

# Corporate Governance

Shareholders and other readers of this report should note that in the context of this report, and this section of this report in particular, the term and title “chief executive officer” (CEO) has the same meaning as the terms and titles “acting managing director” and “managing director” that may be used elsewhere in the report. Since the resignation of former chief executive officer (CEO) Greg Muir, in July 2003, Stephen Tindall has temporarily assumed the powers and responsibilities of the role of CEO preferring to adopt the title “acting managing director” until a new chief executive officer is appointed. Stephen Tindall was the company’s managing director from 1994 until January 2001.

## Role of the board

The board of directors (“the board”) of The Warehouse Group Limited (“the company”) is elected by the shareholders to supervise the management of the company and its subsidiaries.

The focus of the board is to enhance the interests of shareholders and other key stakeholders and to ensure the company is properly managed. The board draws on relevant best practice principles of corporate governance to assist and contribute to the company’s performance.

The functions of the board include:

- Reviewing and approving corporate strategies and the annual budget.
- Overseeing and monitoring organisational performance and the achievement of company strategic goals and objectives.
- Monitoring management’s performance relative to these goals and plans having delegated day-to-day management of the company to the chief executive officer.
- Monitoring financial performance including approval of the annual and half-year financial reports, and liaison with the company’s auditors.
- Appointing and annual assessing of the performance of the chief executive officer and the members of the senior executive team.
- Ensuring that there are effective management processes in place, and approving major corporate initiatives.
- Promoting and authorising ethical and responsible decision-making by the company.
- Identifying and ensuring that the significant risks facing the company and its controlled entities have been identified, and that appropriate and adequate control, monitoring and reporting mechanisms are in place.
- Reporting to shareholders.

## Delegations

While the day-to-day responsibility for the operation of the business is delegated to the executive management, there are a number of matters which are required to be, or that in the interests of the company should be, decided upon only by the board of directors as a whole. The board has therefore formally adopted a list of “Matters Reserved for the Board” for which no delegation is permitted. A copy of this list is available on the company’s web site: [www.thewarehouse.co.nz](http://www.thewarehouse.co.nz).

Delegations to the chief executive officer are reviewed on an annual basis.

## Board operations and membership

The composition of the board is determined in accordance with the following principles and guidelines:

- It should comprise at least seven directors of whom a majority should be non-executive. As at the signing of the annual report the board consisted of two executive directors and seven non-executive directors.
- The chairman must be a non-executive director.
- The directors should have an appropriate range of qualifications and expertise.
- The full board should meet at least nine times a year, and follow meeting guidelines set down to ensure all directors are made aware of, and have available, all necessary information for them to participate in an informed discussion of all agenda items.
- The full board also participates in a two-day strategic planning meeting, a two-day off-site operational visit, and other company-related events as requested by the chairman, including The Warehouse annual conference.

The company Constitution sets out policies and procedures on the operation of the board including the appointment and removal of directors. The board supports the concept of the separation of the role of chairman from that of the chief executive officer. The chairman’s role is to manage the board effectively, to provide leadership to the board, and to interface with the chief executive officer.

## Criteria for determining the independence of board members

Under the ASX Corporate Governance Council guidelines a company must identify which directors are “independent” based upon pre-determined criteria. Accordingly, the company recently updated its criteria for determining whether directors will be considered executive, non-executive or independent.

The following criteria have therefore been adopted by the company to assess whether a non-executive director is considered to be independent.

A non-executive director is considered to be "independent" providing he or she:

1. Does not hold more than ten percent of the company's voting shares.
2. Has not been employed in an executive capacity by the company within the last three years, or has been a director after ceasing to hold any such employment.
3. Is not a principal or employee of a professional advisor to the company and/or its entities whose billings exceed five percent of the advisor's total revenues.
4. Is not a significant supplier to or customer of the company. (A significant supplier is defined as one whose revenues from the company exceed five percent of the supplier's total revenue; a significant customer is defined as one whose purchases from the company exceed five percent of the customer's total purchases.)
5. Has no material contractual relationship with the company.
6. Has no other interest or relationship that could interfere with his or her ability to act in the best interests of the company and independently of management.

On 4 September 2003 the board resolved that:

- A majority of the members of the audit committee shall be independent directors.
- A majority of the members of the remuneration, talent and nomination committee shall be independent when director nominations are considered.
- All members of the corporate governance committee shall be independent directors.
- The audit committee shall comprise only non-executive directors.
- All board committees shall be chaired by an independent director.

The company acknowledges the importance of having independent directors as determined by objective criteria. However, a balance is required between having board members with first-hand experience of

the business and ensuring the company has the correct balance of skills to optimise the financial performance of the company and maximise returns to shareholders.

The chairman of the company – K R Smith – is classified as a non-executive director under the above criteria. While he is an independent trustee of the Tindall Foundation, which is a substantial security holder of the company, Mr Smith does not hold a beneficial interest in those shares. Mr Smith is also a non-beneficial trustee for 1,201,428 shares held by various family trusts. The board considers that while Mr Smith is not independent, as defined by its criteria, it is in the best interest of shareholders to retain Mr Smith's skills as a non-executive chairman.

The current board and committee memberships are detailed below together with the independence classification based upon the criteria for determining independence of board members.

### **Terms and conditions of appointment and retirement of non-executive directors**

The terms and conditions of the appointment and retirement of any new non-executive or independent director are set out in a letter of appointment which prescribes:

- Remuneration.
- Term of appointment, subject to shareholder approval.
- Expectation of the board in relation to attending and preparing for all board meetings and board committee meetings.
- Procedures for dealing with conflicts of interest.
- Availability of independent professional advice.

### **Board nominations**

The procedures for the appointment and removal of directors are governed by the company's Constitution. The remuneration, talent and nomination committee is delegated the responsibility of identifying and nominating, for the approval of the board, candidates to fill board vacancies as and when they arise.

## **Board composition**

as at 4 September 2003

<b>Director</b>	<b>Membership classification</b>	<b>Committee membership</b>		
		<b>Audit committee</b>	<b>Remuneration, talent and nomination committee</b>	<b>Corporate governance committee</b>
Keith Smith	Non-executive (Chairman)	Member	Member	–
Stephen Tindall	Executive	–	Member	–
Glen Inger	Executive	–	–	–
John Avery	Non-executive	Member	–	–
Joan Withers	Independent	Member	Chairman	Member
Graham Evans	Independent	Member	Member	Chairman
Neil Plummer	Non-executive	–	–	–
Rob Challinor	Independent	Chairman	–	Member
John Dahlsen	Independent	–	–	–

### **Retirement of directors**

The Constitution specifies that in each year one-third of the directors, or if their number is not a multiple of three then the nearest number to one-third, shall retire from office and may offer themselves for re-election at the annual meeting. The directors to retire shall be those who have been longest in office since they were last elected or deemed elected.

While the Constitution provides for the payment of retirement benefits to directors the company has not paid a retirement benefit since listing in 1994. Shareholders at the 2003 annual meeting will be asked to vote on a resolution that would require any retirement allowances to be approved by shareholders.

### **Board performance review**

On a regular basis the chairman, with assistance from the general manager, people, formally assesses the performance of individual directors whilst directors also assess the collective performance of the board and the performance of the chairman.

In September 2003 the board met and reviewed the findings of the recent board performance review. That review identified a number of opportunities for improvements for which action plans have been set. The next board effectiveness review will be conducted in early 2004.

### **Board committees**

Following the formation of a corporate governance committee in May 2003, and recommendations on governance from that committee to the main board, new board committee responsibilities, terms of reference and membership were agreed.

The board has three formally constituted committees: the audit committee, the remuneration, talent and nomination committee and the corporate governance committee. The disclosure committee is a committee of management and directors. Copies of the terms of references of all committees are available on the company's web site: [www.thewarehouse.co.nz](http://www.thewarehouse.co.nz).

### **Audit committee**

The audit committee is a committee of the board of directors. The committee must have at least three members, be comprised of only non-executive directors, and the majority must be independent directors. The chairman of the committee must also be an independent director. The charter was reviewed in September 2003.

The members of the audit committee are:

- R L Challinor, chairman
- K R Smith
- J Withers
- G F Evans
- J R Avery

Messrs Smith and Challinor are Fellows of the New Zealand Institute of Chartered Accountants.

The main responsibilities of the audit committee are to:

- Review and report to the board on the annual report and the half-year financial report.
- Assist the board to review the effectiveness of the organisation's internal control environment covering:
  - Effectiveness and efficiency of operations.

- Reliability of financial reporting.
- Compliance with applicable laws and regulations.
- Determine the scope of the internal audit function and ensure that its resources are adequate and used effectively, including co-ordination with external auditors.
- Oversee the effective operation of the risk management framework.
- Recommend to the board the appointment, removal and remuneration of the external auditors, and review the terms of their engagement, and the scope and quality of the audit.
- Review and approve, within established procedures and before commencement, the nature and scope of non-audit services being provided by the external auditors.

In fulfilling its responsibilities the audit committee receives regular reports from management and the internal and external auditors. The committee meets with the internal auditors at least three times a year and with the external auditor at least twice a year. The committee has an opportunity to meet with external auditors without management of the company being present.

The internal and external auditors have a clear line of direct communication at any time to either the chairman of the audit committee or the chairman of the board, both of whom are non-executive directors. The committee met four times during the year.

### **Remuneration, talent and nomination committee**

The remuneration, talent and nomination committee is a committee of the board of directors. The majority of the committee are independent directors where the committee is considering director nominations, and the chairman of the committee must be also be an independent director. The charter was reviewed in September 2003.

The committee is responsible for determining and reviewing compensation arrangements for the directors, the chief executive officer, and the executive management team. The committee is also responsible for reviewing the structure, size and composition of the board, and identifying and nominating candidates for the approval of the board.

The members of the remuneration, talent and nomination committee are:

- J Withers, chairman
- K R Smith
- G F Evans
- S R Tindall
- Plus another independent director where the committee is considering director nominations.

The committee met four times during the year.

### **Corporate governance committee**

The corporate governance committee is a committee of the board of directors comprised of independent directors. The charter was reviewed in September 2003. This committee was established to ensure that the company maintains a high level of corporate governance through continuous monitoring of international corporate governance best practice as promulgated by the relevant authoritative bodies.

The committee is responsible for developing recommendations to the board on corporate governance matters, undertaking an annual review of the alignment of the board's governance systems with best practice, determining the independence of directors, approving the corporate governance statements in the annual report, and reviewing the company's disclosure policy.

The members of the corporate governance committee are:

- G F Evans, chairman
- J Withers
- R L Challinor

The committee met three times during the year.

### **Disclosure committee**

The disclosure committee is a committee of board directors and management. The committee is responsible for ensuring the company meets its disclosure objectives under the Australian Stock Exchange Listing Rule 3.1 and the New Zealand Exchange Listing Rule 10.1. The company has a written continuous disclosure policy; this policy outlines a formal procedure for dealing with potentially price-sensitive information and involves referrals to a disclosure committee.

The board firmly believes that shareholders and the investment market generally should be promptly informed of all major business events that influence the company.

The members of the disclosure committee are:

- K R Smith, chairman
- R L Challinor
- S R Tindall, acting managing director
- The chief financial officer
- The secretary to the board

Information is communicated to shareholders in the annual report and the interim report. The company also reports quarterly, through the Australian Stock Exchange and the New Zealand Exchange, on store sales and other announcements in accordance with continuous disclosure rules.

Shareholders are invited to attend the company annual meeting which is usually held towards the end of November. The board encourages full participation of shareholders at the annual meeting to ensure a high level of accountability and identification with the company's strategies and goals. Shareholders are provided with notes on all the resolutions proposed through the Notice of Annual Meeting each year.

Investors can obtain up-to-date information on the company's various activities from its web site: [www.thewarehouse.co.nz](http://www.thewarehouse.co.nz). This site contains recent announcements, presentations and reports, including all major notices to the Australian and New Zealand stock exchanges.

### **Audit independence**

The board has adopted a policy and procedures for audit and non-audit work that may be performed by the external audit firm.

The key principles arising from that review, and so adopted by the company, are:

- The external auditor must remain independent of the company at all times and comply with Professional Standards F.1 (Australia) and ICANZ Code of Ethics and ICANZ EG1 Guide to Objectivity.
- The external auditor must monitor its independence and report to the board that it has remained independent.
- The company will not recruit the audit partner or other members of the external audit firm into finance roles within the company.

The company has developed a set of procedures for the external audit firm and their related firms and has implemented a set of guidelines on

what non-audit services are permitted and not permitted by the audit firm in respect of the company.

The audit firm may provide audit and audit-related services that, while outside the scope of the statutory audit, are consistent with the role of auditor. Examples include financial audits and audits of regulatory returns and prospectuses.

The audit firm will not provide services that are considered to be materially in conflict with the preservation of the independence of the auditor. These include investigations and consulting advice and subcontracting of operational activities normally undertaken by management, and where the auditor may ultimately be required to express an opinion on its own work. Examples include preparing accounting records and financial statements, designing or implementing new IT systems or financial controls, valuation services and taxation advice.

The audit firm may be permitted to provide non-audit services that are not considered to be in conflict with the preservation of the independence of the auditor subject to the approval of the company audit committee. The company audit committee will specifically confirm activities in this category. Examples include internal audit activities capped at fifty percent of total internal audit work, advice on appropriate accounting standards, and the review of new legislation and advice on its application to the company. The value of non-audit work is reported at every board meeting.

Auditor's remuneration is disclosed in Note 6 to the financial statements.

The company continues to closely monitor developments in the areas of audit and threats to audit independence to ensure its policies and practices are consistent with emerging best practice in these areas.

### **Independent professional advice**

Directors and board committees have the right, in connection with their duties and responsibilities, to seek independent professional advice at the company's expense. Prior written approval of the chairman is required.

Independent professional advice includes legal advice and the advice of accountants and other professional financial advisers on matters of law, accounting and other regulatory matters but excludes advice concerning the personal interests of the director concerned (such as service contracts with the company or dealings in the company's securities or disputes with the company). Any advice obtained under this procedure will be made available to the other members of the board.

### **Board meetings**

#### **Scheduling and selection of agenda items for board**

Board meetings are scheduled in advance. The chairman of the board and the company secretary draft the agenda for each board meeting and distribute it seven days in advance to members of the board. Each board member is free to suggest the inclusion of items on the agenda.

#### **Board presentations and access to team members**

The board has complete access to any company team member. The board encourages management to schedule presentations at board meetings by managers who:

- Can provide additional insight into the items being discussed because of their personal involvement.
- Have future potential that management believes should be demonstrated to the board.

## Remuneration

A board committee – the remuneration, talent and nomination committee – makes recommendations to the board on salaries and incentive programmes, and more generally on group issues, plans and policies relating to people management.

### Non-executive directors' remuneration

The fees payable to non-executive directors are determined by the board within the aggregate amount approved by shareholders. The committee considers the advice of independent remuneration consultants when setting remuneration levels. Total remuneration available to non-executive directors is fixed by the shareholders at the annual meetings. The current directors' fee pool limit is \$489,000 which was approved by the shareholders at the annual meeting on 29 November 2002. Certain named directors can forego up to \$10,000 of fees to acquire share options in the company.

Details of the remuneration paid to directors, and other benefits provided by way of salaries, bonuses and exercising share options, are disclosed in Note 5 to the financial statements "Directors' remuneration".

### Senior executive remuneration

Senior manager remuneration strategy provides competitive remuneration aimed at:

- Aligning managers' rewards with shareholders' value.
- Achieving business plans and corporate strategies.
- Rewarding performance improvement.

The composition of senior executive remuneration is made up as follows:

- **Base or fixed remuneration:** determined by the scope, level of knowledge, skill and experience required by the individual.
- **Short-term incentive plan:** typically comprises an extra payout, based on a percentage of the fixed remuneration, dependent on the achievement of key performance and operating result objectives.
- **Long-term incentive plan:** a reward for the achievement of long-term shareholder return. Under various options plans that have been approved by shareholders, participants may be entitled to purchase ordinary shares in the company if certain share price targets are met. Details of those plans, and the share price targets, are contained in Notes 30 "Options plans" and 31 "Share purchase plans" to the financial statements.

## Code of conduct

The board has adopted a Code of Conduct and a Code of General Business Principles.

The Code of Conduct provides directors and executive officers with clear expectations of ethical standards expected in the company. The Code has been adopted by all Warehouse companies. It addresses:

- Confidentiality
- Trading in company securities
- Receipt of gifts and entertainment
- Transparency and avoiding conflicts
- Use of company information and assets
- Delegations of authority
- Processes for reporting and resolving ethical issues.

The Code of General Business Principles covers:

- Workplace responsibilities (diversity, employment practices, health and safety)

- Doing business in an environmentally responsible manner
- Interaction with customers and suppliers
- Fair competition in all the markets in which the company operates.

Both codes are intended to also meet the requirements of both the Australian and New Zealand stock exchanges by providing guidance in the area of avoidance of conflicts of interest by the directors and officers.

## Trading in Warehouse securities

The Code of Conduct also contains a Code Of Practice for dealing in Warehouse securities modelled on the Securities Amendment Act 1988, and the subsequent Insider Trading (Approved Procedures for the Company Officers) Notice 1996.

The in-house Code of Practice also limits directors and senior management to dealing in the company's shares, options or other securities only in the six-week period commencing one day after the release of the interim and annual financial results. (In this connection, team members deemed to be senior management are those defined by the chief executive officer from time-to-time.)

All The Warehouse team members must obtain written consent of the chief executive officer or company secretary or, in the case of directors, from the chairman of the board, prior to dealing in The Warehouse shares or options at any time.

Directors and senior management are prohibited from short-term trading in company shares.

## Managing risk

The board is responsible for risk management generally. It delegates this responsibility to the chief executive officer who may further delegate such responsibilities to brand chief executive officers and other officers.

The board acknowledges that it is responsible for the overall internal control framework. The audit committee reviews the reports of management and the external and internal auditors on the effectiveness of systems for internal control, financial reporting and risk management. To assist in discharging this responsibility the board has in place a number of strategies designed to safeguard the company's assets and interests and ensure the integrity of reporting.

### Internal audit function

The internal audit function of the company is co-managed with Ernst & Young.

Store audits are conducted by company internal auditors. For the year ended 31 July 2003 forty-four programmed, follow-up or trigger store audits were conducted by the internal auditors.

Non-store internal business processes are audited by Ernst & Young. These audits include business process reviews of each of the three retail businesses together with group functions. During the year Ernst & Young undertook twenty reviews. The findings of internal audit have or are being acted upon by management and are subject to monitoring by the internal audit teams.

The respective internal audit teams reports to, and are directed by, the audit committee.

### Financial reporting

The company has a comprehensive budgeting system with annual budgets approved by the directors (usually in July each year). Monthly actual results are reported against budget and revised forecasts for the year are prepared regularly.

### Capital investment appraisal

The company has clearly defined guidelines for capital expenditure investment. These include annual capital budgets, delegated levels of authority for the chief executive officer and retail business managers, detailed capital expenditure appraisal process for large investments, and post-capital expenditure reviews.

### Treasury policy

Exposure to foreign exchange and interest rate risks are managed in accordance with the company's treasury policy that sets limits of management authority. Derivative instruments are used by the company to manage its business risks; they are not used for speculative purposes. The policy was subject to an external review in August 2001. Note 32 "Financial instruments", in the Notes to the financial statements, details the current treasury policy.

### Insurance

The company maintains insurance coverage with reputable insurers for most types of insurable risk. The company retains a \$1 million insurance deductible for any single non-earthquake event loss arising from damage or business interruption to stores, distribution centres or support offices. The company has capped non-earthquake losses in total of \$5 million in any one year.

The Warehouse Limited and Warehouse Stationery Limited are accredited employers under the ACC Partnership Programme for workers' compensation insurance. This programme encourages eligible employers to take responsibility for their own workplace health and safety, and injury management. This includes rehabilitation and claims management of employee work injuries. As a partnership employer, the company self-insures the costs and compensation arising from workplace injuries up to a maximum limit of \$150,000 for any one event and up \$1.6 million in any one year.

### Compliance with Australian Stock Exchange Governance Council standards

The table below details the company's compliance with the key ASX Corporate Governance Council Standards as at 4 September 2003.

<b>ASX Corporate Governance Council Standards</b>		<b>Do we comply?</b>	<b>If not, why not?</b>
1.1	Formalise and disclose the functions reserved for the board and those delegated to management.	Yes	
2.1	A majority of the board should be independent directors.	No	Currently four of nine directors are considered independent with three non-executive and two executive directors.
2.2	The chairperson should be an independent director.	No	Chairman is considered not to be independent as he is a trustee of the Tindall Foundation, a substantial security holder in The Warehouse.
2.3	Role of chairperson and CEO should not be exercised by the same person.	Yes	
2.4	Establish a nomination committee.	Yes	
3.1	Establish a code of conduct.	Yes	
3.2	Disclose the policy concerning trading in securities.	Yes	
4.1	Require the CEO and CFO to sign a representation letter.	Yes	
4.2	Establish an audit committee.	Yes	
4.3	Structure of the committee shall comprise: Only non-executive directors; Majority independent; Independent chairman; At least three members.	Yes	For all board committees apart from the remuneration, talent and nomination committee, (S R Tindall, an executive board member sits on this committee).
4.4	Board committees should have a formal charter.	Yes	
5.1	Written policies to ensure compliance with ASX Listing Rule disclosure requirements.	Yes	
6.1	Design a communications strategy to promote effective communication with shareholders.	Yes	
6.2	External auditor to attend the annual meeting.	Yes	
7.1	Establish policies on risk oversight and management.	Yes	
7.2	CEO and CFO should represent that risk management systems are in place.	Yes	
8.1	Disclose evaluation process for performance of the board, its committees, directors and executives.	Yes	
9.1	Provide disclosure in relation to the company's remuneration policies.	Yes	
9.2	Establish a remuneration committee.	Yes	
9.3	Clearly distinguish the structure of non-executive directors' remuneration from that of the executive.	Yes	
9.4	Ensure that payment of equity-based executive remuneration is made in accordance with thresholds set in plans agreed by shareholders.	Yes	
10.1	Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.	Yes	