"The Scrip"
MANY INVESTORS; ONE VOICE
New Zealand Shareholders Association Inc. NZSA

ISSN 1179-4275 **February 2010**

BRUCE'S EDITORIAL – THE RATIONAL INVESTOR – YEAH RIGHT!

The key assumption behind Modern portfolio theory and the efficient Market hypothesis is that Investors are as a collective group, rational.

Some time ago I had a debate in Hamilton with a number of parties, the theme of which was that ethics pay. I lost the debate, as the head of finance of Waikato University stated there is no evidence that ethics pay; the only economic theory relevant to this debate is that all participants in the economy act to maximize their "personal utility."

In economics people are just economic units participating as producers, consumers and investors. When we buy goods and consume we endeavour to buy the best value for money, thus optimising our "personal utility," Some buy on price and some buy on quality or for other reasons that maximize their personal utility. It is fair to say that most consumers get spun senseless by marketing to their wants and desires, and what they actually want is confused. Thus many consumers are far from rational. As producers we maximise our personal utility by giving as little as we can to get as much as we can. So we cut corners and sell crap at a high price. Not all producers do this. Some actually still value long term relationships and want to produce quality; this for them is their utility. The point is "utility" is not necessarily a monetary concept. I just love economic psycho babble.

Now to investors. In order for them to be rational, they must have some element of financial discipline when making buy or sell decisions. The reality is that investment is often motivated more by emotion than by common sense. In aggregate, it could be hoped that a collection of investors is rational. The assumption is of course that there are enough of them buying and selling at the same time to get a rational collective response, - the ingredient of market liquidity. However, there is not a single stock that is traded on NZX that has anywhere near enough liquidity daily, let alone by the minute, to satisfy this requirement to deliver up this theoretical rational investor. In any event, the aggregate is really the sum of thousands of irrational buy and sell transactions. People sell for all sorts of reasons that have to do with their personal utility, (which is not necessarily dollars or commonsense,) and have nothing to do with a rational analysis of the investments prospects, at least not in real time which is the assumption behind efficient market theory.

At least in theory, investing is about creating wealth, or at least the hope that wealth will be created, investing thus in theory is a financial activity. Investing is about balancing future returns against risk. Thus in theory capital markets should be efficient eventually. The issue is how far from the rational do irrational investors allow a price of an asset to deviate from the rational response before it gravitates back to the theoretical price, and how do investors know that the price today is indeed a rational price that reflects all known risks relative to a prospective return. The simple answer is they do not. Here is another quote from Buffet, this time on the market, and on share prices and momentum trading which is what share traders look at more than they look at the fundamentals of the business. Perversely share price momentum analysis is often called fundamental analysis. The essence of Buffet's quote: (Sorry, it is not verbatim,) "Share markets respond to emotion. When sentiment is positive, they over-shoot any rational response, and likewise when they are pessimistic they also over-shoot. These are the hallmarks of a manic depressive, and who would use a manic depressive as an investment advisor."

Markets are far from efficient in my view. At times they are hopelessly over priced, and at other times they are hopelessly under priced. Markets especially ones with thin liquidity, are a random walk of human manic activity, yet portfolio theory, efficient market theory, the capital assets pricing model all assume that the wild oscillations in share markets can in some way be used as a proxy for the risk of markets as a whole, which may be true, and also individuals' shares in particular, which is far from true.

Now the final assumption of efficient market theory and the capital assets pricing model, and ultimately portfolio theory, is that in addition to there being enough rational investors pricing risk in real time, that these so called rational people have all relevant information real time to do that job.

Now shall we get real about this? Who has the information and who provides it to the investors? - management and maybe boards. Who decides what is relevant to the market? - boards. When something is price sensitive they are obliged to disclose it under the continuous disclosure rules, but this has not always been the case, and in terms of the data used by Markowitz on share price movements, no such regime was in place. Thus markets were only informed of information that the board considered was necessary.

Now regardless of the continuous disclosure regime, human nature is to communicate good news fast, and bad news, slow. Hello! If markets are supposed to be processing real time risk which is more important do you think?

Simply look at the great debt debate issues, and also look at the minnows that were not worth even thinking about. Did Provenco ever announce they were in default with their bank? When did Charlie's, and IRG announce bank problems? Not when they were emerging, and they don't just pop out of nowhere. They announced when the bomb was dropped. Do you think the occupants of Hiroshima would have been pleased to learn that a plane was approaching in 1945 12 hours before it arrived? Of course, but what actually happened, is that they found out about it when the plane was over the city and the bomb was dropped, - too late. This is continuous disclosure in business, real time.

So the whole hypothesis is flawed on the basis that investors never have all the information, and certainly only get bad news late, and mostly, there is insufficient liquidity to support the hypothesis that a price is rational in aggregate.

Now yet another theory, which at least has some common sense to it, which if followed should bring all this nonsense into disrepute. This is Agency theory, and the concept of Information Asymmetry. The guts of this theory are that there are always those who have information and have an obligation in agency to communicate it well and effectively, and it observes that this rarely occurs and it create a market mismatch. Hello again! It creates insiders. This is why we have insider trading penalties, because the use of insider information is now considered criminal theft, as it should be.

So efficient market theory, assumes also that there are no thieves operating in the market place - so many assumptions to support a theory that has driven the world financial markets for 2 decades to unprecedented levels of stupidity and mayhem.

There are theories for everything. People spend their lives dreaming this stuff up for no other reason than that they can, and when the rest of us think they have some greater knowledge just because they have got a PHD or a Nobel prize, we lose our ability to reason. Then, we have no one to blame but ourselves.

Bruce Sheppard

NEW ZEALAND SHAREHOLDERS ASSOCIATION INC.
PO Box 6310, Wellesley Street, Auckland Ph (09) 309-9768
Website – www.nzshareholders.co.nz

Chairman- Bruce Sheppard - bruce@gilshep.co.nz Ph (09) 309 5191
Secretary/Treasurer- Chris Curlett - chris.curlett@xtra.co.nz Ph (021) 738 032
Corporate Liaison- Des Hunt - desmondhunt@xtra.co.nz Ph (09) 521 6117
Research Director- Kevin McCaffrey kevin.mccaffrey@xtra.co.nz Ph (021) 925 675
Newsletter & Branch Liaison- Alan Best fleshnfruity@xtra.co.nz Ph (09) 524 0317
Proxy Coordination- Jacquie Staley – proxies@nzshareholders.co.nz Ph 021 2889990
Governance and strategic relationships - John Hawkins jhawkins@internet.co.nz
Coopted member - Grant Diggle - grant.diggle@gmail.com
National Manager- Patrick Flynn - patrick.flynn@nzshareholders.co.nz

VOLUNTEERING - WHY BOTHER?

You've had experience no doubt of being a member of at least 1 voluntary association (such as a sports club, service organization) and so you'll be very much aware of the fact that the most successful ones are where the members, who effectively own the association, pitch in to help whenever needed. Committee members who volunteer to help not only when asked, but give their time on an ongoing basis to administer, organise, fundraise or whatever else is required, are the unsung heroes of the voluntary world.

In the New Zealand Shareholders' Association, it is no different. We have 40 members who serve on the 5 Branch Committees + a further 8 who serve on the National Board of Directors (2 of whom are also on the Auckland Branch Committee), so just under 5% of the membership is in an ongoing commitment to serve on behalf of their fellow members.

There are also a number of committed members who serve in co-opted roles such as auditing, acting as proxy representative at AGMs, manning the NZSA membership promotion table, helping with organising Branch meetings and company visits etc – your help is much appreciated.

So, the question is "what can the other 95% of the membership do to keep their association vital, active and successful in achieving its objectives as the champion of shareholders' rights in New Zealand?"

The answer lies in your hands, so put them up if you want to make a difference. If you are not already actively involved, irrespective where you live, but would relish a bit of active service on behalf of yourself and your fellow members, then I invite you to contact me by phone, letter or email and we can take it from there. It doesn't mean you have to join a Committee - just registering your willingness to help is all I ask at this stage.

The more people who do put their hands up, the less the workload will be on those already involved. The Australian Shareholders' Association with 50 years of shareholder activism under its belt and almost 8,000 members to draw on is still actively seeking volunteers to come forward.

Please initially contact Patrick Flynn NZSA National Manager
NZSA National Office PO Box 6310 Wellesley Street Auckland 1141
Phone 09 309 5191 Ext 739 or 021 368 325
or leave a message on toll free 0800 6972 7478 or 09 309 9768
Email: patrick.flynn@nzshareholders.co.nz

Patrick Flynn

WAIKATO UNIVERSITY ESSAY

Editor: Final year Business School students compete for a prize offered by Bruce Sheppard in company with CSNZ. This year although the prize was not awarded, we thought Alison Fletcher's essay for Corporate Law would interest our members.

The subject: Over the past decade, small shareholders in New Zealand and other countries have formed themselves into organised groups to advocate for change in corporate governance and also to challenge company directors as to their actions and non actions. Consider whether or not, in your opinion, it is possible for such groups to influence the governance of companies, and provide reasons for your opinion.

Company Law has evolved over the last 200 years. It seems that now there is a push towards the original incarnation of the company concept. The laws of the nineteenth century held "the view that directors were simply agents of 'the company' and subject to the control of the shareholder" (Ireland, 1999, p. 39). The ideals behind 'shareholder activism' appear to be leading back towards that perspective.
Cases and statutes produced varied interpretations of the Company entity. Alderson B said in the 1837 case of Bligh v. Brent (2 Y & C Ex. 268) "The individual members of a corporation are quite as distinct from the metaphysical body called "the corporation", as any others of his Majesty's subjects are" (Mayson, p. 4). This precedent led to the courts holding "that shareholders had no direct interest, legal or equitable, in the property owned by the company, only a right to dividends and a right to assign their shares for value." (Ireland, 1999, p 41).
In 1846 the case of Coleman v Eastern Counties Railway Co (1846) 10 Beav 1. the doctrine of ultra vires developed. This was a shareholder suit that prevented the directors of the railway company from using company funds to enter into a transaction that was not "for the purpose of constructing and maintaining the railway". Putney. Ultra vires (meaning 'outside the power of') was "developed principally to protect the integrity of the share as a form of property" (Ireland, 1999, p. 43). This shareholder showed that the actions of the directors were beyond the scope allowed them by the type of company they were directing, and this was backed up by the court.
The 1854 case of Watson v. Spratley (10 Ex. 222), determined that "shareholders, even in unincorporated joint stock companies, had no direct interest in the assets of their companies". This lead to "a legal space" emerging "between joint stock companies and their shareholders". (Grigg-Spall, Ireland, and Kelly).
From these three cases it can be deduced that a shareholder has no direct legal ownership in the company's assets, but still maintains a right to ensure the governance of the company is within boundaries. The theory of directors as agents for shareholders is one that is upheld by many shareholders today. Shareholders vote for the directors on

the company board, therefore they have employed the directors as governors of their investment. Shouldn't the directors, therefore, be governing the company with a view to increasing shareholder wealth by way of dividend and increased capital value?

1856 Companies Act (19 & 20 Vict. c 47), known as the Joint Stock Companies Act, put into statute "that people 'formed themselves' into companies, with its implication that companies were made of, rather than by, them." (Ireland, 1999, p. 39). This was refined, and the following statute was the 1862 Companies Act (25 6r 26 Vict. c. 89) where "people no longer 'formed themselves' into incorporated companies, they 'formed' incorporated companies, objects external to them, made by them but not of them." (Ireland, 1999, p. 42). From this point onwards the 'separate entity' concept was clearly defined. The test case for this 1862 Companies Act is Salomon v Salomon & Co Ltd ([1897] AC 22), where the court reiterated the concept of a company being a separate legal entity form the owners or shareholders, even if all the shares are held by a single shareholder.

Company Law changes have not changed the concept of 'separate legal entity'. The indemnity from personal liability for the company's debts has appeared to have countered the ability of shareholders to play a role in a publically listed company's direction.

An article by Anabtawi and Stout (2008) discusses the factors that inhibit individual shareholders with small shareholdings. The reasons discussed are summated into two key prohibitors: legal, fear of defeat by the company's proxy rules; and economic, it does not make sense to take a role as the individual investment is so small, and they would not have an influence, and the financial cost of mounting a challenge against the directors. This has been overcome to a degree by institutional investors - managed portfolios where one investor may only have a small stake, but as a group of investors the portfolio manager controls a more significant proportion of shares. This overcomes the issues of geographically disperse investors, as they are grouped together through an investment portfolio. Financial cost to the large shareholders is proportionately lower than it is to an individual small shareholder. The net social benefit of this expenditure should be seen to outweigh the cost. Social benefit can be seen as "large shareholders provide a public good and that they incur a private cost in doing so." (Admati, Pfleiderer and Zechner, 1994, p. 1102).

Institutional investment is behind the trend to revisit a more 'hands-on' role in shareholding. Institutional investors control a larger proportion of shares than many individual investors could have. They have the experience, and, in most cases, the education to understand shareholder reports, and identify the positives and negatives within company documentation. They become the voice of a group of shareholders, and push directors to ensure they are working in the best interests of that shareholder group. The influence these institutional investors have has lead to governance monitoring and shareholder activism.

"Monitoring by large shareholders typically involves identifying companies whose actions are in conflict with shareholders' interests and attempting to bring about change through negotiation with management, proxy fights, and involvement in the choice of board members." (Admati, Pfleiderer and Zechner, 1994, p. 1099). Shareholder monitoring of companies is undertaken predominantly by the institutional investors and other large shareholders in order to protect their investment. The flow on effect from monitoring is reassurance for the individual investors, leading to confidence in the directorship of the company. Monitoring the management and board of a company is a tool used to identify any 'need for change'. Once an issue is identified through monitoring, the next step is 'Shareholder Activism'.

Shareholder activism is the conscious act of lobbying the board and management of a company in order to attain a goal. Active shareholders in a company are taking themselves back to the earlier ideal of owners participating in their business. This can be seen to be an attempt to blur the lines between company and individual, or a positive step towards protecting their investments.

Smith (1996) analyses the effect of shareholder activism on targeted companies. Among the measures instituted are the success rates on changing corporate governance structures and changes in the firm's management, as well as the changes in stock prices and operating performance. The findings indicate that targeting companies is likely to result in changes to corporate governance, and lead to increased value to stock holders. Operating performance is not statistically linked to shareholder activism. "72 percent of targets either adopted proposed governance structure resolutions or made changes sufficient to warrant a settlement." "Overall, the evidence indicates that shareholder activism is largely successful in changing governance structure and, when successful, results in a statistically significant increase in shareholder wealth." (Smith, 1996, p. 251).

CalPERS is the California Public Employees Retirement System. It has over 1.6 million members. As an institutional investor, CalPERS has a significant influence over many investment options, and within this role it is "devoted to educating and influencing shareowners, corporations, regulatory authorities, and other institutional investors on market-wide issues that will significantly improve ethical responsibility, accountability and transparency in the marketplace." (CalPERS, 2009). CalPERS' model for monitoring and targeting companies has been analysed by many business researchers. Wilshire Associates Incorporated consultant, Andrew Junkin, has evaluated the effectiveness of CalPERS targeting on the corporate governance of 139 companies between 1997 and 2007. CalPERS identified through monitoring that "many corporate assets are poorly managed and that resources spent on identifying and rectifying those cases can create substantial opportunity and premium returns for active shareholders." (Junkin, 2009, p. 10).

Junkin also has statistically ranked the performance of these companies, and found that "CalPERS' involvement has had an impact on the stock prices of the targeted companies and, at a minimum, has slowed the erosion of shareholder value on a cumulative basis." (Junkin, 2009, p. 7). The influence of this shareholder group on the companies it invests in is significant and shows the effectiveness of this shareholder's influence on corporate governance. The slowing of the "erosion of shareholder value" leads to greater confidence in the companies targeted by the other 'small' investors. This proves that the employing the concept of good corporate governance is beneficial to companies, management and boards, as well as share value and ultimately all shareholders. Other companies could learn from this research and consider implementing active shareholder initiatives in order to obtain similar benefits.

Russo and Turner (2009) discuss the benefits of an active shareholder engagement model, with examples from Schering-Plough, a pharmaceutical company. The goal of this program was to "stay in tune with shareholders." Understanding the needs of their shareholders enabled a comprehensive framework for decision making and the disclosures that would be valuable to their shareholders. The value of including shareholders' needs has proved to be beneficial, and the program has been continued through their merger with Merck. "The focus was on listening to investors and learning from their perspectives." (Russo and Turner, 2009, p. 12). Two way communications with shareholders has been the key to successful implementation of this active shareholder engagement policy. Schering-Plough promotes the fact that "the company almost never declines a shareholder request to engage on a governance topic, and they have also initiated engagements." (Russo and Turner, 2009, p. 13). "We believe all shareholders deserve the trust of the Board, Management and employees. We do not assume they have adversarial intent just because they have a different view on a particular issue." (Russo and Turner, 2009, p. 14). This is not to say that implementing and maintaining a shareholder engagement program is a simple process. An investment of time and finances is necessary in order to ensure a timely and relevant flow of information both ways.

> "Establishing and maintaining a robust shareholder engagement program is not easy. It demands time from management, the CEO and the board. It requires a steady allocation of resources. And it takes flexibility and continuous re-adjustment. But the rewards of staying in tune with shareholders are many, and very valuable, for the business and for all stakeholders of a company." (Russo & Turner, 2009, p. 16).

There is also the consideration of relevance of the information sought by shareholders, and the impact any changes suggested would have on the company and on other shareholders. Shareholders are individual human beings and as such will have individual opinions and perspectives on all issues. "Like other issues in management, such as organizational structure, the interests of shareholder activists are subject to their time and societal context, that is, to the fads and fashions of social policy and the changing public policy agenda. "(Graves, Rehbein, and Waddock, 2001. p. 299). The effect of 'fads' in business and in society will sway the issues that shareholder activists and institutional investors are concerned with. Most 'fads' will roll around in a cycle. Graves, Rehbein, and Waddock, (2001) have shown that many issues for shareholder resolutions in companies will follow political and societal issues closely. The resolutions proposed cover such diverse hot topics as apartheid, abortion and tobacco. Corporate governance appears to be the latest consistent issue for shareholder resolutions. "The issue of governance is not addressed at all until 1993 (with 2 resolutions) and then receives relatively consistent attention thereafter," (Graves, Rehbein, and Waddock, 2001. p. 306). This trend has been brought to the forefront by the public awareness of institutional investors' insistence on targeting this issue. "Clearly, the decisions that these institutional investors make-whether on their own behalf or on behalf of their beneficiaries-will have a profound effect on the governance and performance of the twenty-first-century corporation." (Ryan and Schneider, 2002, p. 569).

"There is widespread agreement that shareholders have an important role to play in ensuring good governance." (Ireland, 1999, p. 32). It is therefore advisable for all companies to observe the trends of not only business, but to consider the political, legal, and social issues relevant to: the business environment in which they operate; the financial environs of their institutional investors; and the lives of their individual shareholders. "Even for companies not currently subjected to shareholder resolutions, there is probably a degree of usefulness in watching the trends in shareholder activism as they may predict future areas of legislative or regulatory action that will affect all companies in an industry." (Graves, Rehbein, and Waddock, 2001, p. 312).

Directors and management teams of companies in New Zealand should be aware of these overseas trends back to shareholder 'ownership' because "there can be little doubt that corporate managers are increasingly subject to institutional investor scrutiny and increasingly aware of the importance, not least in terms of their own survival, of maintaining share price and enhancing 'shareholder value'." (Ireland, 1999, p. 51). A shareholder, or group of shareholders, who feels included and involved with the decision making within their investment should then feel more confident in his investment and be less likely to actively lobby for change. This will lead to enhancement in overall market certainty, which will be of benefit to the business environments in New Zealand.

On consideration of all the sources documented in this essay, it is possible for groups of shareholders to influence the governance of companies. It is not a simple process and requires either: actively monitoring and targeting boards, from a position of influence, in order to achieve results; or investing in a company that has an existing shareholder engagement policy modelled on the one implemented by Schering-Plough. The research shows that there are benefits for the company as well as for the shareholder, of involving the 'owners' in the running of the business. Shareholders need to undertake the responsibility of being informed and keeping up to date in order to provide relevant issues for management consideration. “Greater shareholder power should be coupled with greater responsibility.” (Anabtawi and Stout, 2008, p. 1256).

Alison Fletcher

Editor: We have a full list of references for any member who wishes to pursue this subject.

BOARD REPORT FOR DECEMBER- JANUARY

The board always reviews financial, management, and Scrip and Corporate liaison reports, but the following points are noted for the general interest of members.

1. Branch attendance: Robin Harrison of Christchurch was our branch attendee for December, and he supplied insight into South Island activities.

2. NZSA comments on the acquisition by Allied Farmers of Hanover Finance. The dangers of this combination to debenture holders in Hanover have been highlighted publicly by the Securities Commission and other commentators. NZSA (Bruce) was as usual early on the scene before voting by Hanover or Allied, and potential legal action involving the Association was avoided by agreement with Chapman Tripp of a correction to the parts of Bruce’s comment which were deemed to be misleading.

3. Members’ Research on individual listed companies: The appeal for volunteers to track company changes was placed on hold, pending further consideration of the role of the website, and liaison with company management to supply published results in our prescribed format.

4. Board renewal: NZSA board is considering motions for the removal of some directors, and support for the efforts of Springboard, an organization which aims to enable younger candidates on to boards and community trusts.

Alan Best

CORPORATE LIAISON FOR 2010.

For the coming year I have set down some key objectives I want to achieve for the NZSA.

The first one is reviewing the remuneration packages being paid to the Managing Director of each company. Depending on the size of the company I am keen to see the basic pay of Managing Director kept to within 10 to 20 times of the average pay earned by the rest of the employees in that company. With regard to short term bonuses they should represent no more than 30% of the Managing Directors basic salary. The exception may be where a major capital program is taking place like a new factory, building etc is being built and a bonus is being paid to stay within the time limit and cost budget.

Long term bonuses should be based on the average results achieved over at least 3 years and preferably 5 years. As one year ends another is added so the incentive is for long term results. I am keen to see key performance indicators (KPI`s) based on goals that can be easily measured and are in line with shareholders returns.
Over the last few years directors have paid to much attention to what outside consultants have recommended what they should be paying their senior executives. Often the packages and bonuses have had no bearing on medium to long term results. As shareholders we need to be more pro-active at AGM`s in voting down any

recommendations made by the chair person which are not in line with future share holders returns.

The second is the appointment of Directors.

Although some progress has been made in voting out under performing directors we still have a long way to go in making the changes necessary to improve the quality of directors on many of our public companies.. Appointment of directors is still being influenced either by the current chair person or outside consultants. I often hear from directors they would like to appoint more women, but claim the talent pool is just not there. The same comments are made about people with other qualifications like science, engineering, marketing etc. This is just not true and they will never find new talent unless they start looking further a field than what is occurring at present.
Feed back from members on individual directors would be appreciated. We should also look closely at the qualifications and experience on each board.

The third is to work with other parties who have similar goals to our members. As an example now ACC and the Superannuation Fund are becoming large investors in many New Zealand companies they will be keen to ensure companies are performing to an acceptable level. We may be able to get support from them with regard to the above issues.

Des Hunt

GOVERNANCE – WORDS OR ACTIONS

In 2009, Grant Diggle, while he was still CEO of CSNZ summarised his organisations findings over NZX listed companies. This is a précis of his report. Members are encouraged to look at key companies in their portfolio to see how they measure up now.

We have examined the Annual Reports of most of the NZX main board for 2007/2008 to determine how they compare in the area of corporate governance. We excluded non-trading companies and those who do not have a physical operating presence in New Zealand.

We looked at 127 companies and in particular the following aspects of their Reports:-

1. Corporate Governance Statement and how they related this to the 9 Principles of Corporate Governance published by the Securities Commission.
2. Board Evaluation process.
3. Corporate Social Responsibility Statement and its subsets of Environment and Sustainability.

Corporate Governance Statement and the 9 Principles of Corporate Governance
The Securities Commission first set out a road-map to good governance in 2002. We would therefore expect a public lister to be fully aware of the Principles and be able to report whether and how it complies with each Principle or explain why and how it does not comply.

Sadly, of the 127 Reports, 3 did not even contain a Statement, and 10 made no mention of the 9 Principles. A further 9 had a minimalist approach, such as, and we quote from one Report:-

"The Company's corporate governance policies comply with the NZX Corporate Governance Best Practice in all respects."
Surely, a classic example of, "Trust us, we know what we are doing".

However, those companies also listed on international stock exchanges where the reporting standards are far more rigorous and robust did a fair job of explaining themselves.

Each Principle (10 in the case of the ASX) is set out and how the company complies with this. For example:-

"Principle 5: Make timely and balanced disclosure
The company is committed to promoting investor confidence by providing forthright, timely, accurate, complete and equal access to information in accordance with the NZSX and ASX Listing Rules. The company has a formal policy designed to ensure this occurs. That policy can be found on the company's website.

The corporate secretary is the company's market disclosure officer, and is responsible for monitoring the company's business to ensure compliance with its disclosure obligations. Managers reporting to the chief executive officer are required to provide the corporate secretary with all relevant information, to regularly certify that they have done so and made all reasonable enquiries to ensure this has been achieved.

The corporate secretary is responsible for releasing any relevant information to the market once that has been approved. Financial information release is approved by the audit and risk committee, while information release on other matters is approved by the chairman of the board and the chief executive officer.

Directors formally consider at each board meeting whether there is relevant material information which should be disclosed to the market."

Some companies go further than the basic requirements and set out other policies. Contact Energy Limited sets out its whistleblowing policy as follows:-

"Whistleblowing Policy
Contact's Whistleblowing Policy, available on the company's website, facilitates the disclosure and impartial investigation of any serious wrongdoing. This policy advises employees of their right to disclose serious wrongdoing, and sets out Contact's internal procedures for receiving and dealing with such disclosures. This policy is consistent with, and facilitates, the Protected Disclosures Act 2000."

A small number of companies have a Policy Manual, or Board Charter that specifies their process in detail. Contact sets out its governance practice in the form of a schedule measured against Best Practice Codes. Such schedules provide a helpful point of reference to determine the company's adherence to best practice.

Board Evaluation
Given the attention Boards place on evaluating the Chief Executives and others in their organisation, we can only conclude this is a case of "Physician – heal thyself".

Of the 127 companies, 61 made no mention of an evaluation process. The others had either an internal or external process or a combination of both. One company stated it was not undertaking an evaluation at the present time. At least this Board had taken the trouble to consider the matter.

One company that clearly states what it is doing is CDL Investments NZ Limited:-

"Evaluation Process
The Board has a formal annual evaluation in respect of its own performance, its committees and individual directors. In respect of the Board and its committees, directors complete an evaluation questionnaire, developed in conjunction with external consultations. Responses from the process are collated by the Company Secretary, who compiles a report which is then presented to the Board. The performance of the executive and non-executive directors is assessed annually by the Chairman. During the year, the Board reviewed and acted upon the findings of the formal evaluation that was undertaken.
The independent non-executive directors, led by the Senior Independent Director, meet annually to evaluate the effectiveness of the Chairman."

Of course statements do not need to be lengthy. An example of a concise but meaningful statement is contained in the Trust Power Report:-

"Review of Board Performance
An annual review of the performance of the Board and individual Directors is undertaken by the Chairman. The Institute of Directors on-line survey is currently utilised as a mechanism for undertaking this review."

Corporate Social Responsibility
Whilst CSR is not mandated in New Zealand, as it is in other jurisdictions, nevertheless companies cannot afford to ignore it. Alas, 80 of the 127 (63%) made no mention and a further 5 had only a passing reference.

So, only 42 or around one third of companies considered CSR important enough to mention it in their Annual Report. Some of these companies made an excellent attempt to relate CSR and its subsets to their own organisation.

One such company was Smith City:-

"Environment
The Group is committed to introducing practices which will reduce harm to the environment. At the present time the Group recycles materials out of washing machines and refrigerators, collects and properly disposes of refrigerant gases and recycles packaging cartons and printer cartridges. The Group also assists with recycling second hand goods through the operation of its small chain of clearance centres. The Group has sought and where practical received assurances from its suppliers that furniture products

imported from overseas are manufactured from timbers grown in sustainable forests and not rain forests."

Another company that took the matter seriously and included a Sustainable Development Report within the CSR section of the Annual Report was Sanford Limited:-

"The definition of sustainability we subscribe to is that or wanting to ensure the needs of today are met without sacrificing the needs of tomorrow."

In summary, CSNZ believes whilst some Annual Reports do set out to inform stakeholders in a full and frank manner, too many are short on detail and substance and appear to be minimalistic.
The Directors of these companies should consider their wider responsibilities other than just to the Companies Act, Securities Commission and NZX Listing Rules requirements.

Voluntary disclosure can mean less mandatory disclosure. For CSNZ a voluntary code is preferable to a mandatory code. Directors who sign up to a voluntary code are more likely to make a meaningful and genuine contribution to the governance process than those forced to do so by the threat of sanctions.

All the same, we suggest the legislators, regulators and NZX have much work to do to raise the standards of corporate governance and reporting by listed companies.

Grant Diggle

WHAT'S COMING IN GOVERNANCE

Kevin McCaffrey has recently circulated information on what is happening across the Tasman in the field of executive remuneration and governance. While New Zealand still considers the separation of policing and disciplining functions from the Stock Exchange as a listed entity, Australia is forging ahead.

New "Diversity guidelines will probably take effect in the middle of this year, in which boards will have to disclose:
• Their achievement against the gender objectives set by their board; and
• The number of women employees in the whole organisation, in senior management and on the board.
Alongside the recommendations, changes will be made to the guidance commentary to:
• Encourage nomination committees of listed entities to include in their charters a requirement to continuously review the proportion of women at all levels in the company. Commentary will highlight that it is the responsibility of the nomination committee to address strategies on board gender diversity and diversity in general.
• Require that the performance review of the board include consideration of diversity criteria in addition to skills.
Also, boards will be required to disclose what skills and diversity criteria they look for in any new board appointment.

New rules for Executive remuneration will also be implemented. Australia is already way ahead of us in its disclosure requirements.

- Termination benefits (now fully defined) will require shareholder assent before the benefit is paid.
- Hedging of executive shares or options will not be allowed.

- If there is a 50% vote against the remuneration report, 2 years running, the full board must submit to reelection
- The details of any professional remuneration adviser must be disclosed.
- Institutional investors will be required to disclose their voting on the remuneration report
- The Remuneration Committee must work with the Risk Committee (Prudential Management)

A good checklist has been published for Remuneration Committees.
how the remuneration policy aligns with the company's strategy, its risk profile and shareholder interests;
how the mix of base pay and incentives relates to the remuneration policy;
how comparator groups for benchmarking remuneration and setting performance hurdles / metrics were selected;
how incentive pay arrangements were subjected to sensitivity analysis to determine impact of unexpected changes (eg in the share price);
whether any incentive plan constraints or caps to guard against extreme outcomes applies;
whether alternatives to incentives linked to complex hurdles have been considered (eg deferral of STI into equity);
whether employment contracts have been designed (to the degree allowed by law) to inoculate against the possibility of having to "buy-out poorly performing executives"; and
whether post-remuneration evaluations have been conducted to assess outcomes and the relationship to the remuneration policy.

As several of our larger companies are also listed in Australia, we can expect a few slow changes here. It is too much to hope that New Zealand could ever lead the way.

Alan Best

COMPANY AGMs AND PROXIES

WINDFLOW TECHNOLOGY AGM - 16TH DECEMBER 2009.

The financial shadow over this meeting had arisen from their dispute with NZ WindFarms (NZW) over whether the certification from the International Electrotechnical Committee (IEC) was required under the supply agreement and NZW who had deferred payments. The CEO, Mr Geoff Henderson, reported to the meeting that although the dispute continues some $1.8m had been released in November with more expected. In response to questions from the floor he clarified that the IEC certification process was proving to be lengthy because of the pioneering nature of their turbines and they were the first to apply for high ED3/1A certification but that "IEC documentation was now substantially completed and was under review by Lloyds Register". It was apparent that IEC certification would be crucial to the future success of establishing the Windflow technology in new markets. This would be vital to the longer term success of the company as it is currently totally dependent on the NZW contracts.
An audio recording of the full AGM is available from the investor relations section of the Windflow Technolgy company's website: www.windflow.co.nz/

Robin Harrison

SANFORD AGM – 27TH JANUARY, 2010.

A successful and well attended meeting of a well run company, which has now been in operation in a period since the late 19th Century (quite a feat for a NZ company).
The main comment from both the Chairman and the CEO was on the subject of the New Zealand Dollar which in present times operates very much to the disadvantage of Sanfords. The exchange rate was and continues at a consistently high levels -the result of big international money speculators placing their funds temporarily in NZ - pushing the value of the NZ dollar way above its fair and reasonable level vis-a-vis other currencies, and then repatriating their monies and untaxed profits when the occasion suits them, very much to the detriment of NZ firms selling their products on the international market. The company has and continues (to date unsuccessfully) to lobby the Government to tax such profitable and non export related money transactions. These representations will continue .
The Sanford shareholders do recognise that they hold stock in the NZ rarity; a long-enduring, successful business venture with a history of success in difficult export markets as well as in the local market.

Joe Turnbull

THE WAREHOUSE AGM - 27TH NOVEMBER, 2009.

Market cap ($m) 1,291 NZSA 25 proxies totalling 155,111 votes
Proxy Votes received by the Chairman represented 63.38%.
Chairman (since 1994) Keith Smith gave the opening 10 minute address for 2009 AGM which was webcast, perhaps being partly the reason for the less than expected shareholder attendance. Under the heading Confident Future, he reported that New Zealand's largest non-food retailer with 132 stores nationwide (86 red sheds + 46 stationery) had Warehouse sales for the year to 31 August 2009 of $1.53 billion, level with last year, and Warehouse Stationery at $187.2m being 6.2% down. The results need to be read taking into account there were 53 trading weeks in 2009 versus 52 in 2008. The Warehouse EBIT was $120.2m, up 6.2% on last year, while Warehouse Stationery had a tough year returning $1.6m versus $5.1m last year. Earnings per share were 24.9c, down on last year's 29.4c. The Board declare a final dividend of 5.5c bringing the total for the year to 21c with a further special dividend of 10c on account of accumulated imputation credits. The company is weathering the recessionary storm well and will come out of it in strong shape, although the economic outlook currently is still a little uncertain. Managing Director & CEO Ian Morrice (now in his 5th year at the helm) addressed the meeting for 25 minutes on Investing Long Term in which he focused on the opportunities available to Warehouse stores in a number of categories in which there are large markets but where The Warehouse currently has a small share e.g. online shopping (including a substantial gift voucher element), health & beauty, consumer electronics, jewellery, shoes, homewares, camping & fishing. The exit from food and liquor retailing means there are opportunities to reconfigure existing space. The 'Extra' name will be added to the 17 largest stores and 'Local' will be added to new small footprint stores being developed in smaller centres such as Mosgiel. Warehouse Stationery had a change of CEO in April 2009 with Mark Powell moving from The Warehouse to take up the reins in its sister company with plenty of challenges ahead. The Group is investing $3m in Project Invigorate, a staff training programme designed to have the Right People in the Right Place at the Right Time. The company's environmental programme has seen a 43% reduction in plastic bags and 16% reduction in carbon footprint. Looking ahead, the critical Christmas spend looks as if it will be late but will still happen. Question Time was remarkable for the few searching questions that were asked, being mostly about store

related experiences from some shareholders. One lady did however ask why Ian Morrice could justify a salary and benefits package of $3.8m in the midst of a recession. The Chairman replied that it was based on Australasian comparisons. Resolutions to elect Ian Morrice (appointed 2004), James Ogden (appointed 2009) and Janine Smith (appointed 2006) as directors were carried unanimously on a show of hands. Earlier in the meeting, the Chairman paid tribute to retiring director John Avery who has been a director since 1994. The Board was authorised to fix the Auditors (PricewaterhouseCoopers) remuneration ($411,000 for 2009 financial year). There were no further questions under General Business and the meeting closed at 11.00am. The NZSA was made most welcome at this meeting and had a well-positioned promotion stand manned by Jenny Merrylees at the back of the meeting room. I spoke to several of the directors and got the impression they are a well-balanced team with complementary skills.

Patrick Flynn
Editor's note: Many members will be aware that subsequent to this AGM, Keith Smith, the Chairman was named as a target for NZSA criticism. This prompted criticism of our views and demands some elaboration. Keith Smith has a background in "corporate recovery" the euphemism for receivership. He has therefore been invited to assist in various problem boards, and has generally commanded respect from his associates. Keith has been associated with The Warehouse since its first store opened in 1982, and has been Chairman since listing in 1994. He therefore shares responsibility for the abortive move into Australia. In 2009 this board conducted a full Institute of Directors review of its members and that assessment of Keith's performance was positive. Our main concern is, with the number and size of his commitments, he seems overloaded. However, he did lead the restructuring of Skellerup divesting 5 non-core businesses and then withdrew. NZSA is also pleased to see that he has withdrawn from the chair of Farming Systems Uruguay which pays a large management fee to PGG Wrightson where he is also chair. He is still on the board of both companies. However shareholders are not happy with the performance or the strategic direction of Tourism Holdings, and will continue to question the under-performance of his other charges.

SCOTT TECHNOLOGY AGM – 2ND DECEMBER 2009.

Introduction
Scott Technology designs and builds automated appliance production lines, and automated systems for the meat processing, mining and other industries.
The NZSA was assigned 146,811 votes from 9 shareholders. 50 to 60 people were in attendance.
The AGM was held at new purpose-built premises at 630 Kaikorai Valley Road, it being the 13th since the company was relisted in 1997. It is also their 97th year in business since founding in Dunedin (as J&AP Scott) in 1913.

Addresses
At the start of Chairman Stuart McLauchlan's address, both the NZSA and the press were welcomed to the meeting. He advised that after tax profit for the year was $265,000 on revenue of $31.3M.The previous year loss was $818,000 on $25M. Despite the $7M order subsequently cancelled (due to the deteriorating financial markets) following its announcement at the last AGM, the company had a very good order book heading into the new financial year.

In his address, CEO Chris Hopkins highlighted the change in 5 years from mainly supplying automated production lines (hit hard by USA downturn,) to also encompassing automated meat processing, mining industry sampling and automation, and industrial

automation. The first commercial sale of a stage of the automated lamb boning room has now been made. The beef boning system is showing good potential. A world first has been achieved with the repeat order for an automated sample preparation system for a commercial laboratory operating in the mining sector. Until now, automation attempts in this field have been unsuccessful.
Prospects being worked on come to $40M and are at a level not seen for some time. Another good sign was the resumption of dividends.

Resolutions
The re-election of 2 directors and fixing of auditors' fees were passed on a show of hands with no dissent.

NZSA Questions
On arrival for the AGM, I spoke with Chairman, Stuart MacLauchlan and CFO, Greg Chiles and put to them two requests from an NZSA member;
1.In order to allow shareholders to gain an understanding of the relative importance of the group's various activities, would it be possible to provide shareholders with enhanced segment information, with the segments focusing on the main activities of the group as stated in the managing director's report, i.e. appliance manufacturing systems, meat processing automation, etc.
Response: Making public segmented information by type/country becomes problematic owing to the nature of the business. One or two large contracts may make up a whole sector, thus making it easy for competitors gain information on margins, etc. made on specific contracts. CEO, Chris Hopkins presented some informative graphs covering this information in his address but, understandably, wished these to be kept in-house owing to commercial sensitivity.
2. Scott Technology exports a very high proportion of its output. Many companies in this position show the average exchange rates experienced during the year as well an indication of the sales made in each of their principal markets or geographical areas. Scott Technology could be encouraged to do likewise.
Response: Much of this will be covered by the IFRS8 accounting standard with which we will comply.

Answers to other shareholders' questions
- The $7M order cancelled is deferred - revivable.
- Scott Milktech Ltd (Dairy Industry) projects are ongoing and imminent positive results are expected.
- Re overdue debts (p26 Annual Report) – the situation has improved since reporting date. No bad debts have had to be written off in the last 3+ years. Exports are all paid for before the goods leave the country
- Re Research & Development - expensed or capitalized (p6 Annual Report)
    - expensed if outcome is as yet unknown (e.g. Scott Milktech)
    - capitalised if income stream current/imminent (e.g. X-ray & primal auto meat processing)
- A shareholder congratulated Graham Batts for achieving 40 years as a director.
- Rare event was noted - All directors had increased their sharehoding in the last year.
- The Joint Venture with Silver Fern Farms, while continually monitored (e.g. for conflict of interest) now that equipment is being sold to SFF's competitors, is presently working well. In fact the company may be a facilitator for the industry having had Alliance and SFF management in the same room at an Invercargill directors meeting!
- Employment of a Chinese national continues. A contract has just been finished in

China making 6 lines there now. Manufacturing in China is not being considered.

After the meeting we walked through to the factory where automated machines and robots were on view (some in demo mode) and explained. Here NZSA member, Bill Whitaker asked the Auditor why the over $6 million of goodwill was in the balance sheet unchanged from last year. He advised this was the current accounting practice and the goodwill was subject to an annual assessment.
Following the factory tour, tasty refreshments were offered, while several officers sought us out and discussed a wide range of matters with us.

Many thanks to Bill Whitaker for notes to help with this report.

Roscoe Lord

BRANCH REPORTS

AUCKLAND

Auckland branch would like to welcome everyone - especially all our new members - to the start of the 2010 programme. We are planning a full round of events. The details of our first meeting and company visit are set out below.
For those with busy calendars, the Branch meetings will be held on February 17, April 14, June 16, National AGM in mid July (tba), September 15 and November 10.
Meetings: The first meeting of the year will be held on February 17 at 7.00pm for a 7.30 start. The venue is the Hobson Room, Level 4, Alexandra Park. We will feature 2 speakers:

- **ING Property Trust** management Ltd. GM **Peter Mence** will update us on his vision and the future outlook for all sectors of the New Zealand Property market.
- Our own **Oliver Saint** will introduce us to **the Z Score formula** for analysing companies

Company Visits: The first visit this year will be to sharemarket-registry-company **Computershare** on Wednesday, 10 March 2010 at 10 am. The venue is 159 Hurstmere Road, Takapuna. This visit will be hosted by Computershare CEO Tim Bond.

Come and find out how a share registry works and the hear about the variety of other services Computershare offer to investors and companies. This visit is limited to a maximum of 20 attendees, so make sure you register promptly.

Anyone wishing to attend should contact Joe by email to rjyturnbull@xtra.co.nz or by phone on (09) 631 5071. Tim has requested that if there are specific questions requiring detailed answers these should be submitted in advance. Send questions to Uli Sperber uksper@gmail.com

The NZSA company visit programme is kindly sponsored by INFOSCAN

Education: The first of our education seminars kicks off at Glenfield College (Night classes) on February 22. Full details are on the Auckland Branch section of the NZSA website.

John Hawkins, Acting Chairman

WAIKATO
The 2009 year came to a very successful conclusion with Brian Gaynor speaking at our Xmas function on 2nd December. Brian addressed the importance of corporate governance and suggested that lack of shareholder participation (especially institutions) and ineffective regulators were responsible for the underperformance of large NZ companies and especially the NZX Top 10. Brian is very proud of his membership of NZSA (no 11) and thought it was doing a good job. Brian's comments with regard to the regulators were particularly scathing and hard hitting.
Following the address Brian took many questions. Of most interest to me was his response to the reason for the excellent performance of his Milford Asset Management Fund. His explanation was that most funds are ***relative funds*** in that they try to beat a particular index; whereas Milford was an ***absolute fund*** that tried to beat a benchmark of 10% return on Funds invested.
NZSA is very lucky to have the support of NZ's most eminent financial commentator, and we in particular are very pleased that he makes the effort to supports us in the Waikato by agreeing to come and speak to us on a regular basis.
Jim Haisman our events co-ordinator has put together an interesting programme for the first half of 2010.
In March - John Wilson, a Fonterra director; April - Bill Falconer, a professional company director; May - Dr Tim Rooke, first branch Chairman and recent Telecom director aspirant; June -Branch AGM, Bruce Sheppard.
The Committee looks forward to seeing our branch members at these events and is looking forward to another successful year.
Robert Foster – Branch committee

BAY OF PLENTY
Bay of Plenty branch has concluded its first committee meeting of the year with a planning exercise for future member meetings during 2010. Our first on the 26th February will commence with an address - What Will 2010 Bring? - by Hamish Coleman from Craigs Investment Partners followed by a member discussion. During March a suitable panel will provide a focus on the forth coming Tax / Capital Markets reforms and their implications. April has been set aside for a look and learn company visit to Comvita at Paeangoroa.

Consensus from BOP members has expressed satisfaction with the Australian Foundation Investment seminar held just prior to Christmas. This was a quality effort and the large attendance to the morning appreciated by the committee.

An update on our project - A Personal Record Of Matters Pertaining To My Estate.

The print run was 650 copies.

To date we have distributed 465 copies equating to 71% of the print run.

We need to sell only a further 5 copies to break even. Come on members!

Allen Smith - Chairman

WELLINGTON
We hold our meetings on the second Tuesday of each month and will have ten meetings this year, the first in February and the last in November, with a guest speaker presenting

at each meeting. Once again First NZ Capital has offered us the use of their meeting rooms in Fujitsu Towers on the Terrace. We really appreciate their ongoing support of the NZ Shareholders Association.
The first meeting this year is on Tuesday 9th when Ray "the bear" Jack will look at investing in 2010 – it looks like we are in for another challenging year!

The other activities this year will be representing NZSA at company AGMs held in Wellington and running shareholder education courses – details of these will be emailed out as they come to hand and will be published on the Wellington branch website page at www.nzshareholders.co.nz.

Martin Dowse - Chairman

CANTERBURY
We celebrated the end of last year with a "Christmas" event on 7th December in Christchurch. It was well attended and proved entertaining and even educational - with a prizes thrown in to add to the party spirit.
The Committee will be holding its regular monthly meetings to discuss events, evaluate outcomes and plan for upcoming activities. Currently we are making arrangements for two visiting speakers to address Branch members at meetings in March and April. Details of these events are still to be finalised but members should be notified by the end of February. As always check our "Events" section under the Canterbury Branch heading of the NZSA web site for more information.
We have been mindful that as the only active committee in the South Island we should try to encourage greater involvement by members in other SI areas. To facilitate this we have been in contact with members in Otago and at the top of the South Island. This has already resulted in representation at company AGMs in Dunedin (see the report on Scott Technology) and Blenheim. We are hoping to encourage more active satellite grouping in the future.
Robin Harrison - Chairman

BRANCH CONTACTS

Auckland	Noel Thompson	tiricrest@clear.net
Waikato	Alex Eames	alex.eames@xtra.co.nz
Bay of Plenty	Allen Smith	allen.smith@wave.co.nz
Wellington	Martin Dowse	martin@dowsemurray.co.nz
Canterbury	Robin Harrison	robin.harrison@canterbury.ac.nz

MEMBER'S ISSUES

Auckland Energy Consumer Trust.
This Trust held its AGM for beneficiaries on Thursday Oct 29.
The trust owns 75% of Vector on behalf of energy users in Auckland & Manukau Cities together with northern Papakura.
If you are an income beneficiary then you might be surprised to know that between 3.5% & 5% ($3.5 -$5 million) is deducted from your cheque by the trust to cover its costs.
The Trust lacks transparency in its operation. For example the minutes of last year's AGM signed in November 2008 were not posted to their website & it was only after a strenuous conversation that I was able to get the 2009 accounts posted there a week before the meeting –they had intended just handing them out.
Their accounts are difficult to follow as they consolidate them with Vector's.

Their minutes routinely fail to cover the sometimes vigorous discussion at the meetings. This year the meeting followed the usual pattern of the Chairman applauding the trust's efforts in paying out a dividend .This was followed by Vector presentations about fibre optics & undergrounding. The latter drew considerable adverse comment about its snail pace (100km done in 8 years). The audience was unable to get any clear picture as to the time frame for completion.
Discussion on the accounts drew criticism about the level of Vector debt & that apart from windfall gains the NPAT was regularly less than the dividend.
The trustee fees which range from 50% (chairman) to 66% (others) of the Vector directors' fees were criticised as being unreasonably high. The Chair defended the fees on the grounds of the involvement of the trust in major Vector decisions.
The top table seemed extremely defensive & the Chair (Warren Kyd) tried to stifle adverse comment.
I am giving these notes in the hope that it will stimulate interest in coming to next year's meeting .The meeting is always late October & details of it normally appear in the documents with your dividend cheque.
Tony Sullivan
Editor: Advocacy around the Community Trusts seems a worthwhile extension of NZSA's mission amongst listed companies. We are hoping that Tony will jog our memories the next time this trust hustles through its agenda of self preservation.

FEATURES INDEX

ISSN: The National Library has allocated the International Standard Serial Number 1179-4275 to The Scrip so that researchers will have ready access to our material.

Copying from our website:
Members who wish to preserve hard copy of articles or parts of articles for their personal use and reference can do this simply by running a curser over the required passage to highlight it, cutting or copying it with the edit function of the programme, and then pasting it on to a word document in their own files. However publication of excerpts may not be done without the writer's permission.

Disclaimer:
Comments or information contained in this newsletter or other editions of The Scrip, or within courses conducted by the NZ Shareholders Association including related course books, should not be construed as providing investment advice under the provisions of the Securities Markets Act of 1988 or its Amendments of 2008. The point of our activities is to provide you with the tools needed to enable you to assess investment proposals, and decide for yourself.