutions related to the re-election of directors and non-salary remuneration. AMP Capital supported all resolutions at only 238 [63%] meetings.

Non-executive director remuneration

At 67 of the company meetings where AMP Capital submitted votes, shareholders were asked to approve an increase in the maximum aggregate level of fees that could be paid to each company's non executive directors. The fee increase was supported at 56 meetings [84%].

Incentive plans

In 2005, AMP Capital submitted votes to 116 company meetings [supporting 62] on various Executive/Director incentive plans and grants [not including remuneration reports]. The reasons for not supporting incentive-related resolutions include: plans of less than three-years; had performance hurdles that were non-existent or too low; poor disclosure of the terms of share and option plans; participation of non executive directors in executive schemes; and/or plans showing no improvement, despite the company having received comments/input in the past.

Remuneration reports

This year we submitted votes on 219 reports, supporting 151 [69%]. The company remuneration reports we voted against over this full year include: AGL, Fleetwood Corporation, Gale Pacific, Investa Property Group, News Corporation, Sims Group, Spotless Group, and Vision Systems.

Board structure

AMP Capital supported the election or re-election of directors at approximately 95% of these meetings. The main issue of concern is the under representation of independent directors on many boards.

profile



Nick Edgerton

Research Analyst, AMP Capital Sustainable Funds team

Following Research Analyst Sarah Kim's move to Asian Business Development within AMP Capital Investors, the Sustainable Funds Team required a new Research Analyst to work with Dr Ian Woods to analyse the universe of investable companies. Our Sustainable Future Australian Share Fund has now increased to over \$1 billion funds under management, with analysts covering about 400 listed Australian companies.

The Team is pleased to announce the appointment of Nick Edgerton to the role of Research Analyst. Nick is responsible for Australian equities stock analysis from an environmental, social and governance perspective. In this role, Nick analyses company corporate responsibility and sector sustainability and constructively engages with companies on environmental and social issues.

Prior to this role in Sustainable Funds, Nick brings 6 years experience working in the sustainability field, working as a Senior Research Consultant at the Institute for Sustainable Futures (University of Technology, Sydney); an Environment Officer and Policy Officer at the Australian Government Department of the Environment and Heritage; and an Environmental Economist at the Scottish Agricultural College. Nick completed a Bachelor of Economics from Macquarie University and a Master of Science in Ecological Economics with Distinction from the University of Edinburgh.



news

performance

The Sustainable Future Australian Share Fund (the Fund) continues to outperform the ASX 200 benchmark in the short and long term. In the year to 28th February 2006, key sectors adding value included the telecommunications, diversified financials and health care sectors.

In telecommunications, the Fund did well by being significantly underweight as Telstra's earnings prospects continued to come under pressure from shifting technology. Diversified financials performed well as equity markets continued to prosper – the team's research uncovered a number of emerging players in this sector such as Record Investments and Select Managed Funds which returned 69% and 83% respectively.

Health care is one of our identified industries of the future and constituted our largest overweight for most of the year. Amongst the larger stocks, CSL and Cochlear each returned over 60%, significantly boosting our Fund's return. We also successfully invested in two key emerging companies – Pharmaxis and Vision Systems. Pharmaxis is a biotech company developing products to manage asthma and cystic fibrosis. During the year it passed a number of key milestones which saw its share price rise more than 70%. Vision Systems engineers cancer detecting equipment and also saw substantial share price appreciation following good sales figures and a corporate reorganisation.

On the negative side, the strong performance of the materials sector detracted from returns as a number of these stocks do not meet our minimum sustainability criteria.

We continue to seek out emerging companies in the industries of the future as well as mainstream leaders – key new entrants into the Fund include companies involved in biofuels such as Babcock and Brown Environmental and Australian Biodiesel Group.

Performance % to 28 Feb (before fees and taxes)

	3mths	1 yr	2 yr	3 yr	4yr	5yr
SFAS*	8.98	25.86	28.36	29.40	17.43	14.73
ASX 200	7.30	23.35	26.48	26.12	14.36	12.65
Relative	1.68	2.50	1.88	3.29	3.08	2.08

Source: AMP Capital Investors, Mercer. * SFAS refers to The Sustainable Future Australian Share Fund.

Momentum is building for greater corporate social responsibility following key events in recent months, including Sustainable Responsible Investment (SRI) certification, reporting, and the role of directors in corporate social responsibility.

Australia's **Ethical Investment Association** launched the world's first certification program for providers of SRI products and services. Certification is now available to Fund Managers and Superannuation Funds with SRI products, and Financial Advisors or Dealer Groups offering SRI advice. The SRI Symbol helps investors make informed choices about investments that take into account environmental, social and ethical considerations. AMP Capital Investors was part of the first round of Fund Managers to gain certification.

Improved reporting and greater disclosure is likely following some key events in the reporting field. In January, the **Global Reporting Initiative** launched the draft version of its third generation reporting guidelines (G3), and following feedback from report practitioners, organisations and users, G3 should continue to be the benchmark standardised sustainability reporting guidelines.

Meanwhile, the **Carbon Disclosure Project** now represents 211 institutional investors with assets of \$31 trillion under management in its fourth incarnation to the 500 most valuable companies in the world as measured by market capitalisation. Named CDP4, it is the first time that all Australian and New Zealand companies listed in the ASX100 and NZ50 have been included in the request, with public disclosure in September 2006 on the CDP4 website.

To assist organisations with triple bottom line reporting, a team from University of Sydney, supported by the Environmental Trust, has developed a reporting tool called **Integrated Sustainability Analysis**. This tool is based upon macroeconomic input-output analysis and integrates sustainability indicators to describe an organisations performance in triple bottom line terms.

Considerable debate about the role of directors, fiduciary responsibility, and corporate legislation, regarding opportunities for encouraging corporate responsibility has culminated in recent events:

- A Freshfields Bruckhaus Deringer study for UNEPFI released in October 2005 examines **fiduciary duty** in a number of international jurisdictions including Australia, summarising statutory provisions for a range of decision makers, including institutional investors, and the possibility for integrating environmental, social and governance considerations;
- The Australian Government has been canvassing stakeholder opinions on **corporate responsibility** through the Parliamentary Joint Committee on Corporations and Financial Services (due to report June 2006) and the Corporate and Markets Advisory Committee (due to report in 2006). See our headline story for more on the Corporations and Markets Advisory Committee; and
- The Institute for Sustainable Futures report on the role of Government in **mainstreaming SRI** in Australia surveyed SRI industry stakeholders to identify instruments to encourage widespread uptake of SRI.

Sustainable Future Funds

The Sustainable Future Funds are a family of three SRI funds available to Australian investors: the Sustainable Future Australian Share Fund, Sustainable Future International Share Fund and Sustainable Future Balanced Growth Fund. The overall objective of these funds is to deliver superior returns to our clients by investing in companies that contribute to, benefit from and best adapt to the shift to an environmentally sustainable and socially responsible global economy.

Further information can be found on our website: www.ampcapital.com.au or by contacting your adviser. Please note that you can subscribe to this newsletter on-line through our website.

Important note: Investors should consider the product disclosure statement available from AMP Capital Investors Limited (ABN 59 001 777 591) (AFSL 232497) for the relevant Sustainable Future Fund before making any decision regarding the Fund. Neither AMP Capital Investors, nor any other company in the AMP Group guarantees the repayment of capital or the performance of any product or any particular rate of return. Past performance is not a reliable indicator of future performance. While every care has been taken in the preparation of this newsletter, AMP Capital Investors makes no representation or warranty as to the accuracy or completeness of any statement in it including, without limitation, any forecasts. This newsletter has been prepared for the purpose of providing general information, without taking account of any particular investor's objectives, financial situation or needs. An investor should, before making any investment decisions, consider the appropriateness of the information in this newsletter, and seek professional advice, having regard to the investor's objectives, financial situation and needs. This document is solely for the use of the party to whom it is provided.