THE BOARDROOM REPORT
Vol 2, Issue 8, May 17, 2004

Private practices The new privacy code has implications for boards. Now there's an easy guide to help directors oversee the implementation of privacy procedures (more...)

Taking stock If you are unsure whether your company is healthy in all respects, then the stock doctor provides an insight (more...)

Paying the price The US tendency toward excessive CEO remuneration is tapering off, according to a recent survey (more...)

APRA softens its approach The board has primacy and a principles-based corporate governance approach is preferable to outright regulation, says APRA chief John Laker (more...)

Regulating the regulators A leading US chairman says corporate regulations provide a convenient smokescreen for more corporate abuses (more...)

Banking on profits Australian banks had another bumper year thanks to a strong domestic economy and a booming property market (more...)

SMEs still struggling SMEs are still struggling according to recent surveys (more...)

Governance in Europe and Asia on the improve The second survey by *Business Week* of European and Asian companies shows corporate governance is being taken seriously (more...)

AUSTRALIAN INSTITUTE OF COMPANY DIRECTORS
ABN 11 008 484 197
Professionalism in Directorship

http://www.companydirectors.com.au

This issue of *Boardroom Report* is brought to you by KPMG

http://www.kpmg.com.au

THIS IS A PRODUCT FROM AICD PUBLISHING

The opinions in Boardroom Report do not necessarily represent the views of the publisher nor the publication. Every effort has been made to ensure accuracy, but no responsibility is accepted for errors. All rights reserved. E-mail to: editor@companydirectors.com.au

Private practices

On 21 December 2001, the private sector provisions of the Commonwealth Privacy Act 1988 came into effect to cover businesses and other organisations with an annual turnover of more than $3 million, and, since December 2002, small businesses that carry on activities that are a higher risk to privacy.

The Office of the Federal Privacy Commissioner in Australia and the AICD have collaborated on a publication called *Privacy and Boards of Directors: What You Don't Know Can Hurt You*, which provides an easy guide to help directors oversee the implementation of privacy procedures in accordance with the new legal requirements.

The publication has been adapted with permission from a publication of the same name prepared by the Information and Privacy Commissioner Ontario.

Hard copies - as well as soft copies - are available from AICD's website under the bookshop icon and clicking "new books" at http://www.companydirectors.com.au

(Back to page 1)

Taking stock

More than one third of ASX listed companies exhibit the financial characteristics of failing companies, according to the latest Health of the Australian Stockmarket report from Lincoln Indicators, the company behind financial risk analysis software program, STOCKdoctor.

These "distressed" companies congregate in the Pharmaceuticals and Biotechnology industry, (74.4 percent) and the Technology Hardware and Equipment (61.8 percent) industry. Other industries containing a majority of companies in a distressed state are the Software and Services (58.5 percent), Telecommunication Services (54.1 percent) and Health Care Equipment and Services (51.8 percent) industries.

According to Lincoln Indicators managing director, Tim Lincoln, these results do not necessarily mean that investors should steer clear of these industries as, in some cases, individual companies within these industries can present excellent opportunities.

The company's STARstocks and Golden STARstocks, for example, are those which it identifies as "quality companies" and can be found in almost all sectors. Testament to the integrity of Golden STARstocks is Lincoln Indicators' Investor Directed Portfolio Service (IDPS), which has had returns of an amazing 39 percent in its first full year to 6 March, 2004.

As well as identifying those companies representing the best investment opportunities, STOCKdoctor also lists those companies which should be avoided. Over the past two decades, for example, of the 680 companies who delisted from the ASX, from the time of delisting to the time that an administrator was appointed, in 94 percent of cases STOCKdoctor showed they displayed an unsatisfactory financial standing.

In spite of the relatively high proportion of companies being classified as "distressed", there are 45.8 percent of ASX listed companies classified as satisfactory or better.

Lincoln says the overall result of the analysis is that corporate Australia has surpassed most analyst expectations with strong margins, revenue gains and cost cutting restructures more than compensating for the strong Australian dollar.

More information at http://www.stockdoctor.com.au

(Back to page 1)

Paying the price

A recent survey by Mercer Consulting shows that executive remuneration has:

- moved away from granting CEOs stock options,
- rebalanced the long-term incentive mix for CEOs,
- reined in overall CEO pay, and
- strengthened the link between CEO pay and performance.

The full survey is at http://www.mercerhr.com

(Back to page 1)

APRA softens its approach

In a speech to the WA Division of the AICD last week, Australian Prudential Regulation Authority chief John Laker said the board was the focal point of the corporate governance system. He made the comments in the context of the discussion paper APRA issued last November and requested submissions on.

There were fears that APRA would take a tough stance particularly after its less than flattering report on what occurred at the NAB. APRA will release its findings later this month.

According to Laker the board is ultimately accountable and responsible for the performance and conduct of the insurer. Delegating authority to board committees or management does not in any way mitigate or dissipate the discharge by the board of directors of its duties and responsibilities.

"APRA's prudential framework is based on the primacy of the board, which has ultimate responsibility for the sound and prudent management of an APRA-regulated institution," he said. "It is the board that should approve and review business strategies and significant policies of the institution.

"It is the board that should determine the institution's tolerance for risk, approve its risk management strategy and ensure that management has in place effective risk controls. In the relevant industries, it is the board that should ensure that the institution maintains capital resources commensurate with the level and extent of risk exposure.

"And, most generally, it is the board which should take the lead in establishing the culture and ethical values of the institution, including the transparency and candour which is brought to the discussion and resolution of problems. APRA has found the submissions to its reform proposals, and the consultations now under way, to be helpful and constructive.

"Our objective of high standards of corporate governance in APRA-regulated institutions is well accepted; the vigorous debate is about means. APRA is willing to consider a principles-based approach which would identify APRA's expectations of boards of prudentially regulated institutions and would put the onus more, if not fully, on boards to demonstrate that they can meet these expectations.

"We welcome views on how a principles-based approach would operate, and why it would be more likely to promote strong and effective board performance than the proposals we have put forward. But please heed the recent warning of a Commissioner of the US Securities and Exchange Commission that having too many principles without specific rules can end up delivering "marshmallow" – that is, principles that are open to misinterpretations and very difficult to enforce. APRA will still need to be able to require boards to improve their practices, if circumstances dictate."

Full speech at http://www.apra.gov.au/speeches

(Back to page 1)

Regulating the regulators

In an address entitled “We’re not waving: We’re drowning”, George Chamillard, chairman/CEO of Teradyne, a large US semi-conductor firm, says regulations have become so complex that anyone bent on mischief was able to hide that mischief from sight.

“The thicket of off-balance-sheet financing, phony revenue recognition, derivatives, and other schemes was so thick that it defied understanding by the average shareholder, by the business press, and even by most regulators,” he says.

“It was, as events have shown, pretty easy for the criminals to succeed. All they had to do was use the mountain of regulations to create a smoke screen under which they made off with the company jewels.

“The reaction of our lawmakers to all this was perfectly predictable: They would simply add more regulations and more complexity.

Full article at http://www.nacdonline.org

(Back to page 1)

Banking on profits

The Australian banking sector had another bumper year thanks to a strong domestic economy and a booming property market, says arecent KPMG survey.

Australia's five major banks (the majors) performed well during the first half of 2003/04, reporting asset growth of 10.7 percent from March 2002/03 to $1,23 billion at March 2003/04. The growth is due to a combination of factors, including continued strength in the housing market which has fuelled credit demand in the consumer sector (up 15.8 percent), and a thriving small to medium business sector that is also driving good credit growth for the majors. Growth in the corporate and institutional sector increased on average by 8 percent. Credit quality also improved; the doubtful debt expenses falling by $11 million. (1.1 percent)

Peter Nash, head of KPMG's financial services group says the banks are enjoying the consequences of a strong domestic economy that is stimulating activity in the consumer and small business sectors, comparatively; the corporate sector is still quite flat.

"Big business has not yet loosened the purse strings, despite an improvement in global business conditions, with most industries experiencing solid growth in demand and solid profits," he says.

"We would expect the current positive business confidence levels to translate into an increased demand for small business and corporate credit during the second half of 2004.

"The banks will be counting on this to offset the expected slowdown in the consumer sector," he adds.

Operating profit for the majors was impacted by various one-off and significant items. The combined "bottom line" increase in profits of $1,457 million (29.0 percent) while impressive, is not a true indication of the performance over the half.

"When you take out the effect of wealth management appraisal value adjustments, overall profits of the majors increased by a more modest $513 million (9.1 percent) from March 2002/03 to March 2003/04."

Profitability has been impacted favourably by an increase in net interest income of $749 million (6.7 percent) and an increase in non-interest income of $1,257 million (16.2 percent) due mainly to the return to favour of the banks' wealth management businesses.

However, total expenses increased by $1,057 million (10.4 percent) due to higher people and IT costs, and increased costs associated with customer service initiatives. Despite increased costs, the majors have reduced their cost to income ratio slightly, falling from 49.2 percent to 48.7 percent. Return on equity has remained relatively stable increasing slightly from 17.9 percent to 18.31 percent.

IT costs came under close scrutiny in the reporting period and rose significantly as depreciation of previously capitalised software once again increased.

The adoption of more conservative capitalisation and amortisation policies by some majors, and write-offs that resulted from carrying value assessments of capitalised software drove IT costs up by $258 million (27.8 percent) during the period.

"We expect cost to income ratios to come under pressure in future periods," says Nash.

"The majors are all investing in customer service initiatives and having to also bear the burden of increasing regulatory and compliance related expenses."

Full banking survey is at
http://www.kpmg.com.au/content.asp?cid=21257&s=13945

(Back to page 1)

SMEs still struggling

SMEs are still struggling according to recent surveys.
A MYOB survey of 2896 SME business owners in March/April 2004 to gauge their views on a range of issues including GST, compliance and provisioning found that:

- 54 percent of SMEs surveyed only calculate their GST liabilities, and whether they have sufficient funds to cover those liabilities, when they complete their BAS statements every quarter
- 80 percent of SMEs surveyed do not separate their tax liabilities from their main trading account
- 58 percent of SMEs do not earn interest on their GST accounts
- 54 percent of SMEs surveyed cited 'fees and charges' as the major source of annoyance in regard to their financial institution.

A survey conducted by the Institute of Chartered Accountants Australia shows that GST and BAS administration is still a major concern to SMEs with 77 percent of respondents citing it as a concern, 39 percent defining it as an "extreme concern":

- 41 percent of SMEs complained paperwork had increased to the point of where they questioned staying in business
- The time it takes CPAs to complete BAS has increased by 51 percent and time spent on annual returns has increased 89 percent.

In a survey conducted by the Victorian Automotive Chamber of Commerce, 71 percent of respondents said that if governments halved compliance burden, SMEs would "have more time to run a business". A further 69 percent believe that halved compliance would lower their stress levels and 50 percent thought that reduced compliance would lead to increased profits as more time could be spent on the business itself.

(Back to page 1)

Governance improving in Europe and Asia

The second survey by *Business Week* of European and Asian companies shows that corporate governance is being taken seriously.

From the Netherlands' Royal Ahold to South Korea's SK Corp, corporate boards are taking major steps to improve shareholder rights in the wake of financial scandals.

More than 40 countries now boast codes or laws regulating everything from financial disclosure requirements to the structure of corporate boards. A veritable industry has sprung up around the issue of corporate governance, with shareholder rights' groups, non-governmental organisations, and ratings agencies all getting into the act.

While many companies still just go through the motions, others have come to a real understanding that good governance is necessary to attract and keep investors. The momentum is strongest in Europe, where investors are challenging companies as never before. There is more sensitivity to governance issues in Asia, too, though the region's family- and government-controlled companies still face potential conflicts of interest.

For further details, see http://www.businessweek.com/magazine/content/04_20/b3883010.htm

(Back to page 1)