



right balance of director competencies for governance, for furtherance of the Australian Ethical Charter and for assisting with and monitoring company performance. Over time, and assuming the availability of suitable candidates, the Board expects to move towards a majority of independent directors.

The Board is of the view that the Board's current composition well serves the interests of shareholders. The Board carries out its responsibilities according to its Constitution, regulatory requirements, and an overall mandate, including the following:

- the Board must comprise at least three and not more than ten directors;
- the Board is bound by the Australian Ethical Charter that is set out in the AEI Constitution. The Charter sets out 23 ethical principles to be applied to the operations and activities of the company;
- each director is committed to the AEI Code of Conduct that governs the conduct of employees and directors. The Code is consistent with the recommendations that form part of the Corporate Governance Council's Principles 3 and 10;
- all available information on items to be discussed at a Board meeting is provided to each director prior to that meeting;
- the Board has adopted a policy for the management of conflicts of interest;
- with the prior approval of the chairperson, each director has the right to seek independent legal and other professional advice at the company's expense on any aspect of the company's operations or undertakings in order to fulfil their duties and responsibilities as directors.

Chair of the Board

The company's chairperson is currently an independent director.

Nomination committee

During the period the company had no nomination committee. The Board does not intend to establish such a committee because such a move would be inefficient, given the company's size. The functions normally performed by a nomination committee will be performed by the Board as a whole, or will be delegated to the chairperson of the Board.

Promote ethical and responsible decision making

Code of conduct

The company has a code of conduct which applies to all staff. It is available on the company's website.

Share trading

The company's code of conduct covers share trading. It requires that as a general rule "staff and directors should

not buy or sell AEI shares between the close of the financial year or half-year and the publication of the company's results".

In accordance with the Corporations Act 2001 and the ASX Listing Rules, directors must advise the ASX of any transactions conducted by them in securities of the company which they own or in which they have a relevant interest.

Directors, employees and their associates must not engage in insider trading, nor the disclosing of inside information to third parties. The company periodically conducts seminars about its share trading policy and educates staff about the offence of insider trading.

Safeguard integrity in financial reporting

CEO and CFO sign-off of financial reports

The company requires the Chief Executive Officer and the Chief Financial Officer to state in writing to the Board that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operating results and are in accordance with relevant accounting standards.

Audit committee

Throughout the period, the Board had an audit committee consisting of two non-executive directors and the company secretary.

The qualifications of those appointed to the audit committee are provided in the directors' report, as are the number of meetings of the committee and attendances at those meetings.

The audit committee does not consist of only non-executive directors (the company secretary being a member and not a director). During the course of the reporting period, audit committee membership moved to a majority of independent directors. The chairperson of the committee is Naomi Edwards.

The audit committee provides a forum for effective communication between the Board and the external auditors. The role of the committee is to advise the Board on the maintenance of an appropriate framework of financial internal control and appropriate discharge of 'trading company' fiduciary obligations for the company and its subsidiary, Australian Ethical Superannuation Pty Ltd.

A charter for the audit committee appears on the company's website.

The Board is of the view that notwithstanding that the audit committee does not comply with all the Corporate Governance recommendations on membership, it is nonetheless able to perform its functions with independence and diligence.



In particular:

- the committee includes the company secretary who is responsible to the Board chairperson and the Board generally on governance matters;
- at a number of meetings the committee speaks directly to the external auditor in the absence of executive management.

The audit committee considers the performance and independence of the external auditor over the course of a reporting period. In selecting an external auditor the Board seeks competence, industry experience, integrity and independence. In normal circumstances, appointment of the external auditor will typically continue for a significant number of years. Rotation of external audit engagement partners will occur in accordance with the rotation requirements of the Corporations Act 2001.

Make timely and balanced disclosure

The company has written policies and procedures designed to ensure compliance with the ASX Listing Rule disclosure requirements. The disclosure policy appears on the company's website.

Respect the rights of shareholders

The company maintains a comprehensive and informative 'investor relations' section on its website which provides shareholders (and others) with up to date information about the corporate activities of the company. The website also provides shareholders with guidance on a range of issues concerning the management of their shareholdings.

AEI maintains a newsletter, 'Aim High', for unitholders and shareholders and, since listing, has introduced a CEO information sheet for shareholders. It has revised its Annual General Meeting arrangements to promote participation and dissemination of information and has ensured access to the external auditor at these meetings.

AEI also produces a Sustainability Report for shareholders and other stakeholders on the triple bottom line performance of AEI (available on the AEI website).

The company complies with the corporate governance guidelines for notices of meeting.

Recognise and manage risk

The Board is responsible for the company's system of internal controls. The Board monitors the operational and financial aspects of the company's activities and, through the audit committee, the Board considers the recommendations and advice of external auditors and other external advisers on the operational and financial risks that face the company.

The Board monitors that appropriate actions are taken to ensure the company has an appropriate internal control environment in place to manage the key risks identified. It has appointed a director as Risk Management Officer and

established a formal 'Statement on Risk Management', together with supporting documents, 'AEI Guide for Risk Management' and section risk registers, that document the major risks facing the company and the way in which these risks are to be managed. The risk registers are updated regularly and the criteria and working standards set out in the guide are periodically reviewed.

A description of the company's risk management policy and internal compliance and control systems is on the company's website.

The chief executive officer and chief financial officer certify to the Board that the integrity of the financial statements are founded on a sound system of risk management and internal compliance and control.

The chief executive officer, risk management officer and compliance officer certify to the Board that its internal control and risk management systems are operating efficiently and effectively throughout the Group.

Encourage enhanced performance

Board and director evaluation

The directors undertake an annual self-assessment of their collective and individual performance and seek specific feedback from the senior management team. An assessment was undertaken in the relevant period.

A questionnaire concerning board and individual performance is completed by each director in respect of themselves and for each other director and the results collected by the Board chairperson. The Board as a whole then considers and discusses the results of the questionnaire at a Board meeting. The Board chairperson also talks to each director individually about their performance and generally on the evaluation and comments received from their peers. The results of the questionnaire are examined from both a qualitative and quantitative perspective.

Where discussed at a board meeting, results and any action plans are documented in Board minutes.

Key executive evaluation

The performance of executives is evaluated in accordance with the company's annual performance review guidelines. For the chief executive officer, the review is conducted by the Board chairperson. For other executives, the review is undertaken by the chief executive officer.

The process is as follows:

- receive 360° comments from staff (and directors if applicable);
- review comments once received and incorporate into the annual review as considered appropriate. Emphasis is to be on themes or perceptions rather than specific comments;
- complete a draft of the annual performance review and provide to the executive for discussion;



- discuss the annual performance review with the executive – cover key responsibilities, overall performance, key behaviours, review achievements against previous year's objectives, discuss objectives for the coming year, discuss aspirations and areas for improvement;
- review competencies and qualifications to ensure they remain applicable to the position. If not, a training program must be developed to bring the executive to the appropriate level; and
- investigate what specific training may be suitable and available.

In respect of the chief executive officer, the chairperson presents the results of the review to the Board, the Board has an opportunity to provide feedback to the chief executive officer, and to consider recommendations from the chair on the chief executive officer's remuneration package.

Remunerate fairly and responsibly

Remuneration policy

AEI's remuneration policy is designed to accord with the principles of the Australian Ethical Charter, as set out in the constitution of the company. It is designed to ensure AEI **does not**

"exploit people through the payment of low wages or the provision of poor working conditions"

and to facilitate:

"the development of workers participation in the ownership and control of their work organisations and places"

AEI's fundamental remuneration policy is to treat all staff in an equitable fashion and not to have special remuneration arrangements for particular staff. All permanent staff (including the CEO and executive directors) receives a cash salary and participate in the staff bonus and employee share ownership scheme. Remuneration is not subject to set performance hurdles.

All permanent staff are eligible to participate in the staff bonus which is determined by the constitution. Each year the bonus is set with reference to the profit of the company. Each full time staff member receives the same amount, part-time staff receive a pro-rata amount. The constitution provides that the bonus can be (and often has been) satisfied by the issue of shares.

Under the employee share ownership plan a pool of options, which would if exercised, amount to 5% of the existing ordinary share capital is issued to staff. All permanent staff are eligible to participate in the plan. The price at which the options can be exercised is set 10% in excess of the market price of the shares. The number of options received by an individual staff member depends on their salary level. Options are not exercisable for a period of three years from their date of grant.

AEI has a mix of full time and part time staff and endeavours to provide flexible employment

arrangements within business needs.

AEI monitors employee's salaries against the wider market and reviews salary levels annually. The company adopts an in-principle guideline of paying individual staff a total fixed remuneration based on 80% to 120% range of the 50th percentile identified in a biennial salary survey, with an unweighted average of 95% – 105% and with appropriate macro economic indexation of comparator benchmarks over time.

The guideline would not be implemented in such a way that salaries would reduce where there was a market crash in relevant salaries.

Remuneration committee

The Board has a remuneration committee. The members of the remuneration committee are George Pooley (independent director), Naomi Edwards (independent director appointed to the committee in June 2006) and Caroline Le Couteur (executive director). The charter for the remuneration committee is available on the company's website.

Details of remuneration

Details of remuneration paid to directors and executives during the reporting period is set out in the directors' report. The reporting distinguishes between the structure of non-executive director remuneration and that of executive directors.

Equity-based remuneration

Equity-based remuneration for executive directors has previously been approved by shareholders. The employee share ownership plan was approved by shareholders at the annual general meeting held in November 2005.

Recognise the legitimate interests of stakeholders

The proper purpose of AEI is to promote ethical/socially responsible investment. By the very nature of AEI, the Board is committed to the highest standards of conduct and ethical practices in guiding the business activities of AEI and its subsidiary. This includes transparency in the way in which it does business and clarity of communication to its members and other stakeholders. Its code of conduct, as mentioned earlier in this report, expects this of each employee and each director.

The company has developed a corporate governance section for its website. The Board has directed that detailed and comprehensive information on the company's corporate governance arrangements and copies of relevant policies and charters are to be placed on that website. It welcomes comments and suggestions from stakeholders on any element of its corporate governance program.