Governance News

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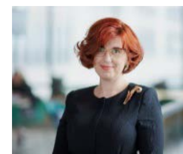

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Board of Directors

In Brief | General Electric Co will reportedly 'renew' its board in the wake of a US federal investigation into accounting practices: GE will reportedly replace three long standing directors with three outsiders and reduce the overall size of the board. Among the new directors is Leslie F Seidman (former Chair of the Financial Accounting Standards Board).

[Sources: General Electric media release: 26/02/2018; [registration required] The WSJ 28/02/2018]

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[Sources: [registration required] The FT 13/03/2018; [registration required] The WSJ 12/03/2018]

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[Sources: MSCI blog 06/03/2018; [registration required] The FT 12/03/2018]

Remuneration

The Australian Institute has released a report: *GFC+10: Executive pay in Australia* which has found that ten years on from the financial crisis, executive pay is back on the rise, though the 'two strikes' rule is holding it in check (to some degree).

Building on a report issued shortly after the global financial crisis (GFC), which documented the rise in CEO remuneration in the period 1993 to 2007 from 15:1 (ie CEO pay was 15 times that of the average worker in 1993) to a peak of 250:1 in 2007, the Australia Institute has released a new report: *GFC+10: Executive pay in Australia* updating the initial research.

The report outlines the latest remuneration figures for the CEOs of two big banks (the National Australia Bank (NAB) and the Commonwealth Bank of Australia (CBA)) relative to average weekly earnings, along with other CEO pay data for the top 100 ASX companies.

The report found:

- The CEOs of the NAB and CBA earned, respectively, 108 and 93 times average weekly earnings (AWE) in 2017. While a retreat from peak levels (267 times AWE for NAB in 2004 and 317 times AWE for CBA in 2010) the report comments that this is still a large rise compared to the 58 and 70 times AWE they earned in 2000. 'Another way of considering this is that while average earnings have less than doubled since 2000, NAB and CBA CEO pay has more than tripled' the report comments.
- Average CEO pay for the largest 100 Australian companies declined from $5.5 million pre GFC to $4.7 million in 2011, but has since increased steadily back to $5.2 million according to the report. Similarly, Australia's highest reported CEO salary peaked pre GFC at $33.5 million, declined to $11.8 million in 2011 before bouncing back to $21.6 million in 2017.

The report concludes that though CEO pay remains 'excessive' and appears to be rising, it is no longer accelerating at the same rate as it did immediately prior to the GFC due to the impact of the two strike rule. The report suggests that further policy intervention could be effective in addressing this.

[Source: GFC+10: Executive Pay in Australia Ten years on from the Global Financial Crisis, average CEO pay is back on the rise 15/03/2018]

Gender pay gap | 30% of the highest earning partners at EY to be women by 2020: EY has reportedly set a gender target to help close the pay gap the firm.

The AFR writes that PwC and EY have recently revealed pay gap data, following moves by the UK government to force companies to disclose pay gaps.

Reportedly, PwC has revealed a gender pay gap of 16% between male and female partners at the firm, due to seniority, and an overall pay gap of 12%. EY has reportedly revealed a similar pay gap of 15% at partnership level and given the same reason, and an overall pay gap of 10%.

According to the AFR, EY has committed have women make up 30% of the highest earning partners at the firm by 2020. EY CEO, Tony Johnson reportedly said: The overall average pay gap across the firm for all partners and staff is 10.1 per cent and at the partner level 14.9 per cent, reflecting the historically higher proportion of men in senior leadership positions in the firm and the industry more broadly… To continue to address this, we have a target of 30 per cent female partners by 2020 as well as a target of 30 per cent of our female leaders being in the top 30 per cent of highest earning partners, also by 2020. We already have some excellent initiatives in place to improve the diversity of our future leadership, including closely monitoring our recruitment, promotion, performance assessment and nominations to leadership programmes. We are committed to equal pay for equal work and to driving change in this area. We know we have more men as partners and as leaders, and we are continuously working to improve the representation of women across all levels of our business.'

The AFR comments that the pay gaps at both EY and PwC are below the equivalent figures for managers and staff in 'management and related consulting services' according to Workplace Gender Equality Agency data.

Are women leaving due to poor culture? Noting the relatively low number of female partners at the big four accounting firms — women reporting make up less than 25% of partners at the big four overall — and the lower numbers of women in senior roles, the AFR suggests that women may be opting to leave the sector due in part to cultural issues eg allegations of misconduct at EY and KPMG.

[Source: [registration required] The AFR 13/03/2018]

United States | US public companies are disclosing their pay ratios for first time: Available data reportedly reveals significant pay variation within sectors and a 250:1 pay ratio at Bank of America.

Significant pay disparity within sectors revealed, but direct comparisons are not straightforward? The WSJ comments that pay disclosure by public companies is revealing that there is significant pay disparity within sectors. For example: According to the WSJ, the pay ratio at Kraft Heinz Co was 91:1 with the CEO earning $4.2 million and the median worker earning $46,000 compensation in 2017. At Kellogg Co, a smaller company in the same sector, the pay ratio was 183:1 with the CEO earning $7.3 million, and its median employee, about $40,000. At Honeywell International Inc (a company with significant numbers of overseas workers) the ratio was reportedly much higher: 333:1. The article suggests that there is a trend towards companies with larger global or retail operations having lower worker pay and a higher pay ratio.

However, the article comments that direct comparisons are not necessarily straightforward for a number of reasons, among them, that the disclosure rule gives companies wide leeway in identifying median workers and the fact that though firms must include part-time, temporary and seasonal workers, they needn't account for independent contractors if they don't set their pay. Firms may also exclude up to 5% of their non-US employees.

The article adds that in some cases, companies are publicly supplementing their pay disclosures with details that go beyond the SEC's requirements. These efforts, the article suggests, are directed more at employees than investors.

[Source: [registration required] The WSJ 11/03/2018]

BoA reveals 250:1 pay ratio: The WSJ writes that the Bank of America is the first large US bank to disclose its pay ratio. According to the WSJ:

- Pay for the media employee at BoA in 2017 was $87,115.
- Pay for BoA CEO in 2017 was $23m (250 times the pay of the average employee at the bank).
- Pay for BoA COO was $19m (which is reportedly an increase of $2m on 2016).

The WSJ comments that the pay range at BoA which has in excess of 200,000 employees varies widely to reflect the range of roles — from bank tellers to investment bankers — performed in the organisation. For example, a similar ratio was reported, The WSJ comments at Capital One Finance Corp (261:1).

[Sources: [registration required] The WSJ 13/03/2018; 12/03/2018]

The Netherlands | The price of 'quasi-governmental status'? ING has reportedly abandoned a proposal to increase CEO pay by 50% due to opposition from the Dutch government.

The FT writes that ING Group has abandoned a proposal to increase the CEO's pay by 50% following opposition by the Dutch government and from the public. The article quotes ING supervisory board Chair Jeroen van der Veer as stating that the company has scrapped the proposal after realising it had 'underestimated the public response in the Netherlands on this clearly sensitive matter.' The article adds that Mr van der Veer, who is stepping down at the bank's annual meeting next month, said in a statement that the supervisory board was 'responsible for this proposal and regret the commotion caused by it'.

The proposal: According to the FT, the board proposed to award the ING CEO €875,000 of deferred shares to boost his fixed pay and lift his maximum total remuneration by 50% to slightly more than €3m. Reportedly, the reason for the increase was to bring his pay more in line with that of his international peers.

Opposition to the proposal: Reuters writes that prior to the company withdrawing the proposal, the Dutch government was reportedly exploring mechanisms to enable it to block the increase, including by changing laws on bankers' pay. The article quotes the Dutch Finance Minister Wopke Hoekstra as stating the government 'really wants ING to take this proposal off the table…We will see what measures we can take to deal with this kind of situation…This deals directly with the confidence we should be able to have in the banking sector. ING is not a cookie factory, it is a systematically important bank.'

The FT quotes the Netherlands Prime Minister as stating that ING was not 'a normal company' but a 'quasi-governmental organisation, if you see that when things go wrong in the end they are dependent on the safety net we as taxpayers have to cough up'.

Reuters comments that parties representing 99% of the seats in Dutch parliament condemned the proposed wage increase.

The price of quasi-governmental status? The FT comments that this is not the first instance in which ING has 'clashed' with politicians on this issue in the Netherlands. The article adds that the Netherlands one of the strictest limits on bankers' pay, capping bonuses at 20% of fixed pay. The article adds that bank was bailed out by the Dutch taxpayer after the financial crisis but it has since repaid all its state aid at a profit to the taxpayer of about €5bn.

[Source: [registration required] The FT 14/03/2018; Reuters 13/03/2018]

In Brief | Following a full year loss, Deutsche Bank executives will reportedly give up bonuses for the third consecutive year according to The WSJ.

[Source: [registration required] The WSJ 10/03/2018]

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[Source: Reuters 14/03/2018]

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[Sources: Takeovers Panel media release TP18/20 14/03/2018; Consultation paper — Guidance Note 1 — unacceptable circumstances 14/03/2018; [registration required] The AFR 14/03/2018]

In Brief | The first time a current US president has halted a deal over national security concerns before the deal was even agreed? President Trump has reportedly issued an executive order blocking Broadcom's proposed hostile takeover of Qualcomm citing national security concerns. Reportedly, as part of the order, all of Broadcom's director nominees are also disqualified from standing for election as directors of Qualcomm.

[Sources: Fortune 14/3/2018; [registration required] The FT 13/03/2018]

Meetings and Proxy Advisers

As You Sow Proxy Preview 2018 released: Conservative 'copycat' resolutions; gender pay equity and the unresolved question of the impact of Staff Legal Bulletin No 14I (shareholder proposal rule) are among the new issues emerging this proxy season.

As You Sow, the Sustainable Investments Institute (Si2), and Proxy Impact have released their fourteenth annual proxy preview: *Proxy Preview 2018*, which examines environmental, social and sustainable governance (ESG) resolutions filed at US companies this year.

Some of the report's key findings include:

- **429 ESG shareholder resolutions have been filed this year** as of 16 February. As at the same time last year there were 430 filings. However, by year's end the overall tally reached 494. The report notes that as of mid-February 2018, 330 were headed for votes which is about the same number as were pending at this time last year.
- **Climate change, corporate political activity and sustainability account for just over 50% of the resolutions** in 2018 which is consistent with last year. 30% relate to human rights, board diversity and workplace diversity and the remainder are made up of resolutions on health issues, board oversight and proposals from conservatives amongst other issues.
- **The topic of climate change** makes up the vast majority of resolutions filed on environmental topics. Of the 83 resolutions on climate, three-quarters raise 'familiar requests', seeking more information about how companies will report and manage carbon asset risk and set goals to reduce their greenhouse gas (GHG) emissions. A core request is for companies to explain how they will adapt to a low-carbon economy that is needed to prevent global temperature increase above 2 degrees Celsius, as agreed in the Paris climate treaty. Most of the 27 recipients are energy and utility companies that routinely get these requests in some form.
- **ESG trend:** More proposals relate to social issues than concern the environment overall: Since 2010, the report notes that there have been more proposal about social issues than concerning the environment, but the long term trend shows growth in sustainable governance. This year marks a drop in social resolutions and a convergence between the environment and governance.

New issues this year

The report identifies a number of new issues, among which are the following:

- The unresolved question of the shareholder proposal rule: 'A sea change in policy' that could dramatically reduce the number of resolutions? 'Most significant this year' according to the report is the unresolved question of whether companies will be successful in using the new legal bulletin to redefine the 'significantly related' portion of the shareholder proposal rule. According to the report, Citibank, Eli Lilly, Goldman Sachs and Travelers are all arguing their political expenditures are insignificant with some also saying that investors are not interested in the disclosure sought by proponents. If the SEC agrees with this viewpoint, the report comments, it will mark a 'sea change in policy that could significantly reduce the number of resolutions'.

[**Note**: Separately, Harvard Law School Forum writes that a successful application to exclude a shareholder proposal has been to SEC. This is discussed briefly below.]

- **Conservative 'copy cats'**: The report comments that new this year are a number of proposals from the free market activist group the National Centre for Public Policy Research (NCPPR) mostly on social issues. The report notes that in two instances so far these resolutions have pre-empted mainstream proposals filed later. The proposals in question related to lobbying at Duke Energy and election spending at General Electric where the question turned on third party spending options.
- **Gender pay equity**: The report notes that there are 36 gender pay equity resolutions. The increase in the number is attributed in the report to the influence of the #MeToo movement and its demand for equal treatment (including equal pay). The report notes that approximately 50% of the resolutions are resubmissions, many at financial sector companies were women are not well represented in higher paying positions. Arjuna Capital is identified in the report as a key player in this space. Reportedly it has negotiated agreements with four of the US biggest banks — Bank of America, Bank of New York, Mellon, Citigroup and Wells Fargo — to work on closing the pay gap between men and women. Other important proponents are Pax World Funds and the New York City pension funds which also address this issue through its numerous proxy access proposals. Gender pay resolutions also often raise the pay differential for people of colour. Reportedly there have not been SEC challenges in response to these resolutions.
- **ESG pay links?** 18 proposals, most of which are the subject of SEC challenges, have requested further information about links between a variety of issues and executive compensation.
- **Mutual funds**? 'A central outstanding question' for the upcoming proxy season the report writes, is the potential impact of proxy voting by mutual funds. Last year, the report notes, large mutual funds were responsible for unusually high shareholder majorities, including votes of 67% at Occidental Petroleum and 62% at ExxonMobil in favour of more climate disclosure.
- **Health**: Investors for Opioid Accountability coalition ($2.2 trillion in assets) is pushing for more disclosure and accountability from opioid makers, distributors and treatment medicine providers. The report notes that the group is starting with two resolutions this year on opioid distribution directly, with a number of others on corporate governance procedures. A report request at AmerisourceBergen earned 41.2% on March 1.
- **Media and cybersecurity**: Media and Cybersecurity and more particularly, the way in which large social media companies (Alphabet, FaceBook and Twitter) manage business risks are key issues (as reflected in the fact that the subject was included in the agenda at the World Economic Forum in Davos).
- **'Hot button' issues: Modern slavery and gun control:** The report notes that two companies—Costco Wholesale and TJX— are facing pressure about goods made with domestic prison labour. In addition, Investors asked Chubb about the insurance it underwrites for gun owners' self-defence shootings and resolutions about gun safety were filed at weapons makers and sellers. In the wake of the Parkland, Florida massacre, Chubb said it would end its shooters' insurance and Dick's Sporting Goods—which faced a resolution—announced it will stop selling assault weapons.

[Sources: [registration required] As You Sow Proxy Preview 2018]

First successful application of the exclusion under Staff Legal Bulletin No 14I (shareholder proposal rule)? Harvard Law School Forum writes that on February 22, 2018, the staff of the SEC's Division of Corporation Finance (the Division) issued a favorable no-action response to Dunkin' Brands Group, Inc. under Rule 14a-8(i)(5) (the economic relevance exception). According to the article, this is the first successful use of the economic relevance exception following the issuance of Staff Legal Bulletin No. 14I (the SLB).

Dunkin' Brands Group, Inc reportedly sought to exclude a proposal requesting that its board issue a report assessing the environmental impacts of continuing to use K-Cup Pods brand packaging on the basis that the subject matter of the proposal was not significantly related to the company's business.

According to the article, the success of the request was due to specificity of the information provided in its no-action request letter regarding the analysis undertaken by the company's board in determining that the subject matter of the proposal was not significantly related to the company's business.

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 11/03/2018]

Disclosure and Reporting

Top Story | Market Forces research has found that climate change disclosure among ASX100 companies in sectors facing the highest levels of climate risk is inadequate and has called on APRA and ASIC to implement a mandatory TCFD-aligned disclosure framework.

Market Forces has released a study: *Investing in the dark: Australian companies are failing to properly disclose climate risk*, that has found that climate risk disclosure among ASX 100 companies in sectors facing the highest levels of climate risk is inadequate. This inadequacy is indicative, according to Market Forces, of a 'failure in the current corporate regulatory system'. On this basis, Market Forces has called on regulators (ASIC and APRA) to implement a mandatory, Task Force on Climate-related Financial Disclosures (TCFD) aligned disclosure framework to address the issue. 'Universal, comprehensive and comparable climate risk disclosure can arm investors with the information they need to allocate capital in a way that drives the transition to a low carbon economy' Market Forces argues.

About the study: The study is based on an analysis of public disclosures 73 ASX100 companies in sectors identified by Market Forces as facing the highest levels of climate risk.

Key Findings

- **Less than half (49%) of the companies studied identify climate change as a material business risk** despite all assessed companies operating in sectors determined by the TCFD to be highly exposed to climate risk.
- **16% of companies do not include climate risk in annual financial reporting:** 16% of companies define climate risk as an 'emerging risk', an 'ESG risk', or a 'sustainability risk', often in the Sustainability Report rather than the Annual Report. The TCFD recommends that climate risk be disclosed as part of mainstream annual financial reporting.
- **25% of companies provide a detailed discussion of climate risks and opportunities in mainstream annual reporting**. 19% provide a limited discussion, while 29% do not disclose any discussion of the risks and opportunities posed by climate change.
- **22% of companies do not disclose responsibility for climate risk:** At 73% of companies, the Board has overall responsibility for managing climate risk. A further 5% of companies placed this responsibility with another (ie non-Board level) executive. 22% of companies did not disclose any such responsibility.
- **84% of companies do not incentivise executives to reduce greenhouse gas (GHG) emissions**: According to Market Forces, only 16% of companies remunerate executives to reduce GHG emissions. Market Forces argues that this indicates that 'broadly speaking, Australia's corporate executives are not being incentivised to tackle climate change'.
- **14% of companies have disclosed some form of scenario analysis** – 8% of these could be considered detailed, while a further 5% have disclosed limited scenario analysis. 88% of companies have not produced analysis of how their business is expected to fare under different climate change scenarios.

- **16% of companies have disclosed a plan to reduce their carbon emissions** while 84% of companies have not produced a plan.
- **26% of companies have set absolute emissions reduction targets**, a further 14% have set emissions intensity targets. In many cases, the latter allows for overall emissions to increase, provided emissions per unit of production decrease. 38% of companies disclose Scope 1+2+3 emissions. 41% disclose Scope 1+2 only, while a further 3% disclose their emissions only in response to the CDP.
- **35% of companies are not clear in their language on climate or have not formally acknowledged the science of climate change**: According to Market Forces, while 66% of companies have unequivocally accepted climate science, 21% of companies are unclear in their language. The remaining 14% have not formally acknowledged the science of climate change.

Recommendations: Market Forces argues that these findings are indicative of a 'systemic lack of climate risk disclosure' and suggestive of a 'failure in the current corporate regulatory system'. Market Forces makes three recommendations to address this:

1. **That regulators (APRA and ASIC) should mandate a comprehensive universal climate risk disclosure framework** ie the TCFD recommendations: More particularly, Market Forces calls for ASIC to provide guidance clearly stating that companies exposed to climate change risks are legally required to disclose those risks as part of their financial reporting obligations and a mandate for TCFD-compliant climate risk reporting for all companies operating in 'high risk' sectors, as well as financial institutions.

   [**Note**: On 2 February 2016, the Senate referred an inquiry into carbon risk disclosure to the Senate Economics References Committee. The committee report, released on 21 April 2017, recommended among other things that ASIC review its guidance to directors on meeting their disclosure obligations in the context of climate risk and that the ASX Corporate Governance Council review guidance material regarding the circumstances in which a listed entity's exposure to carbon risk requires disclosure under Recommendation 7.4 of the Australian Stock Exchange Corporate Governance Principles. The Government response to the report, released on 7 March, expressed 'agreement in principle' with both of these recommendations. See: Governance News 12/03/2018.]

2. That investors should hold companies accountable and escalate climate risk disclosure in their engagement programs.

   [**Note**: ASIC's report on the 2017 AGM season: *Report 564 Annual general meeting season 2017 identifies growing concern among investors around diversity and ESG issues including climate risk (as evidenced by what ASIC characterises as high levels of shareholder engagement as a key trend. See: Governance News* 02/02/2018*]*

3. That companies should educate themselves about the need to take action and improve disclosure.

[Sources: Market Forces media release 14/03/2018; Investing in the dark: Australian companies are failing to properly disclose climate risk 14/03/2018; The SMH 13/03/2018]

Top Story | ASX additional guidance on continuous disclosure obligations: Following recent disclosure issues, the ASX has issued revised guidance on meeting disclosure requirements and has cautioned entities of the possible consequences of failing to meet their obligations.

Following a number of recent disclosure issues, the Australian Securities Exchange (ASX) has released updated Listing Rule guidance on meeting continuous disclosure requirements and has reminded entities of the possible consequences of failing to meet their obligations.

Issues with disclosure of customer contracts: The ASX writes that recently there have been a number of incidents where the disclosures by 'listed entities about their contractual arrangements with customers have fallen short of the required standards'. The ASX cites a number of examples of this including entities:

- 'announcing a contract with a major global customer without providing any details of the nature or substance of the contract or its significance to the entity (ie seeking to benefit from the association with the customer without providing proper disclosure);
- announcing what appears to be a material customer contract without disclosing that it is subject to a trial period or other conditions and therefore may not proceed;
- disclosing revenue projections for customer contracts that do not have a proper basis or that do not state the material assumptions or qualifications underpinning them;

- not disclosing when a previously announced material customer contract is terminated or does not proceed (ie disclosing good news but not bad); and
- misrepresenting customer contracts as being "material" or with other superlatives when plainly they are not (one of the more notable examples being a listed entity that disclosed a "material commercial agreement with a leading financial entity" under which it was to receive less than $1000 in revenue)'.

[**Note**: ASX does not name specific companies. Examples of recent disclosure issues and subsequent trading halts at three small cap technology companies: GetSwift, Big Un and Buddy Platform were discussed in Governance News 26/02/2018]

Reminder of the possible consequences of failing to meet continuous disclosure obligations: ASX comments that when it detects the sort of behaviour identified above, it 'will not hesitate to suspend the entity, query it and require it to correct any inadequate or misleading disclosures. It will also refer the entity to ASIC for consideration of regulatory action'.

Updates to Guidance Note 8 Continuous Disclosure: Listing Rules 3.1 – 3.1B

Changes include:

- Additional guidance in section 4.15 on ASX's disclosure expectations for material contracts.
- Expanding the guidance in section 5.10 to address the new insolvent trading safe harbour for directors in s588GA of the *Corporations Act 2001* (Cth) and what should be disclosed when an entity in financial difficulties requests a voluntary suspension to complete a transaction necessary for its survival.
- Removing a reference in section 4.20 to disclosing the impact of material contracts on revenue, costs or profits.
- Clarification of the material in the worked example of the operation of listing rule 3.1 relating to mineral discovery (Changes to Example D of Annexure A).

In light of recent disclosure issues, the ASX highlights the new passage in section 4.15 of the guidance note regarding the need to provide sufficiently detailed information for investors: 'Wherever possible, an announcement under Listing Rule 3.1 should contain sufficient detail for investors or their professional advisers to understand its ramifications and to assess its impact on the price or value of the entity's securities' the ASX writes.

Other updates to the Listing Rule Guidance Notes

The ASX has also released updates to the following Listing Rule Guidance Notes:

- **Guidance Note 1 *Applying for Admission – ASX Listings***. The ASX writes that changes include the addition of further materials in section 3.8 on using artificial means to achieve spread and in section 3.19 on ASX's good fame and character requirements.
- **Guidance Note 12 *Significant Changes to Activities:*** The ASX writes that the changes reflect a change in policy for back door listings (which is effective immediately) requiring all directors or proposed directors 'to provide evidence of their good fame and character, including existing directors who have been elected by shareholders to the board, and clarifying the accounts that need to be disclosed in an announcement under Annexure A to that Guidance Note'.
- ***Guidance Note 16 Trading Halts and Voluntary Suspensions*** Changes reflect changes to section 5.10 of Guidance Note 8.

[Source: Listed@ASX – Compliance Update 02/18 March; Revisions to ASX Listing Rules Guidance Note 8]

United Kingdom | Multiple fund managers using the same 'meaningless pro forma text' to avoid explaining non-compliance with the UK stewardship code? Financial News writes that the International Transport Workers' Federation has accused 30 fund managers, including Elliott Advisers, of breaching the UK Stewardship code.

Financial News writes that trade union, the International Transport Workers' Federation (ITF) has accused 30 Financial Conduct Authority regulated fund managers, including Elliott Management, Och-Ziff Capital Management Fundsmith, Cerberus Capital Management, Amber Capital, Kairos Investment Management and Melqart Asset Management of breaching the UK Stewardship code through use of intentionally poor disclosure practices. According to the article, the ITF has alleged that the fund managers have used the same 'meaningless pro forma text', from what is alleged to be the same source, to avoid explaining why they have chosen not to comply with the code. The article quotes ITF as stating that poor disclosure practices 'leaves investors and the wider public in the dark about how these managers actually approach their interactions with companies. Since the phrases used are clearly drawn from a common text, the ITF believes the source of the text must be disclosed, as it is being used by investors to avoid compliance.' Reportedly, the ITF noticed the duplicated statements while researching shareholder engagement with Carillion in the wake of the company's collapse and around Melrose's ongoing bid for GKM.

According to Financial News, the ITF has requested that the Financial Reporting Council, which is currently reviewing both the stewardship code and the corporate governance code, investigate the alleged non-compliance, and has indicated that it will also approach the Financial Conduct Authority.

[Source: Financial News 13/03/2018]

Regulators

Australian Securities and Investments Commission

ASIC Market Integrity Report 569 released: Technology, Cyber resilience, Conduct and Effective capital markets are identified as key areas of focus for the year ahead.

ASIC has released its latest report on market integrity: *Report 569 Market Integrity Report: July to December 2017*. The report identifies key ASIC activities during the six month period and highlights ASIC's ongoing priorities and areas of focus for 2018. These include: technology and cyber resilience, conduct and effective capital markets.

Three areas of focus for 2018 identified in the report

1. **Technology and cyber resilience**: ASIC states that it will continue to review the technology and operational risk of stakeholders and focus on malicious cybercrime in the context of rapid technological developments.

2. **Conduct**: ASIC states that it will continue to focus on conduct that enhances market integrity across all marked based activities. In particular, ASIC states that it is asking firms to consider whether their controls are appropriate.

3. **Effective capital markets**: ASIC states that it will continue to review market activity in the OTC sector, primarily fixed income, currencies and commodities (FICC) and equity derivatives. ASIC adds that it is also: using Report 525 Promoting better behaviour Spot FX (released 26 May 2017) to inform its surveillance of the FX market and, where appropriate, broader wholesale OTC markets; considering allocation processes inequities markets, and building on our existing market surveillance capabilities.

Key activities highlighted in the report

- **Setting standards and educating stakeholders:** ASIC highlights a number of activities relating to setting standards and educating stakeholders in relation to:
  - *Client money*: The release of final client money reporting rules in October 2017.
  - *Sell side research*: The release of guidance on managing conflicts of interest at each stage of a capital raising transaction, identifying and handling inside information by research analysts, the structure and funding of sell side research teams.

- *The NSX listing standards*: ASIC's review of the NSX listing standards and the identification of the need for the NSX to make changes to improve compliance. ASIC comments that, due to the issues uncovered in the NSX review, it is conducting a separate review across all Australian equity markets.

The report also highlights ASIC activities to drive market reform including: consolidating ASIC's existing market integrity rulebooks, consulting on a new financial benchmark regulatory regime, issuing new guidance for licensed exchanges seeking to admit exchange traded products and consulting on reforms to the market licensing regime to facilitate emerging and specialised markets.

- **Behavioural change:** ASIC highlights a number of activities aimed at driving behavioural change ie preventing risky conduct, potential breaches and investor losses. In particular the report highlights activities related to relating to cyber resilience (the release of Report 555 Cyber Resilience of firms in Australia's financial markets) and systems and controls (ASIC acceptance of an enforceable undertaking from Foster Stockbroking Pty Ltd following an ASIC investigation of the firm's management of conflicts of interest).
- **'Disruption' of, and actions to address, poor conduct:** ASIC highlights actions against ANZ and NAB in relation to their role in setting the bank bill swap rate; the review and publication of ASIC's review into binary option trading apps and the work of the Markets Disciplinary Panel which issued six infringement notices and imposed $1138000 during the period, including against Bell Potter Securities Ltd and the action against Jin Xi Li for insider trading.

[Source: 18-074MR ASIC releases market integrity report; Report 569 Market Integrity Report: July to December 2017]

ASIC has issued further guidance to 'help banks and other lenders ensure that their small business loans are fair and do not breach the rules prohibiting unfair contract terms': *Unfair contract terms and small business loans (REP 565)*

ASIC has released a report: *Unfair contract terms and small business loans* (REP 565) outlining the details of the changes made by the big four banks to remove unfair contract terms from their small business loan contracts up to $1 million. The report, ASIC writes, is intended to provide further, detailed guidance to bank and non-bank lenders about compliance with the unfair contract terms laws as they relate to small business.

More particularly, the report:

- Identifies the types of terms in loan contracts that raise concerns under the law.
- Provides details about the specific changes that have been made by the banks to ensure compliance with the law.
- Provides general guidance to lenders with small business borrowers to help them assess whether loan contracts meet the requirements under the unfair contract terms law.

No excuse for non-compliance: ASIC Deputy Chair Peter Kell commented that the 'report provides further guidance to help banks and other lenders ensure that their small business loans are fair, and do not breach the rules prohibiting unfair contract terms.' He added that 'ASIC will review small business lending contracts across the market. There are no excuses for failure to comply with the UCT laws, and we will consider all regulatory options available to us if we identify lenders whose unfair contracts break the law.'

Ongoing compliance monitoring: ASIC states that ASIC and ASBFEO will continue work together to ensure small business loan contracts comply with the unfair contract terms law and that it ASIC will monitor the big four banks' use of the clauses to ensure they are not applied or relied on in an unfair way. ASIC will also examine other lenders' loan contracts to ensure that their contracts do not contain terms that raise concerns under the unfair contract terms law.

[Sources: 18-073MR ASIC reports on changes to small business loan contracts by big four banks; REP 565 Unfair contract terms and small business loans]

In Brief | Government planning to make advancing competition one of ASIC's core objectives and to give the regulator additional resources? The AFR writes that the government plans to implement changes to ASIC's remit, in line with Murray Inquiry recommendations, to make advancing competition one of the regulator's core objectives. Minister for Revenue and Financial Services is reportedly planning to announce the changes 19 March 2018.

[Sources: [registration required] The AFR 18/03/2018]

Australian Prudential Regulation Authority

In Brief | APRA has released revised prudential standard LPS 230 Reinsurance, following consultation. In a letter to all life insurers dated 9 March, APRA stated that the revised standard incorporates a number of changes in response to submissions received during the consultation period. The new standard will come into operation from 1 April 2018.

[Sources: Final release of revised Prudential Standard LPS 230 Reinsurance; Prudential Standard LPS 230 Reinsurance Management]

In Brief | APRA has released quarterly ADI performance statistics for December 2017 and separately, APRA has released statistics on ADI property exposures for December 2017.

[Source: APRA has released quarterly ADI performance statistics for December 2017; APRA has released statistics on ADI property exposures for December 2017]

Other Developments

United Kingdom | Culture is a top priority says the FCA: The UK Financial Conduct Authority has released a paper featuring 28 diverse essays on building good culture with a view to encouraging consideration of the issue by stakeholders.

The Financial Conduct Authority (FCA) has released a 'discussion paper': *Transforming culture in financial services DP 18/2* featuring 28 essays from 'thought leaders' drawn from academia, industry and regulators from inside and outside the UK on the topic of culture as a driver of conduct in financial services. 'Culture in financial services is widely accepted as a key root cause of the major conduct failings that have occurred within the industry in recent history, causing harm to both consumers and markets' Jonathan Davidson, the FCA's Director of Supervision (Retail and Authorisations) writes. The FCA states that it is not currently seeking formal feedback on the paper, but rather is seeking to prompt stakeholders to participate in the debate about what constitutes a healthy culture and how to promote it.

Key themes identified by the FCA across the essays included in the paper.

The essays relate to four questions.

- **The question of whether there is a 'right' culture.** The FCA writes that it recognises that each firm's culture is different comments that this is appropriate. The FCA adds that that the essayists 'agree with us that there is no one culture for firms to aspire to' but notes that they do believe that healthy culture have some specific characteristics that reduce harm. The FCA also notes that it has introduced minimum standards of behaviour through its Conduct Rules and regulatory interventions eg the introduction of a Senior Managers and Certification Regime (SM&CR) which are at reducing harm to consumers and strengthening market integrity by making individuals more accountable for their conduct and competence.
- **The role of regulation in managing culture.** The FCA writes that its approach to culture and regulation is underpinned by the concept of holding individuals as well as the firm to account and by the concept of holding leaders to account for managing the culture of their organisation. These concepts are reflected in the Senior Managers and Certification Regime, the FCA writes. Ultimately, the FCA adds there isn't consensus among the essayists on the role of regulators in driving culture. There is acknowledgement however, that regulation is only part of the picture and that firms have a role to play.
- **The role of incentives and environment in driving behaviours.** 'This paper confirms the notion that behavioural science is directly applicable to a subject often seen as an art' the FCA comments.
- **How to bring about cultural change.** Though leaders have a role to play in bringing about cultural change, the essayists write, too much focus on 'tone from the top' can 'overlook the complexity' of the issue. Rather, every individual is accountable for the culture of the organisation.

Three common themes identified across the diverse range of essays.

The FCA writes that three themes emerge from the various essays.

1. **Shift in thinking has meant reframing ideas about how to think about, how to assess and how to change culture**: The FCA writes that there has been a shift in thinking about culture and conduct. Previously, the approach tended to be linear ie tying a single cause to a single effect. This has now shifted to a 'dynamic systems based perspective' that acknowledges the role of the whole system around an individual and the interactions and interdependencies between each part of the system in driving good conduct. In practical terms, the FCA writes, this means assessing the alignment between various elements in the system — for example the role of incentives, the influence of peers, managers and leaders — and desired conduct. Practically, this requires a 'whole system approach', rather than focusing on an individual.
2. **The necessity of fostering 'psychological safety and learning' as a means for employees to speak up, collaborate and innovate**.
3. **Recognition of the fact that regulation in its current form can only go so far in improving culture**. Rather firms and other industry stakeholders have a role to play.

In addition, the FCA notes that there are some areas on which there was no consensus. These included the question of whether culture is measurable, and whether there is value in measuring culture if so and how cultural change can be brought about.

How to effect cultural change? Questions for financial services industry, regulators. shareholders and boards to consider: The FCA adds that the paper offers 'actionable insights' for financial services leaders and practitioners to consider how they effect change in their organisations. These include:

- Using behavioural science to guide incentives and cultural change;
- looking beyond the role of leadership in effecting change;
- applying strategic focus to the continuous process for adapting culture;
- fostering environments of trust to encourage openness and learning; and
- applying a systems perspective in assessing both internal culture and external influencers.

[Sources: Financial Conduct Authority discussion paper: Transforming culture in financial services: discussion paper DP18/2 March 2018; Bloomberg 12/03/2018; [registration required] The FT 13/03/2018]

China | China to merge its financial regulators? Reportedly China plans to merge the banking and insurance regulatory commissions, consolidate bureaus that regulate business and pricing into a new market supervision agency and create a new ministry to manage land, ocean and other resources.

Reportedly, China plans to significantly restructure a number of government agencies.

According to the WSJ:

- The Banking and insurance regulators will be merged into a single agency.
- A new national market regulatory administration will be established. It will reportedly have broad responsibilities and will incorporate functions of a half-dozen offices to oversee business competition and practices, from corporate and antitrust regulation to pricing and food safety.
- The National Health and Family Planning Commission will be replaced by a National Health Commission, with responsibilities over public health issues and focusing particularly on policy for an aging society rather than government-set birth limits.
- The Culture Ministry and the National Tourism administration will be merged.
- The environment ministry's remit will be expanded to include antipollution and conservation functions currently spread across six other agencies.

Reuters writes that the new heads of these bodies will be announced before the close of the annual session of parliament on March 20. It's suggested that the change will give the Community Party and President Xi Jinping more oversight and control over the agencies' functions.

[Source: Reuters 13/03/2018; [registration required] The WSJ 13/03/2018]

United States | The Federal Reserve has ordered compliance improvements at the Industrial and Commercial Bank of China Ltd and Industrial and Commercial Bank of China Ltd New York Branch following identification of 'significant deficiencies' in AML compliance.

The Federal Reserve Board has announced the execution of an enforcement action against the Industrial and Commercial Bank of China Ltd and Industrial and Commercial Bank of China Ltd New York Branch following the identification of 'significant deficiencies in the Branch's risk management and compliance with applicable federal and state laws, rules, and regulations relating to anti-money laundering compliance' uncovered in the most recent examination of the Branch by the Federal Reserve. The enforcement action requires the bank and the New York branch to improve corporate governance and management oversight of its anti-money-laundering compliance programs and submit various reports to the Federal Reserve within 60 days and also to engage an independent third party to conduct a transaction review to commence within 30 days.

Further Detail

The enforcement action requires the bank to:

- Submit a governance plan 'to enhance oversight, by the management of the Bank and Branch, of the Branch's compliance with the BSA/AML Requirements and the regulations issued by the Office of Foreign Assets Control of the United States' within 60 days.
- Submit a revised of BSA/AML compliance program within 60 days.
- Submit a revised customer due diligence program within 60 days.
- Submit a revised suspicious activity program 'reasonably designed to ensure the identification and timely, accurate, and complete reporting by the Branch of all known or suspected violations of law or suspicious transactions to law enforcement and supervisory authorities, as required by applicable suspicious activity reporting laws and regulations' within 60 days.
- Submit a written plan to enhance the bank's compliance with Office of Foreign Assets Control Compliance within 60 days.
- Submit a revised internal audit program within 60 days.
- Engage an 'independent third party' to conduct a transaction review within 30 days.
- Primary Contact: Nominate an officer to be responsible for coordinating and submitting to the Federal Reserve the written programs etc required under the order.

[Sources: US Federal Reserve Board of Governors media release 13/03/2018; Enforcement order Docket Nos. 18-013-B-FB]

Singapore | Monetary Authority of Singapore and the Commercial Affairs Department of the Singapore Police Force have announced that they will extend the Joint Investigations Arrangement to cover all offences under the Securities and Futures Act and the Financial Advisers Act.

The Monetary Authority of Singapore (MAS) and the Commercial Affairs Department (CAD) of the Singapore Police Force have announced that they will extend the Joint Investigations Arrangement to cover all offences under the Securities and Futures Act (SFA) and Financial Advisers Act (FAA) to enable greater efficiency and enforcement of capital markets and financial advisory offences. The expansion in the scope of the Joint Investigations Arrangement will commence from 17 March 2018.

The CAD-MAS Joint Investigations Arrangement was launched in March 2015 , when both agencies collaborated to co-investigate market misconduct offences under Part XII of the SFA, such as market manipulation and insider trading activities. To date, MAS writes the joint investigations have secured convictions against three perpetrators of market misconduct.

[Source: MAS media release 13/03/2018]

Corporate Social Responsibility and Sustainability

European Union | European Commission Action Plan on sustainable finance released

The European Commission (EC) has released an action plan on sustainable finance as part of broader efforts to 'connect finance with the specific needs of the European and global economy for the benefit of the planet and our society'. The EC writes that the aims of the action plan are to: reorient capital flows towards sustainable investment in order to achieve sustainable and inclusive growth; manage financial risks stemming from climate change, resource depletion, environmental degradation and social issues; and foster transparency and long-termism in financial and economic activity. Actions identified in the plan include (among others):

- Establishing an EU classification system for sustainable activities.
- Creating consistent standards and labels for green financial products.
- Fostering investment in sustainable projects.
- Incorporating sustainability when providing financial advice (amendment of MiFID II and IDD delegated acts).
- Developing sustainability benchmarks.
- Clarifying institutional investors' and asset managers' duties.
- Incorporating sustainability in prudential requirements: The Commission will explore the feasibility of the inclusion of risks associated with climate and other environmental factors in institutions' risk management policies and the potential calibration of capital requirements of banks as part of the Capital Requirement Regulation and Directive.

[Sources: European Commission: Action plan: Financing Sustainable Growth 08/03/2018; Investment Week 12/03/2018]

ACCR proposal at Rio Tinto moot? Only Australian investors will have the opportunity to vote on the company's continued membership of the Minerals Council after the company determined that it would not present the proposal to UK investors but this may now be moot as the Minerals Council has reportedly changed its stance on climate and Rio (and possibly BHP?) reportedly look set to remain members.

The Guardian writes that Rio Tinto Ltd (RTL), which like BHP is dual listed in Australia and the UK, will not allow its UK shareholders will to vote on the Australasian Centre for Corporate Responsibility (ACCR) proposal at the upcoming AGM.

The Guardian notes that there is no legal requirement that RTL present the proposal at its UK AGM since the proposal was filed only to the Australian arm of the company. The Guardian quotes a spokesperson from ACCR as commenting that by allowing only the Australian arm of the company to vote on the motion, RTL appeared to be taking a position against the proposal and attempting to frame the issue as an Australian-specific rather than a global issue. The article reports that an RTL spokesperson said that the company is working constructively with the co-filers of the motion and would be happy to continue to do so: 'Our willingness to maintain this dialogue, including at the upcoming shareholders meeting in London, is not constrained by the fact that no formal resolution will be considered at the London AGM' the article quotes RTL as stating.

Minerals Council changes its stance — Rio Tinto (and BHP?) to remain members: The AFR reports that the Minerals Council has adopted some of BHP's public positions on climate change and energy policy following threats from BHP that it would stop being a member of the lobby group.

Rio Tinto has reportedly welcomed the change in stance. The AFR quotes a Rio Tinto spokesman as stating that the change in position is a 'a good development…We've been engaged in the process and it affirms a number of positions on climate change that we consider important'.

The Australian writes that Rio Tinto has since committed to remain a member and suggest that BHP also looks set to remain a member.

[Source: The Guardian 09/03/2018; [registration required] The AFR 15/03/2018; [registration required] The Australian

Financial Services

Royal Commission | First Round of hearings: Consumer Credit hearings 13 March to 16 March

- The Financial Services Royal Commission commenced its first round of public hearings starting Tuesday 13 March. The first round hearings will focus on consumer lending products as per the schedule of Topics and Case studies (see: Governance News 05/03/2018).
- The 13/3 to 16/03 hearings focused on the first topic as per the schedule: Residential Mortgages and on the case studies under that topic namely the: NAB Introducer Program and fraudulent loan applications (13/03 and 14/03 hearings); the Aussie Home Loans fraudulent brokers and broker arrangements (15/03 and 16/03 hearing) and the CBA accreditation of brokers and broker arrangements (15/03 hearing).

Common themes and questions for the inquiry: The common themes and questions for inquiry by the Commission during the Round 1 hearings include:

- Whether the misconduct in question was attributable to a particular culture, system, or practice within the entity, including in relation to remuneration incentive or commission arrangements.
- Why the misconduct went undetected (in some instances for a long period of time).
- Whether the entity's processes were adequate to prevent and detect the misconduct.
- Whether the entity responded respond in a timely and sufficient way to the misconduct.

Counsel Assisting's opening address dealt with the following issues:

- Outlined why each of the consumer lending products to be explored are of significance to consumers and to financial services entities.
- The key features of the complex legal framework in which consumer lending occurs and the particular roles that credit providers and intermediaries play in the provision of consumer credit.
- What consumers have told the Commission about their consumer lending experiences through public submissions submitted via the Commission's online portal, and also from consumer bodies and advocates.
- What the two external dispute resolution bodies who deal with consumer lending disputes, the Financial Ombudsman Service and the Credit and Investments Ombudsman have told the Commission.
- The work that regulators, such as ASIC and APRA have done in relation to consumer lending, some which remains ongoing, especially the second report on interest only home loans by ASIC which is due later in the year.
- What financial services entities and intermediaries have acknowledged to the Commission as their own misconduct and conduct that has fallen below community standards and expectations in relation to consumer lending by reference to some of the early responses to the Commission's 15 December 2017 letter. The early responses from ANZ, Aussie Home Loans (contained within the CBA responses (as an associated entity), despite the Commission independently approaching Aussie), Citibank, CBA, NAB and Westpac were specifically referred to by Counsel Assisting.
- The nature of the evidence that will be heard over the next two weeks, giving an overview of the case studies that the Commission will be considering and why these case studies have been chosen.

Issues identified

Among the points that emerged from the initial week of hearings were the following (among others).

- **Possible review of the point of sale exemption?** Counsel Assisting Ms R Orr, noted that currently 'Not all entities who engage in consumer credit transactions are required to be licensed under the National Credit Act or to comply with the responsible lending obligations…In particular, the National Credit Regulations provide an exemption for persons assisting consumers to apply for credit at the point of sale, including at car dealerships and retail stores. When the National Credit Act and National Credit Regulations were enacted, members of Parliament foreshadowed that this exemption may be reviewed.

However, the point of sale exemption remains approximately eight years later'. Witness from the Financial Rights Legal Centre, Karen Cox expressed concern about the exemption stating: 'We find the point of sale exemption a serious concern' on the basis that it promotes irresponsible lending practices.

- **Attitude of the industry to 'obedience to the law' to be considered by the Commission?** The first case study considered by the commission dealt with the NAB introducer program and fraudulent loan applications. Anthony Waldron was called as the first witness. Mr Waldron conceded that processes for detecting fraud, managing conflicts of interest and monitoring and reporting processes in connection with the program were ineffective and NAB did not do 'all things necessary to ensure this in respect of large numbers of residential home loans that were the subject of introducer referrals entered into between 2013 and 2016'. He also conceded that the breakdowns were 'contrary to the obligation imposed on NAB as a licensee under section 47 of the National Credit Act'. Commissioner Hayne commented that 'Things go wrong. It's a human system, therefore things go wrong. Sometimes things go wrong through dishonesty. Sometimes things go wrong because of neglect, carelessness, or just sheer coincidence. I understand all of that. There is a whole raft of law up there governing this industry. One thing that I may have to look at, I think, is what the attitude, either of the industry generally, if there were such a thing, participants in the industry, is to the notion of obedience to the law. Obedience to the law that governs the way they conduct their affairs. There may be a difference – I don't say there is – there may be a difference between a breakdown in controls and an acknowledgment of breach of law. Treat that as the soliloquy it undoubtedly is, Mr Waldron, or deal with it as you wish. But I don't want people ignoring the fact these are ideas that are at least on the table'.
- **Review of broker incentives?** The second and third case studies to be considered by the Commission related to brokers and broker arrangements (Aussie Home Loans fraudulent brokers and broker arrangements and CBA accreditation of brokers and broker arrangements). Lack of transparency in communication to customers around payment of incentives to brokers, and lack of action by the entities in addressing the issue of paying incentives to brokers which encouraged them to sell risky mortgages to consumers to preserve profit, were among the issues identified by the Commission. Failure of internal processes to detect issues with payments of incentives and then to take action to address the issues identified also emerged as an issue.

Round 1 Hearings will continue this week.

Round 2 Hearings: The second round of hearings will commence on 16 April 2018 and will focus on the financial planning and wealth management industry.

Commission has released a fourth background paper: Everyday Consumer Credit: Overview of Australian Law Regulating Consumer Home Loans, Credit Card and Car Loans Background Paper 4

The Commission writes that the paper provides an overview of consumer credit protection law and regulation in Australia and an analysis of the interaction between the regimes focusing on three types of credit products: home loans, credit cards and car loans and on the credit specific provisions in the NCCP Act and the NCC.

The paper also includes discussion of other consumer protection provisions applying to financial services and financial products in the ASIC Act. These provisions provide a 'safety-net' response to issues not adequately addressed by the credit specific legislation. The statutory regime applying to consumer credit provides the major enforcement tool for the regulator in this context, the Australian Companies and Securities Commission (ASIC).

The paper also discusses what 'might be termed 'soft law' options for regulating consumer credit: industry codes, ASIC guides and external dispute resolution (EDR) schemes'. While these regimes do not have the same force as general law and legislation, the Commission writes, from the perspective of many consumers they are 'central to the consumer credit protection regime and to practical redress'.

[Sources: Royal Commission into Misconduct in the Banking Superannuation and Financial Services Industry Public Hearings; Transcripts of hearings 13/03/2018; 14/03/2015; 15/03/2018; 16/03/2018; ABC 18/03/2018; [registration required] The AFR 16/03/2018; 18/03/2018]

Mortgage pricing is 'opaque' and not strongly competitive says ACCC: The ACCC's Residential Mortgage Price Inquiry interim report has found that there is 'less-than-vigorous' price competition, especially between the big four banks.

The Australian Competition and Consumer Commission (ACCC) has released its interim report on competition in residential mortgage pricing. The report examines the 'motivations, influences and processes' behind the pricing decisions of the five banks affected by the government's major bank levy: Australia and New Zealand Banking Group Limited (ANZ), Commonwealth Bank of Australia (CBA), Macquarie Bank Limited, National Australia Bank Limited (NAB), and Westpac Banking Corporation (the Inquiry Banks) during the period 30 June 2015 to 30 June 2017 and the consequences of these decisions for current and prospective borrowers.   The report concludes that mortgage pricing is 'not strongly competitive', especially among the big four banks and that the opaque pricing of discounts offered on residential mortgage rates makes it difficult for customers to make informed choices and disadvantages borrowers who do not regularly review their choice of lender.

The ACCC will issue a final report, considering the residential mortgage pricing decisions of the Inquiry Banks through to 30 June 2018, after that date. .

Preliminary findings

- **Lack of price competition**: The ACCC writes that a review of the internal documents of the Inquiry Banks revealed 'a lack of vigorous price competition between the Inquiry Banks, and the big four banks in particular'. Rather the pricing behaviour of the Inquiry Banks was found to be more consistent with '"accommodating" a shared interest in avoiding the disruption of mutually beneficial pricing outcomes, rather than consistently vying for market share by offering the lowest interest rates.' Chairman Rod Sims commented 'We have seen various references to not wanting to "lead the market down", to have rates that are "mid-ranked" and to "maintain orderly market conduct"'.
- **Lack of transparency on pricing**: 'The discounting by the big banks lacks transparency and it's almost impossible for customers to obtain accurate interest rate comparisons without investing a great deal of time and effort. But the potential savings from these discounts are immense' ACCC Chairman Rod Sims said.   The report states that as a consequence, there is a trend towards borrowers turning to mortgage brokers to provide them with a broader view of the available options. The ACCC comments that while borrowers might assume a broker is offering them independent advice, this may not always be the case as many large mortgage broking businesses are owned by or affiliated with an Inquiry Bank, and brokers are generally paid commissions by the lenders. The ACCC adds that the Inquiry Banks have 'tended to gain a disproportionately high share of referrals from the mortgage broking businesses in which they have an ownership interest'.
- **Basic or 'no frills' loans rates are often higher than standard rates**: The report also found the average interest rates paid for basic or 'no frills' loans are often higher than for standard loans at the same bank. The ACCC comments that 'We consider it to be doubtful that this would accord with most borrowers' expectations.' ACCC Chairman Rod Sims commented 'We think many customers who opted for "basic" or "no frills" loans thinking they are saving money would be surprised to learn they might actually be paying more.'
- **Existing customers not 'rewarded for their loyalty'**: The ACCC found that to attract new borrowers, residential mortgage lenders have been increasing the discounts offered in recent years compared to the discounts they offered to new borrowers in the past. The ACCC concludes that as a consequence, new residential mortgage borrowers often pay a lower interest rate than existing borrowers. Between 30 June 2015 and 30 June 2017, existing borrowers on standard variable interest rate residential mortgages at the big four banks were paying up to 32 basis points more (on average) than new borrowers. 'These findings suggest that many bank customers would likely benefit from either switching mortgage providers, or approaching their bank for a better rate and indicating they are prepared to switch to get one…It seems existing customers are not being rewarded for their loyalty; in fact they are worse off.' ACCC Chairman Rod Sims commented.
- **The public's reaction has been a constraint on pricing**: The ACCC found that 'expectations of strong public reaction have acted as a constraint on pricing decisions, and that without this reaction residential mortgage interest rates could have been higher and/or increases could have been introduced earlier'.

- **Public messaging on rate changes do not always tell the full story:** We observe that there are often multiple factors contributing to the Inquiry Banks choosing to change their headline interest rates but those reasons are not always disclosed in the media releases or other public statements accompanying the rate changes. Instead some public communications focus on one factor, or a subset of the factors, influencing the decision to change rates.
- **Prudential benchmarks have led to increases in some interest rates**: We observe that residential mortgage interest rates have been particularly affected by the Inquiry Banks' reactions to two policy initiatives by APRA aimed at addressing emerging risks to both individual ADIs and the broader financial system from the housing sector. The first of these initiatives, announced by APRA in December 2014, was for ADIs to limit their annual growth in residential mortgage lending to investors to 10 per cent. The second initiative, announced by APRA in March 2017, was to limit residential mortgages with interest only repayments to 30 per cent of total new mortgage lending. The Inquiry Banks tried a number of different approaches to comply with the investor cap.
- **The Major Bank Levy**: As at November 2017, the Inquiry Banks have stated that no specific decisions have been made to adjust residential mortgage prices in response to the Major Bank Levy

Final Report will be released after 30 June: In addition to examining the way banks make their mortgage pricing decisions, the ACCC's Residential Mortgage Pricing Inquiry final report will detail if the banks have adjusted their pricing in response to the Government's Major Bank Levy.

Context

- On 9 May 2017 the Treasurer directed the ACCC to inquire into prices charged or proposed to be charged by Authorised Deposit-taking Institutions (ADIs) (banks) affected by the Major Bank Levy in relation to the provision of residential mortgage products in the banking industry in Australia. The Major Bank Levy came into effect from 1 July 2017, and the Inquiry will consider residential mortgage prices for the period 9 May 2017 until 30 June 2018.
- The ACCC writes that the it is reporting on this period 30 June 2015 to 30 June 2017 in order to have a baseline against which to compare pricing decisions for the review period set by the Treasurer. The ACCC will continue to examine the banks' mortgage pricing decisions and how they have dealt with the Major Bank Levy through to 30 June 2018.
- The inquiry is the first task of the ACCC's Financial Services Unit (FSU), which was formed as a permanent unit during 2017 following a commitment of continuing funding by the Australian Government in the 2017-18 Budget. Alongside the ACCC's role in promoting competition in financial services through its enforcement, infrastructure regulation, open banking, and mergers and adjudication work, the FSU will monitor and promote competition in Australia's financial services sector by assessing competition issues, undertaking market studies, and reporting regularly on emerging issues and trends in the sector.

[Sources: ACCC media release 15/03/2018; Residential mortgage products price inquiry: Interim Report 15/03/2018]

Credit Reporting | The ACCC has instituted proceedings in the Federal Court against credit reporting agency Equifax Pty Ltd for alleged breaches of the Australian Consumer Law

The ACCC has instituted proceedings in the Federal Court against credit reporting body, Equifax Pty Ltd (formerly Veda Advantage Pty Ltd), for alleged breaches of the Australian Consumer Law (ACL).

The ACCC alleges that:

- From June 2013 to March 2017, Equifax made a range of false or misleading representations to consumers, including that its paid credit reports were more comprehensive than the free reports, when they were not.
- Equifax represented that consumers had to buy credit reporting packages for it to correct information held about them, or to do so more quickly when in fact, Equifax was legally required to take reasonable steps to correct the information in response to a consumer's request for free.
- Equifax's represented that there was a one-off fee for its credit reporting services, when its agreement provided that customer's subscriptions to the services automatically renewed annually unless the consumer opted out in advance. ACCC alleges that the renewal terms were an unfair contract term (void under the ACL).

- Equifax acted unconscionably in its dealings with vulnerable consumers including by making false or misleading representations, and using unfair tactics and undue pressure when dealing with people in financial hardship.

[Source: ACCC media release 16/03/2018]

New Zealand | The Minister of Commerce and Consumer Affairs has released the terms of reference for a review of NZ Insurance contract law.

The New Zealand Minister of Commerce and Consumer Affairs has released terms of reference for a review of New Zealand's insurance contract law.

The terms of reference outline the scope and proposed timeframe for the review which will examine a range of issues with insurance contract law, including:

- 'Disclosure obligations for policyholders
- technical issues that have been identified by the Law Commission and insurance industry
- gaps in New Zealand's regulation of insurers' conduct
- the scope of terms defined to be not "unfair contract terms" under the *Fair Trading Act 1986* (NZ), and
- consumers' ability to find and compare prices and policies'.

The Ministry of Business, Innovation and Employment is preparing an issues paper which is planned for release and public consultation in mid-2018.

[Source: New Zealand Ministry of Business Innovation and Employment media release 06/03/2018]

In Brief |Following the identification of 'significant issues' with how responsibly second charge lenders were lending, the UK Financial Conduct Authority has written to second charge lenders asking them to review their mortgage lending processes and confirm to the FCA by 1 May 2018, they are lending responsibly and that their processes, systems and controls ensure this.

[Source: Financial Conduct Authority: Dear CEO Letter second charge lenders 01/03/2018]

In Brief | United Kingdom: Insurance cover for financial advisers providing pension transfer advice is reportedly being withdrawn by insurers amidst an investigation by the Financial Conduct Authority into poor transfer advice and concerns over a new pension mis-selling scandal writes The FT. The FCA said it recognised the risk of professional indemnity insurers withdrawing from the market for pension transfer advice, and was reviewing the situation.

[Source: [registration required] The FT 12/03/2018]

In Brief | Technological changes in the banking sector have prompted regulators to issue guidance on attracting and managing staff with the appropriate skills in Singapore: The Monetary Authority of Singapore, The Association of Banks in Singapore, the Ministry of Manpower, National Trades Union Congress and Singapore National Employers Federation have issued guidance on revising HR policies and practices in the banking industry in light of the technological changes in the industry and the consequent need to upskill and recruit staff with the necessary skillset.

[Source: Monetary Authority of Singapore media release 14/03/2018]

Accounting and Audit

Audit quality | International Forum of Independent Audit Regulators sixth annual survey of inspection findings has found that 40% of audit engagements were deficient and that improvement is needed.

The International Forum of Independent Audit Regulators (IFIAR) (which is comprised of independent audit regulators from 52 jurisdictions representing Africa, North America, South America, Asia, Oceania, and Europe) has released its sixth annual report on the results of its sixth annual survey of inspection findings arising from its member regulators' individual inspections of audit firms affiliated with the six largest global

audit firm networks. IFIAR members reported that 40% of audit engagements inspected had at least one finding of deficiency, compared to 42% in the 2016 survey and to 47% in the first survey capturing this percentage (2014 survey).

High number of findings is indicative of the 'need for improvement': IFIAR comments that though the survey results are only one measure of progress in improving audit quality, the high number findings is indicative of the 'need for improvement': Although the frequency of findings from inspections of individual audit engagements has reduced on an overall basis compared to the last survey, IFIAR adds, progress was not experienced in all jurisdictions or at the same rate and no definitive trends were noted for findings arising from inspections of firm-wide systems of quality control. IFIAR comments that 'These results affirm IFIAR's views that the global networks must continue in their efforts to strengthen their systems of quality control and drive consistent execution of high quality audits throughout the world'.

On track to meet the 29% or less goal by 2019: IFIAR notes that in 2015, the IFIAR Global Audit Quality Working Group set a goal for the six largest network firms to reduce the number of deficient audits reported by a least 25% ie to 29% or less by 2019.

IFIAR comments that the 2017 survey results show a 30% rate of findings at the mid-point in this measurement period. The six largest networks and their individual member firms have taken actions over several years with the objective of addressing deficiencies in audit execution in these jurisdictions. IFIAR adds that the six largest network firms have indicated their commitment to sustained efforts to maintain and further reduce the overall level of findings over the target to 2019.

About the survey: IFIAR collected information about two categories of activities: inspections performed on firm-wide systems of quality control and inspections of individual audit engagements. Forty-two IFIAR members contributed to the 2017 survey.

[Sources: Deloitte media release: 09/03/2018; IFIAR stakeholders announcement 08/03/2018; IFIAR 2017 inspection findings report 08/03/2018; [registration required] The FT 12/03/2018]

United States | Securities and Exchange Commission (SEC) has charged foreign affiliates of KPMG, Deloitte, BDO with improper audits. The firms, without admitting or denying SEC's findings, have agreed to settle the charges by paying penalties or disgorging their audit profits.

The Securities and Exchange Commission (SEC) announced that it has charged foreign affiliates of KPMG, Deloitte & Touche, and BDO for their involvement in audit work that SEC alleges 'circumvented the full oversight of the Public Company Accounting Oversight Board' (PCAOB).

SEC states that Deloitte & Touche Chartered Accountants in Zimbabwe and KPMG in Zimbabwe breached Section 102 of the Sarbanes-Oxley Act (which makes it unlawful for any accounting firm not registered with the PCAOB to prepare, issue or participate in the preparation or issuance of any audit report), and BDO Canada LLP and KPMG in South Africa engaged in improper professional conduct, violated Rule 2-02 of Regulation S-X (failed to meet reporting requirements), and caused the audit client to violate its reporting obligations.

SEC writes that the firms agreed to settle the charges by paying penalties or disgorging their profits from the audits. Without admitting or denying the findings, BDO Canada agreed to pay a $50,000 penalty, KPMG in South Africa agreed to pay a $100,000 penalty, Deloitte in Zimbabwe agreed to pay disgorgement and interest totalling $99,057, and KPMG in Zimbabwe agreed to pay disgorgement and interest totalling $141,305.

Scott W Friestad, Associate Director of the SEC's Division of Enforcement commented: 'It's in the best interest of Main Street investors that all firms substantially involved in the audit of a public company are properly registered with the PCAOB so they are subject to the oversight necessary to ensure accuracy and prevent fraud…These unregistered foreign component auditors performed significant audit work outside the PCAOB's regulatory purview, and the principal auditors failed to consider the registration status of these firms as they used their work.'

[Sources: Securities and Exchange Commission media release 13/03/2018]

Risk Management

Whistleblowing

Top Story | ACSI report finds ASX200 codes of conduct and whistleblower systems are weak: ACSI advocates changes to ASX Corporate Governance Principles and Recommendations, continuing engagement on legislative change and strengthening of board oversight to address.

The Australian Council of Superannuation Investors (ACSI) has released a report: *ACSI Codes of Conduct Whistleblowing and Corporate Culture* which has identified a number of weaknesses in the quality and coverage of codes of conduct and limitations in the whistleblowing systems at many ASX 200 companies. This is of concern, ACSI CEO Louise Davidson writes, because these weaknesses represent 'a material risk' the 'reputation, licence to operate and value' of the companies in question. The report includes three recommendations to address the weaknesses identified: strengthening board oversight; strengthening guidance in the *ASX Corporate Governance Principles and Recommendations* and continuing engagement with government on legislative change.

Key Findings

Code of Conduct issues

- **Poor risk management of some risks and zero coverage of some key risks in codes of conduct**: According to the report, 67% of companies failed to cover five of the 13 recommended topics in their code of conduct. Overall, ASX50 companies were found to have better coverage than the ASX51-200 companies, but there were still, ACSI writes, 'significant gaps among their coverage'. These omissions include: fair dealing/product responsibility, data protection and cybercrime, anti-money laundering and counter-terrorism finance (AML/CTF) which ACSI comments are known business risks. ACSI states that 'Companies whose codes of conduct do not include key topics miss an important opportunity to manage these risks'.
- **Set and forget? Codes of conduct are not being regularly reviewed**: ACSI found that 58% (116 ASX200 codes of conduct) had not been reviewed in last two years or were undated. ACSI adds that, 8% (15 codes of conduct) had not been reviewed for five years or longer. ACSI notes that the New York Stock Exchange recommends that codes of conduct be reviewed every two years, or after significant corporate compositional changes – an approach ACSI supports.
- **'Tone from the top' is missing**: ACSI states that an 'essential element in setting the tone from the top' is signalling endorsement of the code of conduct by the CEO eg via an introduction. ACSI found that a relatively small proportion — 28% (56 ASX200 codes of conduct) — included an introduction by the CEO.
- **Hard to read, navigate and put into action**: ACSI writes that a key factor in determining whether a code of conduct will be effective is the usability of the code ie the ease with which it can be read, interpreted and put into action. ACSI suggests that the use of case studies, questions and answers, frequently asked questions could assist in this, for example. ACSI found that only 17% of companies incorporated these features into their codes.
- **Very few codes of conduct demonstrate 'leading practice'**: According to ACSI, 6% or 11 codes demonstrated 'leading practice' as measured by being two years old or less, using examples, Q&As or case studies and setting a tone from the top by having a CEO introduction. ACSI comments: 'Clearly, there is significant opportunity for ASX200 companies to improve the quality of their codes of conduct'.

Whistleblowing systems — weaknesses

- **According to ACSI, a number of 'vital features' are absent from many whistleblowing systems**. Many ASX200 companies do not disclose if they offer anonymity (91 companies or 45%) or 24-hour availability1 (97 companies or 48%) or a commitment that retaliation is not acceptable (71 companies or 36%) ACSI writes.
- **Missed opportunity?** ACSI states that whistleblowing is the initial source of detection for 39% of frauds and the code of conduct is the document most widely distributed to employees. Yet, ACSI notes, a relatively small proportion of codes of conduct — 38 ASX200 codes of conduct (19%) — make no reference to whistleblowing. ACSI comments that this is 'a significant missed opportunity for companies to detect fraud as well as other types of wrongdoing'. ACSI CEO Louise Davidson states, 'I find it hard to fathom that so many of Australia's largest listed companies tolerate such significant gaps in their codes of

conduct and whistleblowing systems. This represents a material risk to their reputation, licence to operate and value'.

Three recommendations to reduce the risk of poor corporate culture

The report includes three recommendations to address the issues identified: strengthening board oversight; strengthening guidance in the ASX Corporate Governance Principles and Recommendations and engaging with government on legislative change.

- **Strengthening board oversight of codes of conduct and whistleblowing systems: Investors and directors should ask relevant questions of boards and company management.** ACSI suggests that active questioning by both directors and by investors will encourage boards to have more robust oversight of codes of conduct and whistleblowing systems. To assist in this, the report includes a set of suggested questions for investors to ask boards and for directors and senior management to consider internally to identify gaps in the quality of the codes of conduct and whistleblowing systems.
- **ASX Corporate Governance Principles and Recommendations (ASX Principles and Recommendations) (due for revision in 2018).** ACSI writes that it is actively advocating for improvements to address weaknesses in companies' codes of conduct and whistleblowing systems identified in the report. More specifically ACSI states that it intends to recommend that the following practices be included in the revised edition of the Principles and Recommendations:
  - Encourage the inclusion of questions in engagement surveys which assess the consistency of lived behaviour as compared with the company's espoused values.
  - Codes of Conduct: regular review of codes of conduct to ensure that their ongoing relevance; encourage the use of practical case studies, Q&As and FAQs and a framework for ethical decision-making in codes of conduct to promote education and understanding; and independent testing of the implementation of codes of conduct (including communication and training effectiveness) and whistleblowing systems.
  - Whistleblowing: whistleblowing systems should allow users to remain anonymous and be available 24 hours a day; ensure that staff that report wrongdoing are protected against retaliation and supported; remediation policies for those found to suffer retaliation for wrongdoing are in place; and provision for services to answer queries regarding the code of conduct (a 'helpline') as well as for reporting wrongdoing ('hotline' services).
- **Legislative change — Whistleblowing Bill does not go far enough**: ACSI notes that the government introduced the *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017* in December of 2017. ACSI comments that the 'draft Bill does not go far enough to promote effective whistleblowing protections. We will be advocating for additional protections and encourage other investors to do the same'.

[Note: *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017* (Whistleblower Bill) was referred to the Economics Legislation Committee for inquiry and report by 16 March (see: Governance News 08/12/2018). On 16 March, the date was extended to 22 March 2018.]

A significant opportunity to 'promote a more resilient culture': ACSI CEO Louise Davidson comments on the report findings overall: 'We have identified a significant opportunity for companies to promote a more resilient culture by addressing shortcomings in their codes of conduct and whistleblowing systems. We're urging companies to move beyond a tick the box mentality and ensure their approach works in practice. We encourage investors to support this process, by asking directors and senior managers questions about their codes of conduct and whistleblowing systems. For our part, ACSI is advocating for leading practices to be enshrined in the legislation that applies to listed companies'.

About the report: ACSI writes that the research and conclusions in the report are based on a review of the relevant literature and a desktop analysis of publicly available codes of conduct and separate whistleblowing policies. The ASX200 codes of conduct and whistleblowing policies examined in this research were accessed between January and March 2017.

[Sources: Australian Council of Superannuation Investors media release 14/03/2018; ACSI Codes of Conduct Whistleblowing and Corporate Culture 14/03/2018; SMH 14/03/2018]

European Union | Whistleblower protections are still weak across Europe and need strengthening according to research by the Change in Direction project.

Blueprint for Free Speech has released a new report in two parts: *Gaps in the System: Whistleblowers Laws in the EU* and *Safe or Sorry: Whistleblower Protection Laws in Europe Deliver Mixed Results* which evaluates specific whistleblower protection laws across all EU member countries against nine recognised European and international standards and assesses how well whistleblower laws are operating in practice.

The report finds that (among other things):

- **Protections are still low across EU countries:** Only four countries – France, Ireland, Malta and the UK – scored more than 50%, with Ireland scoring the highest at 66.7%. Only 13 of the 28 countries scored above 25%. Seven countries (25%) met none of the standards, in whole or in part, and scored 0% across all categories: Czech Republic, Denmark, Estonia, Finland, Lithuania, Poland and Spain.
- **Particular areas of weakness** identified in the report include:
  - **Protection of whistleblowers from all types of retaliation**: 79% of EU countries score a zero on providing immunity from prosecution for disclosing sensitive information. When it comes to protecting whistleblowers from all types of retaliation, 13 countries – 46% of EU member states – fail this standard. This is important because whistleblowers will not step forward if they fear being demoted, sacked or threatened.
  - **Penalties for retaliation against whistleblowers**: 75% of EU countries score a zero on penalties for whistleblower retaliation and other mistreatment.
  - **Disclosure channels**: When it comes to providing a range of disclosure channels, 43% of EU-member countries also failed to meet any of this standard. This standard is important as it reflects countries' commitment to freedom of expression.
- **Some signs of progress?** Of 16 countries (57% pf the EU) with specific provisions in place, 12 have passed their laws since 2011. Three of the four highest-scoring countries passed their laws since 2013. The report comments that many of the laws in question reflect European and international standards – namely, those in France, Ireland, Malta, Italy and Slovakia. However, the report writers comment that as the laws have only been enacted so recently, no long-term assessment of their efficacy in providing reliable disclosure channels and protecting employees from reprisals is possible. The report writers argue that this is a 'clear result' of several 'positive trends'. These include: the recent development of standards and principles by the Council of Europe, OECD, UN and other international organizations, and by NGOs specialising in whistleblower protection; increased media coverage of whistleblower cases, including high-profile political, banking, financial and national security scandals; enhanced appreciation among policy-makers and citizens of whistleblowing as a highly effective tool to expose and correct crime and corruption; significantly greater attention on whistleblower policies and practice within civil society, academia, journalism organizations and the human rights community.
- **Several EU countries are yet to enact whistleblower protections**: The report comments that several countries that have undergone severe financial hardship and political uncertainty in recent years still lack strong whistleblower rights, despite the fact that these difficulties have been exacerbated by pervasive corruption within government and companies. Among these are Croatia, Greece, Portugal and Spain, though efforts by policy-makers and civil society to pass laws have been underway in Spain. Germany and Finland are also yet to enact specific laws comments the report. The report notes that these and other EU countries lacking specific laws have failed to act despite being signatories to numerous agreements that call on them to do so including the European Convention on Human Rights, UN Convention against Corruption, European Civil Law Convention on Corruption and the European Criminal Law Convention on Corruption.
- **A case for standalone whistleblower laws?** Of the nine highest-scoring countries, eight have a standalone law covering public and private sector employees. The report writers argue that the results overall demonstrate that a 'piecemeal approach' to protecting whistleblowers is less effective than enacting standalone laws, which tend to lead to better results.

About the report: Blueprint's report forms part of the activities of the Change of Direction of Direct Project team in support of whistleblower protection across Europe. The partners in the Change of Direction Project are: Blueprint for Free Speech, FIBGAR, Latte Creative, Libera Association, The Department of Political and Social Sciences at The University of Pavia and GREQAM (Aix-Marseille University School of Economics).. Ireland ranks first in the European Union in protections for whistleblowers, achieving a score of 66.7% in results published Monday, compared with 22.9% for countries within the bloc as a group.

[Sources: Blueprint for Free Speech media release 12/03/2018; Gaps in the System: Whistleblowers Laws in the EU; Safe or Sorry: Whistleblower Protection Laws in Europe Deliver Mixed Results]

In Brief | Victory for good governance? Following allegations against non-executive members of the UK Institute of Directors board including Chair Barbara Judge and board members Kenneth Olisa and Arnold Wagner, all three have reportedly elected to resign from their roles. The IoD has issued a statement in which it praised the courage of the whistleblowers for coming forward and characterised the handling of the issue by the IoD as a victory for good governance.

[Sources: IoD media release: 09/03/2018; 10/03/2018; [registration required] The FT 09/03/2018]

Cybersecurity

How to mitigate against the threat of 'human hacking' MinterEllison's Leah Mooney, Paul Kallenbach and Cameron Oxley outline steps businesses can take.

Writing in The Australian, MinterEllison's Leah Mooney, Paul Kallenbach and Cameron Oxley outline the steps businesses can take to meet the rapidly evolving cybersecurity threat of 'social engineering'.

What is 'social engineering'? 'Social engineering is the term used to describe the manipulation of individuals to bypass cyber-security measures. The concept is based on the premise that it's much easier to trick a human into revealing confidential information than it is to bypass complex cybersecurity controls'. According to the writers, reports of cyber incidents involving social engineering, and increasingly sophisticated forms of social engineering, are on the increase and businesses need to evolve their risk management systems and processes accordingly to meet it.

Steps organisations can take to mitigate the social engineering threat:

- **Awareness and training:** Organisations should ensure employees are trained to recognise and respond to social engineering attacks. The Australian Signals Directorate has published a guide to identifying socially -engineered messages, which encourages users to consider questions including whether they recognise the sender, whether they are being asked to open an -attachment, access a website or perform some other task. You can consult ASD Identifying Socially Engineered Messages for further guidance.
- **Develop good policies and procedures and update regularly**: Given the rapid rate at which threats are evolving, cybersecurity policies and procedures should be regularly reviewed an updated. With respect to social engineering attacks the writers suggest that protocols should be put in place to prevent losses from social engineering scams, particularly where transfers of large sums of money are involved eg having many points of confirmation for payments.
- **Auditing third-party contractors:** It is not sufficient for an organisation to simply implement its own policies and procedures without making arrangements to audit third-party suppliers who have -access to its systems. Some social engineering scams have been perpetrated on organisations using intelligence or access obtained through compromising a third-party contractor's systems. Have the right protocols in place to prevent this from happening.
- **Take out cybersecurity and crime policy insurance: Though businesses should recognise that cyber insurance is not a 'panacea', they should nevertheless review their cybersecurity and crime policies** to ensure there are no gaps in cover for social engineering losses. These losses are often excluded from cybersecurity policies on the basis that a crime policy should provide cover. But a crime policy may not respond where scammed payments are deemed to have been made "voluntarily" by an individual induced to make a payment to a perpetrator's -account. Organisations should therefore consider whether a -social engineering endorsement on their cyber policy is an appropriate solution. They should also consider whether their insurance will -respond to a social engineering scam facilitated through a third-party contractor's systems, as cover is often limited by reference to an organisation's own computer systems.

- **Continued vigilance:** The writers note that these steps will ensure businesses are more secure against social engineering attacks, but emphasise that continued vigilance is also needed and add that it's up to boards and senior executives to ensure their financial analysts (as well as all of their other personnel) have the tools and know-how required to protect against the risk of 'human hacking'.

[Source: [registration required] The Australian 13/03/2018]

Equifax data breach update| The former Equifax CIO has reportedly been charged by the SEC with insider trading linked to the 2017 data breach at the company: SEC alleges he used confidential information to conclude that his company had suffered a massive data breach, and dumped his stock before the news went public.

The Securities and Exchange Commission (SEC) has announced that civil and criminal charges have been filed against former Equifax Inc chief information officer (CIO), Jun Ying, in connection with the 2017 data breach at Equifax Inc.

Civil charges: The Securities and Exchange Commission (SEC) announced that it has charged a former Equifax Inc chief information officer (CIO) Jun Ying, with insider trading in advance of the company's September 2017 announcement about the data breach that exposed the social security numbers and other personal information of about 148 million US customers. The SEC's complaint charges Mr Ying with violating the antifraud provisions of the federal securities laws and seeks disgorgement of ill-gotten gains plus interest, penalties, and injunctive relief.

Details: SEC alleges that having concluded, based on confidential information, that there had been a data breach at the company, and before the public announcement of the breach, Mr Ying elected to exercise all of his vested Equifax stock options and then sold the shares (for approximately $1m). According to the SEC, by selling before public disclosure of the data breach, Mr Ying avoided more than $117,000 in losses.

Richard R Best, Director of the SEC's Atlanta Regional Office said: 'As alleged in our complaint, Ying used confidential information to conclude that his company had suffered a massive data breach, and he dumped his stock before the news went public…Corporate insiders who learn inside information, including information about material cyber intrusions, cannot betray shareholders for their own financial benefit.'

Criminal charges: SEC writes that the US Attorney's Office for the Northern District of Georgia has announced parallel criminal charges against Mr Ying.

Charges unrelated to stock sales by other Equifax executives? ITNews comments that Mr Ying was not the only executive who sold shares prior to the public announcement of the breach — the company investigated and ultimately cleared four other executives of wrongdoing in November 2017 — but that Equifax has said that the charges against Mr Ying are unrelated.

[Source: Securities and Exchange Commission media release 14/03/2018; [registration required] The FT 15/03/2018; ITNews 15/03/2018]

Coincheck data breach update| Cryptocurrency exchange Coincheck Inc has reportedly spent $435m to compensate 260,000 customers following the January theft of NEM tokens.

The WSJ writes that Japanese cryptocurrency exchange Coincheck, has spent ¥46.3 billion ($435 million) to compensate 260,000 customers for the theft of digital currency called NEM in January (see: Governance News 05/02/2018).

Reportedly the customers received refunds in yen at a rate of ¥88.549 per NEM, in line with earlier promises by Coincheck which is higher, The WSJ writes, than the current market rate but lower than the ¥110 value at the time of the hacking. The WSJ adds that the payments were begun and finished on the same day and that the company used its own funds for the payments.

Reuters writes that Coincheck also resumed accepting withdrawals of some cryptocurrencies (including Bitcoin) that it had put in place following the January theft, though The WSJ writes that it hasn't resumed accepting deposits.

Reuters adds that the news comes after The Financial Services Agency (FSA) directed Coincheck and six other exchanges, to improve risk management processes to prevent the criminal use of digital currency. Reportedly, the FSA said Coincheck lacked proper systems for dealing money laundering and terrorism financing and ordered it to submit a report on how it would improve by 22 March. Reportedly, this is the second action by the FSA since the theft occurred. The WSJ comments that the FSA has not reported significant progress in identifying the hackers.

[Sources: Reuters 12/03/2018; [registration required] The WSJ 13/03/2018]

In Brief | Price of failure to warn users that accounts weren't secure? Yahoo! now owned by Verizon Communications Inc is facing a consolidated class action stemming from three data breaches between 2016 and 2016 in which the personal data attached to 3 billion email accounts was compromised. The four classes of plaintiffs allege that as a result of the company representing that email accounts were secure, they suffered an injury (in the form of the risk of future identity theft, and loss of the value of their personal identifying information). In addition, the plaintiffs allege that as a result of the data breaches, they have been required to spend money to monitor their credit and prevent future identity theft.

[Source: Reuters 14/03/2018; Yahoo Inc Customer Data Security Breach Litigation, U.S. District Court, Northern District of California, No. 16-md-02752].

In Brief | Chief Information Security Officer perspectives on managing evolving cybersecurity risks: Reportedly 80% of CISOs believe their organisation has already been breached?

[Sources: LegalTechNews 12/03/2018]

Other Developments

In Brief | Rio Tinto Ltd is reportedly facing a new inquiry from an anti-corruption agency: Reportedly the Mongolian Anti-Corruption Authority has raised questions about the development of the Oyu Tolgoi mine. Reportedly the request relates to an investigation about possible abuse of power by authorised officials during negotiation of the 2009 Oyu Tolgoi Investment Agreement.

[Source: [registration required] The AFR 14/03/2018]

Key contacts

Insert key contact photos and phone, email details here