



**Submission to:**

**Parliamentary Joint Committee on  
Corporations and Financial Services**

**Inquiry into Corporate Responsibility**

**September 2005**

<b>1. Executive Summary</b>	<b>3</b>
<b>2. Introduction and approach to submission</b>	<b>5</b>
<b>2.1. Westpac’s experience as a major Australian corporation</b>	<b>5</b>
<b>2.2. Defining the scope of corporate responsibility</b>	<b>6</b>
<b>2.3. Westpac’s experience as a global sustainability leader</b>	<b>6</b>
<b>3. Westpac’s response to the Terms of Reference</b>	<b>8</b>
<b>3.1. Current practice</b>	<b>8</b>
<b>3.1.1. Key points</b>	<b>8</b>
<b>3.1.2. Discussion</b>	<b>8</b>
<b>3.1.3. Westpac’s practice in taking stakeholder interests into account</b>	<b>9</b>
3.1.3.1. Corporate responsibility in vision, mission, values and objectives .....	10
3.1.3.2. Formal business principles and reporting against these principles .....	10
3.1.3.3. Formal Board stewardship of stakeholder interests .....	10
3.1.3.4. Strategy and business planning .....	10
3.1.3.5. Leadership and competency models .....	11
3.1.3.6. Stakeholder interests within performance appraisal and remuneration ....	11
3.1.3.7. Recruitment, training and development .....	11
3.1.3.8. Supply chain management .....	11
3.1.3.9. Contributing to the debate on corporate responsibility and sustainability .	11
<b>3.1.4. Case study of stakeholder engagement at Westpac</b>	<b>12</b>
<b>3.2. Why decision-makers should take account of stakeholder interests</b>	<b>15</b>
<b>3.2.1. Key points</b>	<b>15</b>
<b>3.2.2. Discussion</b>	<b>15</b>
<b>3.2.3. Westpac's sustainability journey</b>	<b>16</b>
<b>3.3 Directors' duties</b>	<b>17</b>
<b>3.3.1. Key points</b>	<b>17</b>
<b>3.3.2. Discussion</b>	<b>18</b>
<b>3.4. Revisions to the legal framework</b>	<b>18</b>
<b>3.5. Alternative mechanisms</b>	<b>19</b>
<b>3.5.1. Key points</b>	<b>19</b>
<b>3.6. Reporting requirements</b>	<b>20</b>
<b>3.6.1. Key points</b>	<b>20</b>
<b>3.6.2. Discussion</b>	<b>20</b>
<b>3.6.3. In practice: non-financial reporting at Westpac</b>	<b>22</b>
<b>3.7. Learnings from other countries</b>	<b>22</b>
<b>3.7.1. Key points</b>	<b>22</b>

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## 1. Executive Summary

Progressive companies like Westpac already systematically take into account the interests of stakeholders other than shareholders.

At Westpac taking account of the interests of stakeholders is simply understood as 'doing the right thing,' that is: behaving in a responsible, ethical and trustworthy manner; accepting responsibility to manage the direct and indirect societal and environmental impacts of business activities; understanding and responding to stakeholder priorities; being prepared to make short-term trade-offs for the sake of longer-term future gains; and having a commitment to transparency and accountability.

Being responsive to stakeholders is at the heart of the primary obligation of companies: to maximise returns for shareholders on a long term, sustainable basis. The successful management of reputational, social, environmental and other 'non-financial issues' is clearly fundamental to the resilience of the company and to sustainable shareholder value.

Organisations are already regarded by the community, shareholders included, as having responsibilities that extend beyond statutory responsibilities to the company's legal stakeholders. To continue to prosper, Westpac believes companies must respond to these evolving legitimate community and shareholder requirements and expectations.

Consequently, Westpac along with other progressive companies takes an expansive view on directors' duties. Taking a balanced view and managing with regard to the interests of stakeholders other than shareholders is viewed as entirely in the interests of long-term shareholder value creation.

There is already very extensive existing regulation and legislation covering the interests of stakeholders, and responsible business practice more broadly. Westpac also considers that the existing provisions of the Australian Corporations Act on director's duties together with the broader legal framework provide adequate scope to allow, if not actively encourage, responsible business practices. As a result, Westpac does not believe that clarification of directors' duties is required. If further regulation is forthcoming, then the reasons for it should be clearly stated so that corporations, if they saw fit, could go beyond mere compliance.

The major challenge to introducing additional and prescriptive regulation in this area is the difficulty of defining corporate responsibility obligations in legislation which can appropriately capture the specific issues in each sector and organisation.

Additionally, it is fundamentally difficult to mandate good, values-based business behaviour through legislation or regulation.

Given the progress in voluntary uptake of responsible business practice in Australia, together with the existing legislative and regulatory framework, Westpac therefore sees no requirement for additional prescriptive legislation or regulation at this time.

There may be a case for considering non-prescriptive approaches to encourage responsible business practice. Examples of this are the ASX Corporate Governance Council Best Practice Recommendations and in the UK, the recently introduced requirement for an Operating and Financial Review.

Beyond that, better engagement by mainstream financial markets on corporate responsibility and sustainability performance is the major opportunity to encourage responsible business behaviour.

To encourage better engagement, non-financial reporting must take into account the emerging needs of investors and analysts and provide the performance information required.

In particular, performance and valuation models capable of assessing total organisational performance across both financial and non-financial dimensions are required. In this regard, clearly stated performance targets are essential.

Boards now have a very broad mandate for the oversight of corporate performance, only part of which is considered by the traditional financial accounting paradigm. This means directors must ensure they properly understand the true value-drivers, risks and opportunities within the business. In Westpac this has been helped by the establishment of a special Board Committee - the Corporate Responsibility and Sustainability Committee.

Directors, shareholders and other stakeholders must consequently have access to the information they need in order to fully assess the company's performance. This is likely to require a mix of financial and non-financial metrics.

On the reporting front, although good progress has and continues to be made, Australian companies still lag global best practice in non-financial reporting compared with many developed countries.

Prescriptive reporting frameworks, however, would be premature as a further critical period of experimentation and engagement between corporations, financial accounting bodies, financial markets participants and other stakeholders is required both within Australia and as part of the global debate on this issue.

## **2. Introduction and approach to submission**

### **2.1. Westpac's experience as a major Australian corporation**

This submission draws on Westpac's experiences as a major Australian corporation and one operating in a sector which has first-hand experience of the changing societal expectations of business - and the complexities of operating in contemporary society.

Westpac began trading on 8 April, 1817 as the Bank of New South Wales and was Australia's first company and its first bank. The company's name was changed in 1982 to Westpac Banking Corporation following the merger with the Commercial Bank of Australia.

As at 31 March 2005, the Westpac Group employed approximately 27,000 people in Australia and around the world and had global assets of \$255 billion.

Westpac is ranked in the top 10 listed companies by market capitalisation on the Australian Stock Exchange Limited and has around 233,000 individual and institutional shareholders in Australia and overseas.

Westpac's operations comprise five key areas of business, through which we serve around 8.2 million customers via an extensive network of branches in Australia and New Zealand and throughout the Pacific region, as well as offices in key financial centres around the world. These five business areas are:

- Business and Consumer Banking, which includes deposit taking, transaction accounts, credit cards and other lending. Westpac is a major home loan provider and also meets the finance needs of business customers with a turnover of up to \$20 million. Investment, superannuation and general and life insurance products are also available through the branch network.
- Wealth Management, which comprises the asset accumulation, investment management and life insurance operations in Australia and New Zealand. Wealth Management designs, manufactures and services financial products to enable customers to build, manage and protect their wealth. This includes managed investments, life insurance, superannuation, and discount broking.
- Westpac Institutional Bank provides financial services to corporate and institutional customers, assisting and advising in the management of cash, funding, capital and market risk for companies and institutions in Australia and New Zealand.
- New Zealand Retail provides a full range of retail and commercial services to customers throughout New Zealand. It is the leading provider of banking services to small to medium business and is the banker of the New Zealand Government.
- Pacific Banking provides a full range of deposit, loan, transaction account and international trade facilities to personal and business customers throughout the region.

## **2.2. Defining the scope of corporate responsibility**

There is considerable confusion as to the meaning of corporate responsibility and related concepts - primarily sustainability and sustainable development.

Westpac defines sustainability as the operating principle of maximising economic, social and environmental value simultaneously. Sustainable development is the goal we are working towards, ie 'development is sustainable where it meets the needs of the present without compromising the ability of future generations to meet their own needs.'<sup>1</sup>

Corporate responsibility is applying this principle in practice: acknowledging we have a major impact on society; accepting we are accountable to diverse stakeholders; and conducting the business to meet all of its financial, social and environmental responsibilities, under-pinned by appropriate values and principles.

Amongst practitioners there is agreement that the crux of corporate responsibility is two-fold:

- Acknowledging that business operates in a societal and environmental context - and accepting responsibility to manage the societal and environmental impacts of its business activities;
- Recognising that corporate responsibility in effect applies to all of an organisation's activity; including the workplace, marketplace, environmental footprint, and broader impacts on society.

The Global Reporting Initiative<sup>2</sup> offers a practical guide to the scope of corporate responsibility by setting out the indicators which companies should report against. Significantly these guidelines are subject to continual review and modification - via a multi stakeholder process.

Certainly Westpac's view is that corporate responsibility is not an add-on but comprises a values and principles-based perspective on the entirety of everyday corporate activity. This is set out in detail on page 10 of Westpac's 2004 Stakeholder Impact Report. Westpac reports against approximately 110 non-financial indicators. Also significantly Westpac considers corporate governance a sub-set of the broader corporate responsibility agenda, and not vice-versa.

## **2.3. Westpac's experience as a global sustainability leader**

The submission also draws on and offers Westpac's perspective as a company publicly committed to the highest level of responsible business behaviour. Westpac's corporate responsibility and governance journey, which started some eight years ago from a reputational risk perspective, has involved the systematic integration of corporate responsibility into Westpac's business model.

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<sup>1</sup> World Commission on Environment and Development

<sup>2</sup> <http://www.globalreporting.org/index.asp>

As a result, Westpac has been consistently rated both nationally and globally as being at the forefront of responsible and sustainable business practices. These independent ratings include:

- Number one rating for banks globally in the Dow Jones Sustainability Index for 2005/2006 - for the fourth year running;
- Number one in the 2004 Business in the Community Corporate Responsibility Index (CRI) in both Australia and the full UK index, ahead of over 140 UK plcs and global organisations;
- Across four consecutive ratings over 2004-2005, the only bank out of approx 3,200 companies assessed globally to be awarded the maximum score for corporate governance by Governance Metrics International; and
- The number one company and only AAA rated organisation for 2004 for the second year running in the Australian Reputex Social Responsibility Ratings.

### **3. Westpac's response to the Terms of Reference**

To assist the Parliamentary Joint Committee, this submission is structured to deal with parts (a) to (g) in turn of the Terms of Reference of the inquiry.

#### **3.1. The extent to which organisational decision-makers have an existing regard for the interests of stakeholders other than shareholders, and the broader community.**

##### **3.1.1. Key points**

Progressive companies, like Westpac, already systematically take into account the interests of stakeholders other than shareholders.

Taking account of stakeholder interests is simply understood as 'doing the right thing.' That is:

- behaving in a responsible, ethical and trustworthy manner;
- accepting responsibility to manage the direct and indirect societal and environmental impacts of business activities;
- understanding and responding to stakeholder priorities;
- being prepared to make short-term trade-offs for the sake of longer-term future gains; and
- having a commitment to transparency and accountability.

In practical terms this requires responsible business practices to be embedded right through business strategy and operations; from vision, mission and values, to every aspect of operational management.

Good progress has been made by Australian companies in embracing responsible business practice - as indicated by the rapid uptake of voluntary non-financial reporting.<sup>3</sup>

At the same time it is important to acknowledge that all organisations are required by law to take into account the interests of stakeholders across a significant proportion of the corporate responsibility agenda, for example workplace practice, corporate governance and environmental practice.

##### **3.1.2. Discussion**

Most corporations have in place formal processes to take into account the interests of stakeholders, including those of shareholders, in their business decision-making.

Beyond shareholders, companies typically categorise key stakeholders into the following groups: employees; customers; suppliers, government and regulators; 'NGO' and other interest groups; and the broader community. Specialised corporate functional areas then manage relationships with these stakeholder groups.

What tends to differ between companies is the approach adopted to resolve the often competing interests of the different stakeholder groups.

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<sup>3</sup> The KPMG International Survey of Corporate Responsibility Reporting 2005 shows that 23% of Australian companies produce a stand-alone corporate responsibility or similar report; up from 14% in 2002.



At one extreme, a reactive, 'ignore it if we can,' stance is adopted to stakeholder interests. And in the most extreme cases, the responsibility of the board and management to fulfil a proper stewardship role on behalf of shareholders for the long term may even be lost sight of. Such extreme situations have shown up in recent corporate scandals and failure, but in no way are the norm for corporate behaviour.

The vast majority of companies at a minimum have formal processes to take account of the interests of their employees and their customers and to ensure they comply with all laws and regulations at a minimum.

The more progressive corporations, in fact, have detailed processes to systematically take into account the interests of all stakeholders in every aspect of business decisions. In significant areas this takes them further than just compliance.

Importantly, the factoring of stakeholder interests into decision-making in leading companies is values and principles-driven, rather than compliance-driven, and the focus is on delivering long-term sustainable value financially, socially and environmentally.

### **3.1.3. Westpac's practice in taking broader stakeholder interests into account**

Westpac itself has adopted a specific 'stakeholder responsive' orientation within its broader commitment to responsible business practices. Put simply, Westpac seeks to manage its business in a way that produces balanced and positive outcomes for all stakeholders and optimises economic, social and environmental value.

In practice, this requires complex but manageable trade-offs to ensure that the maximisation of long-term shareholder value is not compromised.

Clearly, the maximisation of longer-term shareholder value is the core responsibility of any corporation. This is not in question and as a result corporations must be governed for the benefit of the shareholders.

But in Westpac's view, the maximisation of longer-term shareholder value is fundamentally put at risk if a company, in narrowly interpreting the *shareholder primacy principle*, does not behave in a responsible, ethical and trustworthy manner towards all its key stakeholders.

Westpac believes that to positively contribute to sustainable shareholder value creation for the company and more broadly to a sustainable society, the following operating principles are essential:

- accepting responsibility in managing the societal and environmental impacts of business activities (the so-called 'externalities;')
- understanding and responding to stakeholder priorities;
- being prepared to make short-term trade-offs for the sake of longer-term future shareholder value gains; and
- being committed to transparency and accountability in every aspect of business activity.

Westpac's approach is to incorporate stakeholder considerations into decision-making across the whole Westpac Group, from the Board and executive management downwards. This has involved the adoption of formal policies, practices and processes which apply across the key functional management processes - as set out below.

#### 3.1.3.1. Reflecting corporate responsibility in vision, mission, values and objectives

Responsible business practice is intrinsic to Westpac's vision, mission, values and objectives. It goes beyond business strategy itself to include: what the business is; how it behaves; and how it presents itself. Westpac's 'DNA' or blueprint sets this all out.

The Westpac DNA is widely communicated externally (for example in Westpac's 2004 Concise Annual Report, page 11) and internally.

#### 3.1.3.2. Formal business principles and reporting against these principles

Over 50 detailed and specific principles and 150 related commitments are set out within Westpac's *Principles for Doing Business*. These extend well beyond a standard employee Code of Conduct and set out the behaviours stakeholders can expect from Westpac in relation to: governance and ethical practice; employees; customers; the environment; suppliers; and the broader community. The Principles apply to everyone at Westpac including non-executive directors and executive management.

Company performance against the Principles is set out in Westpac's, non-financial or *Stakeholder Impact Reports*. These are designed in conjunction with the financial reporting to together fully report Westpac's performance to its stakeholders across both financial and non-financial metrics. Westpac's employee involvement, community partnerships and capacity-building activity is given specific focus within an additional, *Community Involvement Report*.

Copies of Westpac's *Principles for Doing Business*, *Stakeholder Impact Reports* and *Community Involvement Reports* can be found at Westpac's website [www.westpac.com.au](http://www.westpac.com.au) under the Corporate Responsibility section.

#### 3.1.3.3. Formal Board stewardship of stakeholder interests

Corporate responsibility is the domain of the whole Board, as set out in the Westpac Board Charter. Specific focus and Board-level stewardship is provided by the Board Corporate Responsibility and Sustainability Committee.

The Committee is chaired by a non-executive director and comprises two further non-executive directors plus Westpac's CEO. However all Board directors are fully informed on Committee matters and are able to attend all meetings - which most times they do. Also the full Board is formally informed on all Committee business.

Typical agenda items include: feedback from external assessments and ratings; external sustainability reporting; and reviews and discussion of specific projects and initiatives, for example sustainable supply chain management. The Committee also examines performance quarterly across a range of social and environmental indicators.

Copies of the Westpac Board Charter and the Board Corporate Responsibility and Sustainability Committee Charter can be found at Westpac's website [www.westpac.com.au](http://www.westpac.com.au) under the Investor Centre section.

#### 3.1.3.4. Strategy and business planning

Corporate responsibility is at the heart of Westpac's business model. Consequently, there is no corporate responsibility or sustainability strategy as such; rather this is integrated into the core business strategy. In turn, corporate responsibility is built into strategic decision-making across the business.

Sustainability is seen as a competitive differentiator for Westpac. Whereas much of the broad debate on corporate responsibility focuses on risk amelioration, Westpac is very much pursuing the business upside from adopting responsible and sustainable business practices; for example through cost reduction, and pursuing new products and new markets.

#### 3.1.3.5. Leadership and competency models

Corporate responsibility principles are embedded into the training and development of management. For example, managing significant relationships with external stakeholders is one critical experience now required for advancement within Westpac. This is alongside managing reputation; understanding the broad stakeholder context for business decisions; applying appropriate judgement and being able to reconcile different objectives; demonstrating consistency with Westpac values; and so on. Encouraged behaviours include practical experience of managing sensitive issues in the public arena and representation on external boards and forums.

#### 3.1.3.6. Stakeholder interests built into performance appraisal and remuneration

Corporate responsibility is incorporated into individual and group performance management via a balanced scorecard framework. This operates from group level objectives down through the business units to the performance objectives of all senior employees. This means decision-makers are appraised and remunerated according to their contribution towards four performance dimensions; for: shareholders; employees and customers; and for an additional corporate responsibility dimension which will be business unit and role specific.

#### 3.1.3.7. Recruitment, training and development

Corporate responsibility principles are embedded into recruitment, induction, training and development across the organisation. For example, the Connect with Westpac induction training covers Westpac's culture and vision, values and purpose; and emphasises the stakeholder concept and how to balance the interests of Westpac's customers, people, shareholders and the community. It reinforces Westpac's commitment to being a responsible organisation whose strategy and key drivers reflect the community it serves and represents. It also covers important aspects of working at Westpac: for example diversity and compliance and legislative requirements.

#### 3.1.3.8. Supply chain management

Westpac's sustainable supply chain management program requires all new suppliers to report on their environmental, social and ethical performance. It has also been applied retrospectively to the top 100 suppliers which account for approximately 80% of procurement spend.

The approach adopted is developmental, requiring continual improvements both by individual suppliers and across Westpac's overall supply chain impacts.

#### 3.1.3.9. A commitment to contribute to the global and national debate on corporate responsibility and sustainability

Westpac's advocacy and outreach commitment has contributed to sustainability practice in Australia and overseas and helps ensure Westpac remains at global best practice. In particular, Westpac contributes to industry and external groups including the Global Compact; World Business Council for Sustainable Development; Global Reporting Initiative; UNEP-FI; and the Equator Principles Working Group. Westpac is represented on various government task forces on sustainability and this includes the direct involvement of the CEO and Chairman. Westpac people also frequently contribute to practitioner conferences and workshops.

Westpac benchmarks its sustainability performance globally on both a bilateral and multilateral basis - for example sharing with peer organisations information provided to external ratings and assessments.

Westpac recognises the critical role of the academic research agenda at this early stage of the sustainability debate and participates in the key academic forums. This has included, for example, the US Academy of Management, the International Association of Business in Society; and the European Academy of Business in Society. Westpac has also contributed to local and global research: for example Monash University research into the organisational competencies which lead to sustainable business outcomes; and pending research by the University of Technology Sydney (UTS) on creating the 'demand side' for sustainability amongst Australian consumers.

#### **3.1.4. Case study of stakeholder engagement at Westpac**

Westpac believes that effective engagement with stakeholders is the basis for taking their interests into account. The approach to stakeholder engagement, however, varies across companies.

At a minimum, most seek the views of their employees on workplace issues through employee surveys, forums and other formal and informal feedback mechanisms. The more progressive corporations have extremely sophisticated mechanisms to engage employees and ensure all of their concerns are understood and factored into business decisions.

In the customer space, most companies again have formal processes although the degree of sophistication and comprehensiveness vary significantly. This is particularly so in relation to complaint management and dispute resolution.

In the government and regulatory space, the approach adopted by companies is typically compliance-driven, with public policy engagement often managed through representative industry groups. The degree of active participation in these industry groups on public policy matters by companies can also vary significantly.

It is in the area of engagement with, and hence having regard to the interests of, NGO interest groups that the practices of companies vary most. And it is in this area that there tends to be least active engagement by companies. Many companies opt to monitor the views of interest groups from a distance, adopting a defensive stance to issues raised by such groups. It is in this area that corporations have typically had most trouble in reconciling the interest of such 'stakeholders' with their obligations relating to the shareholder primacy principle.

Westpac's approach is to maintain active stakeholder dialogue with a broad range of representative groups ranging across NGOs, trade unions, financial and consumer advocacy groups, government and industry bodies, shareholders and investors, and international sustainability organisations such as UNEP-FI, the World Business Council for Sustainable Development, the Global Compact and the Global Reporting Initiative.

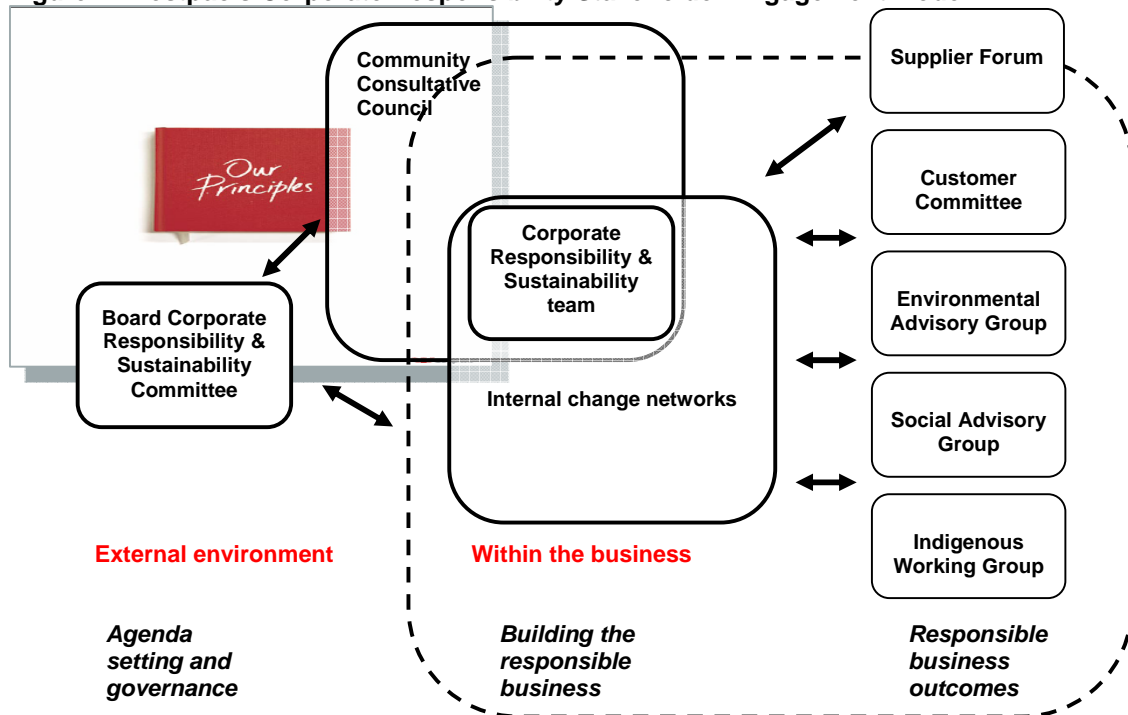
Stakeholder engagement is devolved to the extent that both the choice of stakeholders consulted and the nature of the engagement can be driven by specific issues and projects and the business units directly involved. This means stakeholder engagement occurs where and when it is required and hence knowledge and learning is delivered where it is most effective.

Emerging issues on which Westpac has recently consulted with our stakeholders include:

- Revisions to the Customer Charter and key performance indicators for customer performance;
- Sustainable supply chain management;
- The New Zealand corporate responsibility reporting framework;
- Responsible lending and financial literacy
- Climate change;
- Lending with high social or environmental benefit;
- Environment-linked banking products;
- Packaged banking services for community organisations;
- Corporate governance;
- Rural and regional services;
- Drought assistance for farmers and small businesses;
- Indigenous access to financial services;
- Public - private sector community partnerships;
- The development of new SRI products;
- The development of a 'talking' ATM for people with a disability;
- The Enterprise Development Agreement;
- Ongoing credit and risk assessment;
- Ongoing environmental management; and
- Non-financial indicator development.

Beyond this informal engagement, Westpac has developed a formal and dynamic cross-functional stakeholder engagement structure on corporate responsibility and sustainability issues to encourage continued dialogue both across the organisation and with external stakeholders. The broad structure of this stakeholder engagement is set out in Figure 1 below.

**Figure 1. Westpac's Corporate Responsibility Stakeholder Engagement Model**



Central to this is the fostering of two-way communication and action between and among Westpac and its stakeholders on the societal issues of mutual importance and relevance.

The Community Consultative Council plays a critical role in focusing the overall engagement program. Council members are drawn from community and government organisations in subject areas relevant to Westpac's social and environmental impacts. Members include Westpac's varied Community Partnerships<sup>4</sup> together with for example the Australian Conservation Foundation, the Australian Council of Social Service, the Australian Council of Trade Unions and Finance Sector Union, the Human Rights and Equal Opportunity Commission, the Commonwealth Department of Family and Community Services, the Commonwealth Department of the Environment and Heritage, and the Australian Consumers' Association.

The Council supplements ad-hoc and project-based dialogue with external stakeholders and brings together the leaders of these organisations with the CEO and key executives. It provides Westpac with feedback on its policies and strategic direction. The Council also specifically assists in setting Westpac's sustainability priorities which are key inputs into Westpac's non-financial reporting and the AA1000 independent assurance process.

Beyond this, the Council has a broad objective of exploring how Westpac as a major financial institution can better collaborate with stakeholders from multiple sectors to take action on key sustainability issues.

Priority sustainability issues identified by the Committee in 2004/05 include:

- The sustainability of current levels of consumer debt;
- Climate change, water scarcity and ecological sustainability;
- Sustainable cities - sustainability and the built environment;
- The emerging underclass; 'postcode poverty' and social estrangement;
- The ageing population - the employment of older workers; and wealth transfer and related intergenerational tensions;
- Disability: particularly access to employment and the increasing incidence of disability and chronic illness as the population ages; and
- Indigenous disadvantage.

Beyond the Council, a further series of predominantly internal groups brings together people within the organisation to focus on specific areas of sustainable business practice:

- The Customer Committee examines monthly complaints management data, addresses customer concerns, resolves specific customer complaints and has a broader remit across Westpac's products and services. The Committee currently has two external, independent customer and ethics advocates, one of whom chairs the committee.
- Regular Supplier Forums bring together Westpac's key suppliers and Westpac's procurement professionals. Westpac's focus is on positively influencing supplier behaviour, and the Forums allow supplier education and other capacity building; the sharing of best practice, problem solving and so on.

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<sup>4</sup> Set out in the Community Involvement Report available at [www.westpac.com.au](http://www.westpac.com.au) under the Corporate Responsibility section

- The Environmental Advisory Group coordinates and drives environment-focused activity, including environmental targets; lending and investment policy including lending and investment with a high environmental benefit; the assessment of environmental risk in lending and investment; and environment-linked product development.
- The Social Advisory Group parallels the environmental group. It coordinates and drives social issue focused activity, for example again lending and investment policy; product pricing; responsible lending and banking; lending and investment with a high social benefit; reputation risk in lending and investment; and community involvement activity.
- The Indigenous Working Group coordinates activity to tackle Indigenous disadvantage. The group shares best practice across Australia, New Zealand and the Pacific. Typical issues and initiatives include financial education, access to services, capacity building and local employee involvement.

### **3.2. The extent to which organisational decision-makers should have regard for the interests of stakeholders other than shareholders, and the broader community.**

#### **3.2.1. Key points**

The rationale for Westpac having regard for the interests of stakeholders other than shareholders, and the broader community - and for why other companies do so - is threefold:

- Firstly organisations are already regarded by the community, shareholders included, as having responsibilities that extend beyond the statutory responsibilities to the company's legal stakeholders. We live in a pluralist society and to continue to operate, companies must meet these evolving legitimate community and stakeholder requirements and expectations.
- Secondly, because doing so is at the heart of what Westpac sees as the primary obligation of companies - to maximise returns for shareholders on a long term, sustainable basis. The successful management of reputational, social, environmental and other non-financial risks is clearly fundamental to the resilience of the company and to sustainable shareholder value generation.

Practical experience within Westpac has shown that the business case arguments for corporate responsibility across the two key dimensions of reduced risk and enhanced business opportunity do indeed apply.

- Thirdly because from an ethical standpoint, doing so is simply the right thing to do.

Overall, Westpac believes that such rational, enlightened and self-interested business behaviour will increasingly be understood simply as good management and indeed the only way to manage in the contemporary society.

#### **3.2.2. Discussion**

Westpac firmly believes that organisational decision-makers (including all of non-executive and executive directors; executive management and organisational decision-makers more generally) should have regard for the interests of all stakeholders for both instrumental reasons (doing so delivers strategic differentiation and competitive advantage, as part of the broader 'business case') and normative reasons (it is the right thing to do.)

Westpac has publicly stated its belief that addressing customer and community concerns and accepting its corporate social responsibilities are integral parts of ensuring the sustainability of its financial performance.

Put simply, companies need employees who want to work for it; customers who want to buy its products and services; suppliers who want to supply to it; and of course investors who want to invest in it. Acknowledging and responding appropriately to the expectations of these groups - the corporate responsibility ethos - implicitly is in the long term interests of the business.

### **3.2.3. Why Westpac embarked on its sustainability journey**

Following the emergence in the late 1990s of clear anti-bank sentiment in the Australian community, Westpac subsequently sought to identify and address those issues of equity and social justice which our stakeholders considered integral to the continuance of the 'social licence to operate.'

Within the existing corporate governance structure, in 2001 Westpac established the Board Corporate Responsibility and Sustainability Committee. Its purpose is to review the social and ethical impacts of Westpac's policy and practice and to oversee initiatives to enhance Westpac's reputation as a socially responsible corporate citizen.

With strong personal support from both the Chairman Leon Davis and Chief Executive Officer David Morgan, Westpac has sought to ensure that the principles of corporate responsibility are incorporated into every aspect of policy and practice.

In June 2001, Westpac released the Social Accountability Charter, recently updated as Westpac's Principles for Doing Business.

In the 2001 Concise Annual Report, Westpac sought to address the underlying causes of anti-bank sentiment within the community. Banks stood accused of pursuing the bottom line at any cost and Westpac felt that this was an issue so fundamental to the sustainability of its long-term success that it could not be ignored. As a consequence, Westpac sought to directly respond to several key community concerns around the areas of accessibility, value for money, acting on customer complaints, supporting employees and working within the community.

In July 2002, the ongoing efforts to identify and address key corporate responsibilities culminated in the release of Westpac's first Social Impact Report (now entitled the Stakeholder Impact Report.) These document Westpac's performance against the social, environmental and economic bottom line and represent the continuing commitment to transparency in addressing stakeholder concerns.

These and other initiatives demonstrate the leadership role that Westpac has taken in the financial services sector, both in Australia and internationally, in addressing social obligations head-on through an inclusive, multi-stakeholder approach.

Moving forward, Westpac believes this rational, enlightened and self-interested business behaviour will come to be understood simply as good management.

In Westpac's case, there is no sustainability strategy as such. On the contrary the core objective of the corporate responsibility program is to support the core business strategy, and to enhance shareholder value by assisting to maximise intangible value.



The corporate responsibility way of thinking and working directly supports Westpac's core service-profit business model; builds the long term drivers of capacity, performance and value within Westpac (these include improved reputation and social licence to operate; reduced regulatory and other operational risk; enhanced operational efficiency; and enhanced innovation and creativity) and in parallel contributes to a more sustainable society.

As part of this the issues considered by the Board and executive management under the corporate responsibility and sustainability remit are quite fundamental to the risk and opportunity profile of the business: for example employee attraction and retention; complaints management; climate change; consumer debt; demographic change and so on.

In terms of outcomes, responsible business practice at Westpac has been a driver of both employee and customer attraction and retention and driven bottom-line savings from better management of our direct environmental footprint.

### **3.3 The extent to which the current legal framework governing directors' duties encourages or discourages them from having regard for the interests of stakeholders other than shareholders, and the broader community.**

#### **3.3.1. Key points**

From a legal perspective, directors' duties can be variously interpreted. Westpac along with other progressive companies takes an expansive view, believing that responsible business practices are entirely in the interests of long-term shareholder value creation.

Westpac also believes that the existing provisions of the Corporations Act and the broader legal framework provide adequate scope to allow, if not actively encourage - responsible management practices. For this reason, Westpac does not advocate a black letter law approach to prescribing directors' duties to stakeholders.

However, Westpac does recognise a diversity of views on this matter. Some have argued for a clarification of directors' duties in line with the expectations of responsible business behaviour.

One such clarification of this type is set out in draft clause (B3) of the March 2005 UK White Paper for the proposed Company Law Reform Bill. This draft proposes a general duty on directors to take into account:

- the likely consequences of any decision in both the long and the short term; and

any need of the company to:

- have regard to the interests of its employees;
- foster its business relationships with suppliers, customers and others;
- consider the impact of its operations on the community and the environment; and
- maintain a reputation for high standards of business conduct.

Unlike Australia, the UK currently has no existing statutory statement of directors' duties. Westpac believes Section 181 of the Corporations Act 2001 (the 'good faith' provision) represents an adequate definition for directors' duties in respect of responsible business practices.

### 3.3.2. Discussion

The current reality is that boards are already regarded by the community as having responsibilities that extend beyond statutory responsibilities to the company's legal stakeholders.

As already noted, Westpac believes the primary obligation of companies today is to maximise returns for shareholders on a long term, sustainable basis. This means that directors are simultaneously thinking both about the interests of today's shareholders as well as the interests of owners of the company into the future.

Whilst specifically discharging duties in the interests of the corporation is not synonymous with acting in the interests of shareholders alone (ie shareholder wealth), Westpac's position is that responsible business practice is almost always shareholder value maximising.

The linkages to shareholder wealth may be tangible and direct (in Westpac's case, the sustainability agenda has delivered specific bottom-line cost savings) or less tangible and more diffuse (for example again in Westpac's case an improved reputation and social licence to operate.)

Westpac accepts that the responsibilities on the Board and management which flow from this approach go well beyond strict legal obligations and the financial bottom-line. In particular, this means an expansive interpretation of directors' fiduciary duties - in line with current societal expectations, which looks beyond just compliance.

The role of the Board in this wider interpretation continues to include managing asset allocation in the usual way, but also extends to managing the trade-offs between short-term profit maximisation and longer-term prosperity and value creation.

### **3.4. Whether revisions to the legal framework, particularly to the Corporations Act, are required to enable or encourage incorporated entities or directors to have regard for the interests of stakeholders other than shareholders, and the broader community. In considering this matter, the Committee will also have regard to obligations that exist in laws other than the Corporations Act.**

There is already very extensive regulation and legislation covering the interests of stakeholders, and responsible business practice more broadly.

This includes numerous provisions across the workplace including occupational health and safety; the marketplace including trade practices; key corporate governance requirements (which Westpac understands as a subset of the broader corporate responsibility and sustainability agenda) and environmental protection.

The major challenge to additional and prescriptive regulation in this area is the difficulty of defining in legislation corporate responsibility obligations which will differ between industry segments and which may be specific to each organisation. Further, additional legislation will encourage a 'compliance only' mentality.

Corporations are no different to the society in which they operate. Societies have laws, but successful societies operate well beyond mere compliance with those laws. So too with corporations.

As set out in (3.6) below, the sustainability movement is an early stage of evolution both in Australia and internationally. A further period of experimentation and debate nationally and globally is required prior to any consideration of prescriptive legislation on corporate responsibility standards.

Westpac, however, advocates active engagement and monitoring by Government with a review of corporate practice in five years.

Westpac believes that a black letter law, compliance approach would promote low standards and discourage voluntary and innovative approaches to corporate responsibility. Westpac's view is that it is difficult to mandate good values-based business behaviour effectively through legislation or regulation.

Of primary relevance to non-financial reporting, Westpac does believe there may be a case for non-prescriptive approaches, such as the ASX Corporate Governance Council Best Practice Recommendations and the recently introduced UK Operating and Financial Review and Directors' Report Regulations 2005.

Under the latter, UK directors are now required to provide a balanced and comprehensive analysis of the business (the Operating and Financial Review, or 'OFR') which is both retrospective and future-focused, focusing on the material trends and factors underlying current and future performance.

The OFR intent is to supplement existing reporting with improved non-financial, qualitative and forward-looking information, which includes social and environmental issues to the extent that they have a material bearing on the current or future financial performance of the business.

For example, directors are specifically guided to consider the importance of corporate reputation and the quality of relationships with stakeholders.

Significantly, directors are enabled to make their own assessment of the significance of these issues and report accordingly - but they must sign off the OFR, with significant penalties for non-compliance.

The OFR approach is not without its detractors, but at the very least the regulation is requiring boards to actively engage with corporate responsibility issues, and report in the specific context of their business; their shareholders; and broader stakeholder base.

In the Australian context, the corporate responsibility agenda is to some extent already considered within the ASX Corporate Governance Council Best Practice Recommendations, and Westpac recommends that the application and usage of the Guidelines be allowed to evolve.

As a final point, any future consideration of non-prescriptive approaches should allow for the convergence of reporting requirements and avoid duplication or redundancy of requirements.

### **3.5. Any alternative mechanisms, including voluntary measures that may enhance consideration of stakeholder interests by incorporated entities and/or their directors.**

#### **3.5.1. Key points**

As set out in Section 3.6 below perhaps the major opportunity for the adoption of responsible business practice amongst listed companies is improved engagement by financial markets on this aspect of business performance.

What is required is the development of more sophisticated performance and valuation models capable of assessing total organisational performance across both financial and non-financial dimensions.

There are examples of multi-sectoral initiatives; for example the Who Cares Wins initiative by the Global Compact<sup>5</sup> and the Enhanced Analytics Initiative.<sup>6</sup>

### **3.6. The appropriateness of reporting requirements associated with these issues.**

#### **3.6.1. Key points**

Boards have a very broad mandate for the oversight of corporate performance, only part of which is considered by the traditional financial accounting paradigm. Much of a business' performance, capacity and value over the medium term is by definition regarded as intangible within this model. As in Westpac's case, these intangible assets frequently account for the bulk of a listed company's market capitalisation.

This has two implications. Firstly directors must assure themselves that they properly understand the true value-drivers, risks and opportunities within the business.

Secondly directors, shareholders and other stakeholders must have access to the information they need to have in order to fully assess and value the company's performance. This is especially critical for investors (for example superannuation investors) who are necessarily concerned with the long-term prospects and performance of a company. This requires a mix of financial and non-financial metrics, reported internally and through existing financial reporting, specialised non-financial reporting, or ideally integrated total performance reporting.

#### **3.6.2. Discussion**

Non-financial reporting (as part of the sustainability movement more generally) is an early stage of evolution both in Australia and internationally. The challenge is that non-financial reporting tends not to offer the rigour and comparability of financial reporting (given its prescriptive framework.) Basic questions for non-financial reporting are yet to be resolved: for example whether reporting specific to the context of each company can be effectively reconciled with the need to provide sector and more general comparability; and the tension between adapting the financial accounting paradigm or adopting more stakeholder-led reporting which emphasises materiality - that is focusing on the material information that affects the long-term prospects of the company.

It is also important to acknowledge this current debate on materiality, which is fundamental to the difficulty of prescriptive reporting, and indeed non-financial reporting and corporate accountability more generally.

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<sup>5</sup> <http://www.unglobalcompact.org/content/NewsDocs/WhoCaresWins.pdf>

<sup>6</sup> <http://www.enhancedanalytics.com>

The concept of materiality has been borrowed from financial accounting, where in essence something is material if it has the potential to affect the perception of a company. Materiality is an emerging but critical issue in non-financial terms because it concerns what to report - and why. One interpretation is that (non-financial) information is material if it is required by stakeholders for them to be able to make informed judgements, decisions and actions.<sup>7</sup> Clearly what is material is open to even more subjectivity and interpretation than applies to financial performance and reporting.

Westpac's response has been to test its non-financial reporting, and underlying sustainability systems and processes against the emerging AA1000 assurance standard from AccountAbility. More generally the issue emphasises the fundamental difference between financial and non-financial reporting; and the critical need for real engagement with stakeholders to understand their perspectives and respond accordingly.

Although Australian corporations are well represented in significant voluntary initiatives like the Global Reporting Initiative - which Westpac endorses as the basic framework for non-financial performance indicators - more generally Australian companies still lag global best practice compared with many developed countries. KPMG research<sup>8</sup> indicates 23% of Australia's top 100 companies publish stand-alone reports on non-financial performance compared with 71% of the top 100 companies in the UK and 80% in Japan.

Westpac is concerned that Australia's strong performance on corporate governance practice and reporting has not yet translated into the broader corporate responsibility agenda.

At the same time there are some relevant initiatives currently in train, including the Corporations and Markets Advisory Committee (CAMAC) reference from the Parliamentary Secretary to the Treasurer; the use of the ASX Corporate Governance Council guidelines to encourage companies to report on non-financial performance; framework development for corporate reporting of non-financial information by CPA Australia; and related standards development by the Australian Accounting Standards Board.

At this stage Westpac believes prescriptive reporting frameworks are premature as a further critical period of experimentation and engagement between corporations, non-financial audit bodies, accounting bodies, financial markets participants and other stakeholders is required both within Australia and as part of the global debate on this issue. It should be remembered that such reporting frameworks are still going through an evolutionary phase and should be given time to fully develop.

Westpac makes two recommendations in respect of non-financial reporting.

Firstly, one aspect of non-financial reporting that requires particular attention is the opportunity to take into account the emerging needs of investors and analysts and to provide the performance information they require and would want to see to enable them to fully engage with this emerging area of management practice.

Along with progressive corporates and investors, Westpac believes that companies embracing sustainability will generate more long-term shareholder value than those ignoring these risks and opportunities.

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<sup>7</sup> <http://www.accountability.org.uk/>

<sup>8</sup> KPMG International Survey of Corporate Responsibility Reporting 2005

The current level of engagement by mainstream (in comparison with SRI specialists) financial markets is limited. However they are key stakeholders for this new performance data. Whilst progressive organisations have a part to play through voluntary reporting and direct engagement with mainstream equities analysts and fund managers, the development of more sophisticated performance and valuation models capable of assessing total organisational (and ultimately societal) performance is now required by market participants.

Secondly, Westpac believes that materiality is indeed critical to the success of non-financial reporting. Where companies do not use a full assurance approach, selective disclosure or 'cherry-picking' should be discouraged by encouraging companies to explain the basis of their disclosure framework. To this end, a non-financial, independent audit function will most probably become customary.

### **3.6.3. In practice: non-financial reporting at Westpac**

At Westpac, comprehensive non-financial indicators are presented to the Board quarterly comprising leading indicators and a subset of indicators now reported externally in the Stakeholder Impact Report.

Transparent and comprehensive external reporting of social, environmental and financial performance is central to Westpac's approach to governance and responsibility management. Beginning in 2001, Westpac has produced four dedicated non-financial reports or Stakeholder Impact Reports, with progressively more sophisticated external verification and assurance.

In 2004, Westpac's financial and non-financial reporting was more closely aligned as the basis for integrated total performance reporting, and comprises three integrated reports: the Concise Annual Report; the Annual Financial Report and the Stakeholder Impact Report. The most recent non-financial report includes over 110 performance indicators.

Westpac now has a stakeholder-guided assurance approach using the AA1000 Assurance Standard which examines both the non-financial reporting and the effectiveness of Westpac's underlying sustainability processes.

## **3.7. Whether regulatory, legislative or other policy approaches in other countries could be adopted or adapted for Australia.**

### **3.7.1. Key points**

In line with the Board's enlarged mandate for the oversight of corporate performance, Westpac believes shareholders and all stakeholders should be given a true picture of the business performance which identifies the key business drivers and risks and opportunities.

As set out in (3.4) above Westpac does not see a need for prescriptive legislation or regulation.

The local ASX Corporate Governance Council Best Practice Recommendations and UK Operating and Financial Review requirements are examples of less prescriptive approaches designed to encourage responsible business practice.

As covered in (3.3) above Westpac does not see a need to revise directors' duties as set out in the Corporations Act. If clarification of directors' duties is required, one model is set out by the March 2005 UK White Paper for the proposed Company Law Reform Bill.