

SANDON CAPITAL

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30 October 2020

To whom it may concern,

Please find below a submission by Sandon Capital Pty Ltd (**Sandon Capital**) on the exposure draft legislation on **Making permanent reforms in respect of virtual meetings and electronic document execution**.

About Us

Sandon Capital is an investment manager for entities that invest in the Australian share market. Our focus is on medium- to long-term investment returns from investing in undervalued listed companies, using shareholder activism as a tool to positively shape the future direction of these companies. This activist aspect of our investment philosophy involves us engaging with a company's stakeholders, including directors and management as well as other shareholders. We have long held the view that Australia's corporate laws and regulations are among the most shareholder friendly in the developed world. Shareholder rights are clearly enshrined in the Corporations Act (2001).

Executive Summary

We consider legislative changes should:

- **allow the use of electronic documentation;**
- **keep the requirement for physical annual general meetings; and**
- **require companies to hold hybrid meetings (the meeting is held both in person and virtually).**

Detailed Submissions

Despite our legal framework, there are still far too many instances in Australia of persistently underperforming companies whose management and directors are practically entrenched due to various reasons including shareholder inertia.

Indeed, one only needs to consider the number of high-profile corporate scandals that have come to light in Australia in recent years. Notable recent examples include Commonwealth Bank, Westpac, National Australia Bank, Crown and AMP. In each instance, we believe stronger oversight and influence by shareholders (as the ultimate owners) may have helped avoid the worst of these scandals. Instead, millions of Australians whose futures are dependent on investment returns either in the short term (for example, those whose incomes rely on investment linked pensions) or in the longer term (for example, those accumulating for their retirement in superannuation schemes) have suffered.

The proposals contained in the “Corporations Amendments (Virtual Meetings and Electronic Communications) Bill 2020” appear at first glance to have a commonsense basis. Reforms to allow the electronic distribution of meeting documents, the electronic execution of company documents, electronic signing of meeting documents and the electronic taking and storage of minutes are sound and common sense. It is also difficult to find any serious unintended consequences of these reforms. We support these proposed reforms.

However, **making permanent the temporary measures allowing general meetings to be held virtually risks a dangerous disenfranchisement of shareholders and their rights and will likely serve to further the entrenchment of company directors, both the good and, more worryingly, the bad.**

It seems most stakeholders disclosed as being consulted by Treasury when formulating the proposed changes were the Governance Institute of Australia (GIA), the Australian Investor Relations Association (AIRA) and the Australian Institute of Company Directors (AICD). We consider their views to be biased towards the interest of their members: company directors and company management.

The basics of an AGM

Today’s AGMs comprise four interrelated functions:

- 1) Reporting
- 2) Questioning
- 3) Deliberation and debate and
- 4) Decision-making

Section 250S of Corporations Act 2001 requires that *“the Chair of AGM must allow a reasonable opportunity for the members as a whole at the meeting to ask questions about and make comments on the management of the company.”* We believe the proposal to allow virtual-only general meetings will severely impinge on the intent and policy underlay of this section of the Corporations Act.

Courts and commentators in Australia, the UK and even some states in the United States *“have identified two justifications for holding physical gatherings: as a forum for face-to-face accountability for stewardship; and as a forum for deliberation and debate of motions.”*¹ According to renowned Australian commercial law barrister, Dr Elizabeth Boros, *“courts have noted that a physical gathering provides a forum for deliberation and confrontation.”*² We believe that in order to ensure shareholders adequate opportunity to question board intentions and company strategy that physical gatherings for general meetings must occur wherever possible. In our view, the Government has not considered carefully enough the likely adverse consequences of virtual-only meetings. The Exposure Draft Explanatory Materials discusses three options:

1. Allow the temporary relief to expire on 21 March 2021 without law reform (the status quo).
2. Allow the use of technology to meet legal requirements in respect of meetings and electronic document execution.
3. Allow the use of technology to meet legal requirements in respect of meetings and document execution with enhancements

Sandon Capital considers all three options are unacceptable:

- Option 1, which would maintain the status quo, does not allow for common sense enhancements to allow for the use of electronic distribution and execution of documentation.
- Under Option 2 is the adverse consequences of virtual meetings will erode shareholders’ rights and serve to further entrench poor performing boards. Furthermore, it does not provide for the recording of all questions and comments (and shareholders’ subsequent access to these).
- Under Option the adverse consequences cited in comments on option two above remain. It is also unacceptable because of the practical delay in members being able to access all questions and comments submitted to the meeting.

Why we oppose virtual meetings

The unintended consequences of allowing companies to abolish physical annual general meetings will be significant and cannot be countenanced.

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Our experience has shown that many directors, especially those of poorly performing companies, would prefer not to have to face shareholder scrutiny and questioning.

As the current AGM season unfolds, meetings we have witnessed have been highly scripted affairs, not only in respect of company statements (which is not unusual) but also in responses to questions. Shareholders do not know what questions remained unanswered. Furthermore, shareholders have been unable to ask follow-up questions if the scripted responses did not address the original question or required clarification.

The proposal that companies be required to record in their minutes all questions submitted to and asked at their virtual meetings seems acceptable, except that section 251A of Corporations Act (2001) allows a company up to 1 month for it to record minutes of a meeting of members. Section 251B allows a member to inspect those minutes in person free of charge but if a member cannot inspect the minutes in person, the company may take up to 14 days (or longer if it requires payment) before it provides the member with access to the minutes. This means that shareholders of a listed company who cannot inspect the minutes in person may not know the details of all the questions until at least 6 weeks after a general meeting has been held. This is clearly unacceptable. Unscrupulous boards may also seek to “edit” the narrative by excluding valid questions from the records and shareholders are likely to be none the wiser – how can they audit compliance?

Another benefit of physical meetings is that shareholders can meet directors and management outside of the formal business of the meeting. For most shareholders and for many directors, this is one of the only opportunities for such informal meetings. Mingling with shareholders for the customary tea and biscuits, while derided by some, is a great opportunity for directors to hear the clear views of shareholders without the filter of management or investor relations. The value of this interaction should not be under-estimated; to both shareholders and companies.

Physical general meetings also provide shareholders with opportunities to meet and discuss relevant matters with each other, something virtual meetings preclude. Shareholders can share views with each other, and whilst this is entirely legal, we suspect this is a practice that some companies would prefer to discourage or, where possible, prevent.

Physical general meetings are not perfect and have their shortcomings, **however** they are better than the alternatives detailed in the Exposure Draft Explanatory Materials.

We believe a far better approach is to allow the use of electronic documentation whilst keeping the requirement for physical meetings.

According to the figures in the Explanatory Materials, the bulk of the savings comes from the documentation reforms. These savings are estimated at \$445 million per year.³ The savings that would be obtained by holding virtual meetings are estimated at \$82 million per annum.⁴

The UK Experience

As we understand the laws in the UK, public companies have a choice of how they conduct their general meetings according to the provisions of their constitutions. Since 2009 (and in practice 2016) some companies have chosen to seek shareholder approval to alter their articles to allow for virtual-only general meetings.

According to international law firm, Baker McKenzie, there is little investor support for virtual-only AGMs, whereas there is more widespread support for the hybrid model.⁵

In the UK, Institutional Shareholder Services (ISS), the world's leading corporate governance advisor, has a policy of recommending shareholders vote in favour of constitutional changes that propose allowing hybrid meetings, but will generally recommend against those proposing virtual-only meeting.⁶ According to ISS, *"While there is recognition of the potential benefits of enabling participation at shareholder meetings via electronic means, investors have raised concerns about moves to completely eliminate physical shareholder meetings, arguing that virtual meetings may hinder meaningful exchanges between management and shareholders and enable management to avoid uncomfortable questions."*

The UK's Investment Association, which represents investment managers in the UK managing more than £8.5 trillion for their clients, has stated unequivocally that its *"members believe that virtual-only AGMs are not in the best interests of all shareholders...as their use could be detrimental to Board accountability."*⁷

It is telling that the UK investors, where virtual AGMs have been permitted for some time, are broadly against the use of virtual-only AGMs.

An alternative proposal

We believe a more sensible approach would have been to follow the path similar to that of the United Kingdom where "hybrid" meetings are increasingly common. The hybrid meeting is one where the general meeting is held both in person and virtually.

UK Law allows a company to hold virtual meetings provided its Articles (or Constitution) allows for it. This means shareholders are first asked to approve whether virtual meetings can be held.

Timing

We consider the timing of the consultation process ill-chosen. October is one of the busiest times for shareholders and other stakeholders. This is the time when the annual general meeting season gets under way. We understand a number of stakeholders have expressed their frustration at the timing and the difficulty in meeting the deadlines for submissions. We request an extension to the deadline for submissions until at least 30 November 2020 to allow stakeholders to make submissions.

If the reforms to virtual meetings are passed, it will be interesting, once COVID-19 related restrictions dissipate, to see how many companies voluntarily conduct their general meetings in person. We suspect good companies will continue to hold physical meetings but bad or underperforming companies will be those that resort to virtual meetings alone.

If you have any questions or would like to discuss this response to the consultation paper, please do not hesitate to contact me.

Yours sincerely,



Gabriel Radzyminski
Director,
Sandon Capital Pty Ltd

³ Exposure Draft Explanatory Materials, page 25, paragraph 2.33

⁴ Ibid, page 25, paragraph 2.32

⁵ Baker McKenzie website, AGM Season 2020 and the Restrictions Related to COVID-19, 17 March 2020 (<https://www.bakermckenzie.com/en/insight/publications/2020/03/agm-season-2020-and-the-restrictions>)

⁶ ISS, United Kingdom and Ireland Proxy Voting Guidelines, Benchmark Policy Recommendations 19 November 2019, Amendments to Articles to allow Virtual Meetings, page 7

⁷ The Investment Association, Position Statement: Virtual AGMs, December 2017 (updated on 30 January 2018)