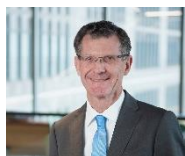


# Governance News

6 August 2018



**Mark Standen**  
Partner

T +61 2 9921 4902 | M +61 412 104 902



**Siobhan Doherty**  
Partner

T +61 2 9921 4339 | M +61 413 187 544



**Kate Hilder**  
Consultant

T +61 3 8608 2907 | M +61 416 353 877

For queries or to subscribe/unsubscribe to Governance News updates, please contact: [kate.hilder@minterellison.com](mailto:kate.hilder@minterellison.com)

## Contents

### Boards and Directors

5

Top Story   Corporate governance stocktake: The AFR reports AMP Chair David Murray has questioned the role and efficacy of the <i>ASX Corporate Governance Principles and Recommendations</i> (and proposed amendments to them) in raising governance standards, and has said that AMP will not be adopting them sparking a broader governance debate.....	5
AICD NFP Governance and Performance Study 2018 released: NFP boards have increased their focus on culture since the last survey but are insufficiently focussed on cyber risk, and divided on the role of the board in driving innovation according to the report.....	8
In Brief   The trend towards companies appointing a board level 'Head of Integrity' (usually following a scandal) does not (and should not?) absolve the board from responsibility and does not necessarily lead to better outcomes argues The FT. ....	9
In Brief   Telstra leadership changes: Telstra CEO Andy Penn has announced a restructure of the executive ranks, including the departure of four senior leaders. Commenting on the change Mr Penn said: 'our new organisational structure and operating model are designed to remove complexity and management layers, decrease the focus on hierarchical decision making and increase the focus on empowered teams making decisions closer to the customer'. ....	9

### Diversity

9

New research confirms that the diversity of the broader Australian population is not represented on ASX100 boards: <i>Beyond the pale: Cultural diversity on ASX 100 Boards July 2018</i> . ....	9
Singapore   Is regular and highly publicised reporting the key to progress on gender balance? Female board representation in SGX 100 is up 20% in 12 months as end of June 2018. ....	11
In Brief   The FT reports that the UK BEIS Committee has called for the extension of gender pay gap reporting requirements to companies with more than 50 employees and for reporting on plans for tackling gender disparities. The call is reportedly based on the fact that the latest data pay gaps are highest in smaller companies.....	11
In Brief   Female board representation is not a priority? The Guardian reports that a number of UK company executives have told a House of Commons Committee that shareholders are more concerned about environmental issues than promoting women to senior positions in boardrooms and some remain unconvinced of the need/benefits of female board representation. ....	11
In Brief   'It's our job to incentivise the market' says the vice-president of supply for BHP Minerals in Australia: BHP is reportedly pushing heavy machinery suppliers to rethink design in line with the needs of a more diverse workforce. The company is also reportedly pushing its labour hire providers to ensure 30% or more of candidates for roles are women. ....	11



In Brief | New Tigerair CEO Merren McArthur (Australia's only female airline CEO) has reportedly used a key address at the annual Centre for Aviation conference to highlight the lack of diversity (ethnicity, age, culture and gender) as a risk for the industry. 'We tend to see aviation as so unique and special, it can only be run by aviation industry veterans... This insularity could mean aviation is missing out on what the industry has previously been renowned for — leading edge innovation she is quoted as saying..... 12

**Institutional Shareholders and Stewardship** 12

In Brief | South Korea's National Pension Service (South Korea's leading institutional investor with US\$570 billion under its control) has reportedly adopted the new investment stewardship code. Health and Welfare Minister Park Neung-hoo has reportedly said that the adoption of the code is intended to boost transparency of its voting rights in companies where it has a stake: 'We are introducing the stewardship code to strengthen transparency and independence of our voting rights, and to improve the NPS' long-term profits' he is quoted as saying ..... 12

**Meetings and Proxy Advisers** 12

United States | SEC has announced that it will hold a 'roundtable' to hear stakeholder views on the need (or otherwise) for the refinement of existing proxy rules. Separately, The Shareholder Rights group has put forward proposals for the improvement of SEC's approach on shareholder proposals under the SEC no-action process..... 12

**Disclosure and Reporting** 13

United Kingdom | The FRC has issued revised guidance on the integration of non-financial information into the strategic report. The guidance encourages companies to consider wider stakeholders and broader matters that impact performance over the longer term..... 13

**Regulators** 14

**Australian Securities and Investments Commission (ASIC)** 14

ASIC has issued new and updated guidance for the funds management industry to reflect changes arising from the Asia Region Funds Passport..... 14

In Brief | From 1 July 2019 the government will reduce and remove the fees for accessing certain information from ASIC business registries. Existing search fees of \$40 will be cut to \$19 to reduce the burden on individuals and businesses that need to access company roles and relationship extracts from the online registries. The government will also extend the fee exemption that is currently available to some journalists for certain registry searches, to all journalists, for all registry searches..... 14

In Brief | *ASIC Report 583: Review of Exchange traded products and retail investors* has found that the Australian ETP market is 'generally functioning well' and delivering promises to investors but there are potential risks that require monitoring by issuers and oversight by market operators. .... 14

In Brief | ASIC has announced changes to reporting dates for certain required notifications in the transition to the new financial adviser professional standards reforms and has clarified the process for recognising advisers as 'existing providers'. .... 14

**Australian Prudential Regulation Authority (APRA)** 15

APRA is reportedly conducting a climate risk survey of regulated institutions..... 15

APRA has released the final two short topic papers on insurance in superannuation and member flows and products as part of its review of the superannuation prudential framework..... 15

In Brief | APRA has released its response to industry feedback on the proposed replacement of Direct to APRA (D2A) with a new Data Collection Solution. A second phase of industry engagement is now underway to help finalise the choice of the system and the transition and roll-out plan. APRA intends to finalise the design of the new Data Collection Solution this year. The roll-out and transition period is expected to start in the first quarter of 2020. .... 15



In Brief | APRA has released monthly banking statistics for June 2018. .... 15

**Other Developments** 16

United Kingdom | The FCA will take no action against RBS following an investigation into its treatment of business customers. .... 16

In Brief | SEC needs to take a collaborative approach to oversight of the cryptocurrency market? SEC Senior Advisor for Digital Assets and Innovation Valerie Szczepanik has reportedly said that the regulator's less confrontational approach to overseeing the cryptocurrency market, is necessary to ensure cooperation. 'We want people to come talk to us...When I'm in meetings with folks, I want them to see me as someone who's interested in communication and back and forth, and looking to encourage innovation that helps investors and the markets' she said. .... 16

**Financial Services**

16

**Superannuation** 16

Time to adopt APRA and PC recommendations for raising governance standards in the superannuation sector (or not)? AICD managing director and CEO Angus Armour has argued in favour of adopting an 'enhanced set of mandatory governance practices for the superannuation sector'. .... 16

APRA's submission in response to the PC Draft Report into the competition and effectiveness of the superannuation sector rejects the view that current regulatory arrangements are 'confusing or opaque'. .... 17

In Brief | The Superannuation Complaints Tribunal's latest newsletter has provided an update on preparations for the transition to the Australian Financial Complaints Authority (AFCA) transition, and has cautioned that it anticipates an escalation in the number of enquiries and complaints following the Financial Services Royal Commission hearings into Superannuation (commencing 6 August). .... 18

**Other Developments** 18

Top Story | Final PC Report into competition in the Australian Financial System released. The report found there is a lack of competition in the sector and recommends (among other things) that the ACCC be mandated as competition champion..... 18

Top Story | ASIC has approved the Australian Banking Association's (ABA's) new Banking Code of Practice (the Code). .... 24

United States | Wells Fargo has agreed to Pay a \$2.09bn penalty for allegedly misrepresenting the quality of loans used in residential mortgage-backed securities. .... 26

An Australian Yukom? The age reports that ASIC has succeeded in securing freezing orders over nearly \$18m in investor money after alleging AGM Markets, OT Markets and Ozfin ran an unlicensed business that allegedly employed high pressure sales techniques to 'lure' investors to deposit funds on the promise of bonus payments..... 27

APRA has released its annual Private Health Insurance annual coverage survey for December 2017: Overall there were decreases in hospital treatment membership across younger age groups and increases across older age groups in the year to December 2017. .... 27

In Brief | A clear drop in client trust? The 'clear trust deficit' between clients and the financial services sector is worsening, according to joint research from Deloitte Digital and Salesforce. According to the report, only 1 in 3 customers believe that the financial services industry can be trusted. This is attributed to a number of factors including: the Financial Services Royal Commission exposing significant failures of providers, rising customer expectations, technological advancements and new competition..... 28

In Brief | Is ASIC's push for the removal of grandfathered commissions an overreaction? Reportedly, Association of Financial Advisers (AFA) head of policy, Phil Andersen has questioned the factual basis for ASIC's argument for the removal of grandfathered commissions on the basis that in his assessment, they constitute little of the overall income of financial advice practices. .... 28



**Accounting and Audit**

In Brief | Is ASIC's tough stance on auditing firms leading to a 'tick the box' culture? Academics suggest that ASIC's enforcement style has shifted from being more collaborative to being more coercive and in response, firms are adapting their audit process in ways aimed at minimising inspection risk and not necessarily at improving audit quality. 'There is an accusation by the auditors – which ASIC denies – that it is almost as if the regulator needs to keep finding something wrong every month or every year' Professor Moroney is quoted as stating..... 28

In Brief | The UK FRC has announced the closure of its investigation into Grant Thornton UK's audits of Globo Plc. The investigation commenced in December 2015 one month after the company had gone into administration and focused on GTUK's group audit (specifically, its direction, supervision and performance of the group audit engagement). The FRC writes that following consideration; Executive Counsel concluded that 'there was no realistic prospect of a finding of Misconduct' and that the matter would be closed without further action..... 28

**Risk Management**

**Supply Chain Risk** 28

Second only to homicide in terms of the cost to UK society? The UK government has commissioned an independent review of the *Modern Slavery Act 2015* after the release of a report into the social and economic cost..... 28

**Cybersecurity** 29

Notifiable data breaches update | Cyber attacks are the largest source of data breaches, and the health sector reported the largest number of breaches, according to the latest OAIC report. .... 29

The case for 'algorithmic accountability': Is publishing the algorithms behind AI applications a solution for all forms and uses of AI? ..... 30

**Whistleblowing** 30

In Brief | The US Commodity Futures Trading Commission (CFTC) has announced multiple whistleblower awards totaling more than \$45 million. CFTC Director of the Division of Enforcement said that the awards demonstrate the growing success of the CFTC's Whistleblower Program, in particular the increasing volume and complexity of incoming whistleblower submissions and added that he expects 'this trend to continue as the Commission continues to receive increasing numbers of high-quality whistleblower tips'..... 30

**Other Developments** 30

#Metoo allegations against CBS Chair and CEO and more general allegations against the company have reportedly led to an immediate share price drop? ..... 30

**Other News**

Progress update on constitutional recognition for Indigenous Australians | The Joint Select Committee on Constitutional Recognition Relation to Aboriginal and Torres Strait Islander Peoples has released its interim report and called for submissions on the proposed models and principles put forward. Submissions close 17 September..... 31



## Boards and Directors

**Top Story | Corporate governance stocktake: The AFR reports AMP Chair David Murray has questioned the role and efficacy of the *ASX Corporate Governance Principles and Recommendations* (and proposed amendments to them) in raising governance standards, and has said that AMP will not be adopting them sparking a broader governance debate.**

The AFR reports that AMP Chair David Murray has questioned both the role and the efficacy of the *ASX Corporate Governance Principles and Recommendations* (Principles) and more particularly, proposed revisions to the Principles, in promoting strong governance standards on Australian boards. Mr Murray has also reportedly said that AMP 'will not be guided by the ASX corporate governance principles where they either weaken accountability or distract the company from less important issues'. Mr Murray's comments have sparked considerable debate over both the proposed revisions to the Principles and about possible methods of raising governance standards generally.

### **AMP Chair David Murray's critique of the current approach**

- **Efficacy of the principles in raising governance standards is questionable:** The AFR quotes Mr Murray as stating: 'I think APRA should reconsider whether they [ASX governance principles] have any value because the culture report on CBA demonstrated that those governance arrangements didn't operate to protect the company...If you look at the financial sector in Australia those principles haven't been of the slightest value at all.'

[Note: The 'culture report' referred to is the Final Report of the prudential Inquiry into the Commonwealth Bank of Australia released on 1 May. See: Governance News [04/05/2018](#).]

- **Adherence to the Principles is no guarantee of strong internal controls:** Mr Murray reportedly questioned whether adherence to the letter of the Principles is any guarantee of strong or effective internal controls: 'Am I okay because I tell the world I've got an audit committee and I follow the ASX corporate governance principals? Or am I okay because I've figured out the best possible set of procedures for the board to follow in signing off the accounts? They are two very different questions' he is quoted as stating. He went on to say 'There are certain things you can do to reduce risk. For example, the rest of the board, excluding the chairman and the CEO, might want to interrogate the CFO and the auditor without the chairman and the CEO present as part of a financial account sign-off process. That's a control system. People do this on your audit committee now. The question is how effectively it is done!'
- **Excessive focus on non-core management issues:** According to The AFR Mr Murray said that the Principles had led to directors being swamped by hundreds of pages of board papers and not having enough time to debate important strategic issues. Mr Murray also reportedly commented that adherence to the Principles was ineffective in preventing governance failures at AMP and other entities: 'The ASX corporate governance principles contributed to what happened to AMP and others in the financial sector. I'm not excusing anything and I'm not looking for a scapegoat at AMP. It has to fix itself. But these principles don't help at all' he is quoted as stating.
- **Committee structure does not ensure stronger outcomes:** Mr Murray also reportedly questioned the assumption that separating audit, risk, remuneration and nomination functions into committees with independent chairs necessarily leads to better governance outcomes. Mr Murray reportedly said that this enables Committee Chairs to develop special relationships with the CFO, CRO and head of HR and as such, potentially undermines the primacy of the CEO.
- **The approach the regulators have taken is questionable:** 'If it's clear that the governance arrangements in the financial system have been ineffective then have the regulators [the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC)] contributed to that by trying to reduce the separation of non-executive directors from the executive? That's the effect of the way they go about it. Once you do that the board gets bombarded with huge amounts of information without a good system of figuring out what is important and what matters and what doesn't matter. APRA holds the board directly accountable and the way they've picked up the corporate governance principles and made mandatory certain committees tends to join the executive in with the board in many ways' Mr Murray is quoted as stating.

### **AMP approach to addressing governance issues**

Mr Murray has also reportedly said that AMP 'will not be guided by the ASX corporate governance principles where they either weaken accountability or distract the company to less important issues'. Instead, he said that he plans to implement the following.



- **Restore the primacy of the chief executive:** 'I think the board's got to conduct itself in a way that it looks to the CEO for everything'.
- **Elevate the role of internal audit:** 'I'm working through the AMP board issues now but what I can say is that the role of internal audit will be elevated substantially in the way the board does its work' Mr Murray reportedly said.
- **Separation of the board and the executive:** Reportedly, Mr Murray envisions a governance system at AMP similar to what was in place at the Commonwealth Bank of Australia when he was CEO between 1992 and 2005 which he said was successful because it remained separate from the executive (and therefore able to keep its strategic focus). 'A lot of the regulation and the principles don't allow that to happen anymore...When you're being dished up 1000 pages of stuff you're not separate from management' Mr Murray said.

### **Debate on the proposed revisions to the ASX Corporate Governance Principles and Recommendations.**

Mr Murray's comments have sparked debate on both the proposed revisions to the *ASX Corporate Governance Principles and Recommendations* and more broadly on the best means of raising governance standards.

In relation to the proposed changes to the Governance Standards, debate has centred primarily around the following issues.

1. **Level of 'prescription':** Both the Australian Institute of Company Directors (AICD) and the Governance Institute of Australia (GIA) have separately raised concerns about the level of prescription in the proposed amendments to the principles.
  - The AFR quotes AICD CEO Angus Armour as commenting: 'Our concern with this draft is it is moving away from the framing of the document as principles...It seems to be trying to address the issues which have emerged from the Hayne royal commission and APRA report on the CBA but it is not helpful because directors have clear obligations in legislation ... as directors contemplate the needs of their stakeholders they have to balance their sometimes conflicting needs... We think it is enough to ask companies to act in a legal and ethical manner'.
  - Separately, GIA CEO Stephen Burrell has commented that 'the increased level of prescription in a number of areas within the draft Principles and Recommendations encourages a "tick the box" approach to disclosure. This could be counterproductive and would not lead to improved disclosures'. He went on to say that 'Our members are concerned about the marked increase in the level of prescription both in the text of some of the Recommendations and in many areas of the new Commentary' which he said is 'at odds with the intent of the Principles and Recommendations' and is also a contrast to the 'recently published 'shorted, sharper' UK Corporate Governance Code which was revised to reduce the level of complexity'.
  - According to The AFR a number of organisations, and individuals have also raised concerns. These include: The Law Council of Australia, Chartered Accountants and Australian Financial Markets Association and Chair of Energy Australia, Graincorp, HSBC Bank Australia and Virgin Australia Graham Bradley.
  - Business Council of Australia CEO Jennifer Westacott has also expressed agreement with Mr Murray's comments regarding the Principles and more particularly at the level of 'prescription' in the proposed changes. 'I think you've got to be very careful that if you've got a set of guidelines that start to add on to already existing legal obligations, or are very prescriptive about things that you and I could debate for hours the definition of, we've got to get corporate Australia back to focusing on its customers, its staff, its shareholders, the community' she said.
2. **'Social licence to operate':** Both the AICD and the GIA have raised concerns about the introduction of this concept into the Principles.
  - GIA CEO Stephen Burrell commented: 'We [The GIA] are concerned that the phrase "social licence to operate"...is now being used in a way that makes it open to a broad range of potentially extremely subjective interpretations. This term can mean very different things to different parties. The term has become loaded and is easily used to describe opposition or disagreement, rather than what we consider the Council intends, which is a concern going to the heart of how an entity is operating. We are concerned that the term is easily appropriated by interest groups that disagree with proposals to argue that their opposition



indicates that a company has "lost" its social licence to operate, when the fact is that there is a particular group opposed to a course of action or proposal' he said.

- AICD CEO Angus Armour is quoted in The AFR as stating: 'We have significant concerns with the proposed revisions ... including the introduction of the fluid concepts of a 'social licence to operate' and acting in a 'socially responsible manner'. [These] concepts ... are subjective and will add unnecessary complexity and uncertainty... The concept of "social licence" is highly subjective and will be interpreted differently by different stakeholders ... these proposed changes have caused significant concern amongst the director community.'
- Former ASX Chair Maurice Newman has also reportedly expressed concern about the concept stating that 'companies should be focused on keeping your costs down and your customers happy'.

### **Broader debate on the best way to raise governance standards**

- **Do independent directors 'destroy shareholder value'?** The AFR reports that University of New South Wales (UNSW) Professor of Finance Peter Swan has questioned the role and efficacy of the ASX Corporate Governance Principles and Recommendations (the Principles) generally and the role of independent directors in particular in raising governance standards, reportedly describing the Principles as 'made up rules' adopted without evidentiary basis. More particularly, The AFR reports that Mr Swan has questioned the assumption that independent directors necessarily add value, arguing that their lack of specific knowledge of the company is a disadvantage as is their lack of personal investment. The 'ASX rules are designed to promote professional directors who are completely ignorant of the companies of which they are directors' he said. For example, in Mr Swan's view it is because it is boards of industry super funds, largely free of independent directors, that have performed better than their for-profit counterparts. The AFR notes that both The Australian Council of Superannuation Investors and Australian Institute of Superannuation Trustees declined to comment on Mr Swan's views. The article goes on to quote the Association of Superannuation Funds of Australia CEO Martin Fahy as stating: 'The ASX corporate governance council has a consultation process under way and like any policy, it's important to get the balance right between transparency and onerous reporting, so that boards can best perform their strategic roles'.
- **Time to rethink board structure?** Mr Murray's comments have also sparked broader debate around the current approach to raising governance standards generally. Writing in The Conversation, RMIT academics Andrew Linden and Warren Staples have reiterated their own calls for consideration to be given to mandating a 'two tiered board structure for corporations and large companies'. 'Instead of looking to quick conventional fixes...such as re-emphasising directors' duties and increasing diversity through soft targets, we argue that the unitary board structure itself is an underlying factor in systemic misconduct' they write.

[Note: Both writers have written previously that a rethink of the current board structure should be considered. The SMH has also suggested that a two tiered board structure should be considered [03/05/2018](#).]

Citing issues uncovered in the Financial Services Royal Commission, they argue that 'industry self-regulation has failed and corporate boards seem incapable of systemically improving corporate governance' and that failing to consider alternatives to the current system, will result in 'more of the same' issues recurring. They argue that separating the non-executive from executive directors, and creating clear, 'legally separate roles for both groups' would address confusion over roles/accountability. The supervisory board would comprise non-executive directors tasked with 'monitoring and control' eg approving strategy and appointing auditors. Separately, 'a lower' executive management board made up of executive directors would be responsible for implementing the approved strategy and day-to-day management. 'To be clear, relying on market-based responses, self-regulation and shareholder primacy will only result in more of the same they conclude.

[Sources: [registration required] The AFR 01/08/2018; 01/08/2018; 01/08/2018; 01/08/2018; 01/08/2018; 02/08/2018; 02/08/2018; 02/08/2018; 31/07/2018; 31/07/2018; 31/07/2018; 01/08/2018; Business Council of Australia Transcript Jennifer Westacott interview with Ticky Fullerton, Sky Business 02/08/2018; Governance Institute of Australia media release 02/08/2018; The Conversation 06/07/2018; 02/08/2018]



## **AICD NFP Governance and Performance Study 2018 released: NFP boards have increased their focus on culture since the last survey but are insufficiently focussed on cyber risk, and divided on the role of the board in driving innovation according to the report.**

---

The Australian Institute of Company Directors (AICD) has released the latest NFP Governance and Performance Study. The study explored current and emerging issues facing the sector including cybersecurity, innovation, financial viability and culture. The study found 'significant variation in how NFP directors are tackling these issues'.

**Key findings** of the 2018 NFP Governance and Performance Study include the following.

- **Zero financial reward:** 82% of respondents undertake their NFP governance role for no financial reward.
- **Respondents reported that they are busier than previously:** 58% said they were working more than 2 days a month on their NFP, compared to 48% in 2017. Of the 58% working more than 2 days a month on their NFP, 9% said that there were working more than 8 days per month (as compared with 7% in 2017), and 15% (as compared with 11% in 2017) said that they were working 5-8 days per month.
- **Focus on culture has increased:** According to the report, 75% of respondents are actively engaged in monitoring, measuring and leading culture. The report found that boards employ a diversity of approaches in combination, to monitoring and measuring culture. The top five methods used are: staff survey results (45%), staff turnover and dismissals (41%), client survey results (40%), OH&S reports (35%) and client complaints (33%) all rating as common methods. The report comments that this year's results compare favourably with the 2017 survey which found that only 30% of respondents that their boards were actively overseeing culture and only 43% reported that their culture was monitored well. In terms of 'controlling' culture, the tools used nominated as the top three ways utilised to manage culture were: role modelling by the board (51%); role modelling by the CEO (48%); and ensuring policy documents include the desired attributed and values (along with actions required) (38%).
- **Not enough attention to cybersecurity?** According to the report, 56% of respondents view cybersecurity as an operational issue rather than a board issue (19%); do not consider it to be regular board business (33%) or do not consider it relevant to their organisation (4%). Overall, only 38% of Chairs reported that their board had a 'very good understanding' of the impact of a cyber attack on service users and 25% of the probability of a cyber attack on their organisation. The AICD comments that this indicates that there is not sufficient acceptance on some boards of the importance of the issue. The AICD goes on to argue that in the current context, and given many NFPs often safeguard significant quantities of sensitive information, directors need to accept that, 'as with financial literacy and other technically dense elements of their role, some degree of technology literacy is paramount in order to execute their responsibilities proficiently'.
- **Almost half of respondents view their organisation as less innovative than needed:** 44% of respondents indicated that their organisation was less innovative than needed (9% indicating it was 'a lot less innovative than needed' and 35% indicating it was 'a little less innovative than needed'). This is attributed in the report to a number of factors including: whether innovation is viewed as the role of the board or whether it is viewed as the responsibility of the CEO; low levels of net assets and little industry support; dealing with significant change in their operating environment (eg the National Disability Insurance Scheme); and 'balancing change with tradition and sentimentality'.
- **Respondents were divided on the role of the board in innovation:** According to the report, 'about half' of respondents view innovation as an operational issue, essentially the responsibility of the CEO, who they expect to 'drive the innovation and report back to the board.' The other half view innovation as a responsibility of the board. Though the different perspectives were common across all sizes and sectors of respondents, there was a 'noticeable difference' between the views of non-executive directors (NEDs) and executives with executives far more likely to see innovation as their responsibility rather than a board responsibility. The report comments that the high proportion of directors (especially executives) who view innovation as an operation issue, it was 'of concern that only 34% of directors believe the board sets clear expectations for innovation'.



- **NFP Director attributes:** For the first time, the survey also examined the attributes of board behaviour and director personality with the aim of identifying any correlations between certain personalities and performance. The results from the survey suggest that 'the anecdotal evidence of the extent of poor board behaviours is overstated'. The majority (over 80%) of directors agreed with all of the statements reporting that their board maintains a climate of trust, has a common sense of purpose, communicates effectively and is open to different points of view. In terms of personal director attributes, the report found that 'Compared to the average member of the Australian public, the average Australian NFP director is neither extroverted nor introverted, tends to be slightly more agreeable, is highly conscientious, not neurotic and tends to be more open to experience. Not surprisingly, their profile is close to that of business school graduates'.

[Sources: AICD media release 31/07/2018; AICD NFP Governance and Performance Study 2018]

**In Brief | The trend towards companies appointing a board level 'Head of Integrity' (usually following a scandal) does not (and should not?) absolve the board from responsibility and does not necessarily lead to better outcomes argues The FT.**

[Sources: ASX announcement 30/07/2018; [registration required] The FT 28/07/2018]

**In Brief | Telstra leadership changes: Telstra CEO Andy Penn has announced a restructure of the executive ranks, including the departure of four senior leaders. Commenting on the change Mr Penn said: 'our new organisational structure and operating model are designed to remove complexity and management layers, decrease the focus on hierarchical decision making and increase the focus on empowered teams making decisions closer to the customer'.**

[Sources: ASX announcement 30/07/2018; [registration required] The Australian 31/07/2018; [registration required] The AFR 31/07/2018]


## Diversity

**New research confirms that the diversity of the broader Australian population is not represented on ASX100 boards: *Beyond the pale: Cultural diversity on ASX 100 Boards July 2018.***

A study by the University of Sydney Business School entitled *Beyond the pale: Cultural diversity on ASX 100 Boards July 2018* has found, consistent with the latest Leading for Change Report (released by the Australian Race Discrimination Commissioner earlier in the year) that ASX100 boards continue to be non-reflective of the diversity in the broader Australian community. According to the report, the majority of board members are male, overwhelmingly drawn from Anglo-Celtic backgrounds and from male-dominated business networks. Among other things, the six actions identified to help inform future progress include the suggestion that diversity targets should be considered.

### Key Points

- **Australia's population and Australia's workforce are culturally diverse.** According to the most recent census, over 26% of the population was born overseas. The Australian Human Rights Commission (AHRC) recently estimated that 58% of the population has an Anglo-Celtic background; 18% has a European background; 21% has a non-European background and 3% has an Aboriginal or Torres Strait Islander (Indigenous) background.
- **The diversity in the general population and in the workforce is not reflected in the leadership of the public or private sectors.** The AHRC's latest Leading for Change report 2018 (see: Governance News 13/04/2018) noted that up to 95% of the nearly 2,500 executives and up to 97% of chief executives surveyed had Anglo-Celtic or European backgrounds.
- **Benefits of cultural diversity for Australian boards:** Interviewees identified diversity of perspectives; market insight/global reach (ability to reflect/understand/bring insights in relation to a diverse market/customer base); and diverse talent (diversity of skills, experience, culture, age materially add to the quality of decision making) as potential benefits for Australian boards. Noting that available research has limited application in the Australian context (as it tends to focus on a narrow, rather than a broad range of cultural backgrounds) the report states that more research is



needed into the barriers and enablers of cultural diversity in Australian boardrooms and into the benefits.

- **5 barriers to diversity:** The five barriers to cultural diversity highlighted in the report are: limited supply at the executive level; 'assimilationist attitudes and a preference for a western leadership style'; biased filters in promotion and recruitment and selection; lack of awareness and contact with cultural diverse talent; and closed and personal circuit in the recruitment process.

### Action is needed in six areas

To address these issues, the report suggests that action is needed in six areas.

1. **'Consider setting targets** and report on progress toward cultural diversity in order to drive change.
2. **Grow and develop the 'supply'** of culturally diverse leaders in the pathway to board positions with special attention placed on the senior executive ranks of Australian business.
3. **Develop transparent pathways to board membership** to allow greater visibility for aspirants to director positions.
4. **Broaden networking arrangements** to open up access for potential directors from culturally diverse backgrounds.
5. **Learn from other diversity campaigns**, including the progress to date to improve gender diversity around the board table.
6. **Clarify definitions around cultural diversity and make cultural diversity part of the narrative**, going beyond the focus on a global mindset and cultural awareness.'

**The investor community also has a role to play:** Australian Institute of Company Directors General Manager — Advocacy Louise Petschler, is quoted in Which-50 as commenting that there is a lack of research and analysis around the drivers of cultural diversity on boards in Australia. 'We see this as an important step in opening up and helping build that business case and the research base that we know is incredibly persuasive for directors and that will be a really important tool in shifting the conversation' Ms Petschler said. As well as supporting the report's recommendation to improve networking arrangements, Ms Petschler also highlighted the role of the investor community in pushing for greater diversity at board level. 'The boards of listed entities do not exist in isolation. Shareholder activism and shareholder demands are incredibly important and we have seen that in terms of the representation of women on boards' she said.

**Time to consider reporting on cultural diversity?** In a statement, Race Commissioner Tim Soutphommasane said the report confirms the need to do more on cultural diversity in the leadership of organisations. 'This research will guide the action leaders need to take, including the collection of better data on cultural diversity and targets for board appointments based on cultural diversity. We need to see more role models for diverse leadership in Australian society, because you can't be what you can't see. Until people can start seeing themselves represented in institutions including at the board level, we're not going to see the kind of change we should be seeing.' Which-50 reports that speaking at the launch of the report, Mr Soutphommasane, took the recommendation to introduce targets a step further, calling for a legislative mandate for cultural diversity.

[Note: When launching the latest Leading for Change Report in April, Mr Soutphommasane said that concerted action was required, including consideration of the collection and reporting on cultural diversity data See: Governance News [13/04/2018](#)]

**About the Report:** The findings in the report are based on 'in-depth interviews' with 18 non-executive directors and 9 representatives from leading executive search firms. The interviewees were drawn from the Australian Institute of Company Directors (AICD) membership. Interviews were undertaken between December 2017 and June 2018.

[Sources: *Beyond the pale: Cultural diversity on ASX 100 Boards July 2018*; [registration required] *The SMH 30/07/2018*; *Business Insider 30/07/2018*; *AHRC media release 30/07/2018*; *Which-50 01/08/2018*]



## **Singapore | Is regular and highly publicised reporting the key to progress on gender balance? Female board representation in SGX 100 is up 20% in 12 months as end of June 2018.**

---

The Singapore Diversity Action Committee (DAC) has announced that female representation on the top 100 SGX listed companies has increased significantly over the past 12 months.

- Female representation on the top 100 SGX increased 20% over the last 12 months (from 12.2% in June 2017 to 14.7% in June 2018).
- As at 30 June, 33 of the Top 100 companies have more than 20% women's participation on boards.
- Overall, the proportion of all-male boards for Top 100 companies continued to decline from 32% as at end of December 2017 to 27% as at the end of June.
- New board appointments were mostly men but 24% of new appointments in first half of 2018 are women; with 60% of them first-time directors.
- Women's participation on boards of all 738 listed companies increased from 10.3% in June 2017 to 11.2% as at end June 2018.

**Opportunity for board renewal if the 'nine-year rule for director independence' is adopted?** DAC writes that there is 'more room for boards to embrace gender diversity with 101 independent directors on Top 100 companies having served 9 years or more' and 705 for all listed companies. DAC adds that the proposed revision to the Singapore Code of Corporate Governance includes a 'stiffer definition of independence for directors at 9 years' and that based on this definition, 50% of listed companies will be appointing at least one new independent director before long.

**DAC Chair Loh Boon Chye** said: 'With the upcoming revisions to Singapore's Code of Corporate Governance calling for more focus on board diversity, I hope that more companies will think how their board composition could be strengthened in line with its strategic gaps. I believe there is room for more capable women to be appointed to the boards. If the pace is sustained, the Top 100 companies will be the first group of companies to achieve DAC's first-tier target of 20% women on boards by 2020, leading the way for other companies to join in.'

**Is transparency on the issue the key to driving progress?** Commenting on the result, Bloomberg suggests that the 'name and shame' approach — the publication of a biannual ranking of firms based on gender representation — has been effective in driving rapid progress on gender diversity. Another factor in the success of the approach, Bloomberg suggests is the fact that the list, (which details how many women each firm has on its board, who they are and the percentage of female representation) also highlights companies that outperform regarding gender. Bloomberg quotes Diann-Yi Lin, a senior partner at McKinsey and Co as stating: 'There's nothing like a good league table that is regulatory reported that moves people to action'.

*[Sources: Singapore Diversity Action Committee media release 31/07/2018; Bloomberg 31/07/2018]*

**In Brief | The FT reports that the UK BEIS Committee has called for the extension of gender pay gap reporting requirements to companies with more than 50 employees and for reporting on plans for tackling gender disparities. The call is reportedly based on the fact that the latest data pay gaps are highest in smaller companies.**

---

*[Source: [registration required] The FT 02/08/2018]*

**In Brief | Female board representation is not a priority? The Guardian reports that a number of UK company executives have told a House of Commons Committee that shareholders are more concerned about environmental issues than promoting women to senior positions in boardrooms and some remain unconvinced of the need/benefits of female board representation.**

---

*[Source: [registration required] The Guardian 19/07/2018]*

**In Brief | 'It's our job to incentivise the market' says the vice-president of supply for BHP Minerals in Australia: BHP is reportedly pushing heavy machinery suppliers to rethink design in line with the**

---



needs of a more diverse workforce. The company is also reportedly pushing its labour hire providers to ensure 30% or more of candidates for roles are women.

---

[Source: [registration required] *The AFR* 30/07/2018]

**In Brief | New Tigerair CEO Merren McArthur (Australia's only female airline CEO) has reportedly used a key address at the annual Centre for Aviation conference to highlight the lack of diversity (ethnicity, age, culture and gender) as a risk for the industry. 'We tend to see aviation as so unique and special, it can only be run by aviation industry veterans...This insularity could mean aviation is missing out on what the industry has previously been renowned for — leading edge innovation she is quoted as saying.**

---

[Source: [registration required] *The Australian* 03/08/2018]

## Institutional Shareholders and Stewardship

**In Brief | South Korea's National Pension Service (South Korea's leading institutional investor with US\$570 billion under its control) has reportedly adopted the new investment stewardship code. Health and Welfare Minister Park Neung-hoo has reportedly said that the adoption of the code is intended to boost transparency of its voting rights in companies where it has a stake: 'We are introducing the stewardship code to strengthen transparency and independence of our voting rights, and to improve the NPS' long-term profits' he is quoted as saying.**

---

[Note: This follows the recent announcement that State Street has also adopted the stewardship code. See: [governance News 30/07/2018](#)]

[Source: *Yonhap News Agency* 30/07/2018]

## Meetings and Proxy Advisers

**United States | SEC has announced that it will hold a 'roundtable' to hear stakeholder views on the need (or otherwise) for the refinement of existing proxy rules. Separately, The Shareholder Rights group has put forward proposals for the improvement of SEC's approach on shareholder proposals under the SEC no-action process.**

---

In 2010, the US Securities and Exchange Commission (SEC) issued a 'concept release' seeking public comment on whether the US proxy system as a whole 'operates with the accuracy, reliability, transparency, accountability, and integrity that shareholders and companies should expect'.

Since the 2010 concept release, SEC writes, there have been significant changes and in light of this, SEC has announced that it will host a roundtable to facilitate discussion on the proxy process, shareholder engagement and to hear investor, issuer and other market participant views on the need (or not) for existing proxy rules to be 'refined'.

The roundtable agenda items are yet to be confirmed, but SEC Chair Jay Clayton has said that he has requested his staff to consider the following issues (among others): the accuracy, transparency and efficiency of the voting process; how to increase retail shareholder participation; the efficiency of the current shareholder proposal process; use of technology; and the role and regulation of proxy advisers.

[Sources: *United States Securities and Exchange Commission public statement Chair Jay Clayton: Statement Announcing SEC Staff Roundtable on the Proxy Process* 30/07/2018]

### **Suggested changes to SEC's approach to shareholder proposals under the no-action process.**

Writing on Harvard Law School Forum on Corporate Governance and Financial Regulation, The Shareholder Action group has made a number of recommendations for changes to SEC's approach to shareholder proposals under the no-action process to enable it to 'better serve the interests of investors as well as companies by providing greater predictability, reduce need for test cases to clarify the Staff's positions, and restoration of shareholder rights'.

---



The proposed changes include:

- That SEC, 'delineate clear limits on the "new micromanagement doctrine" of excluding proposals that seek specific methods for addressing complex policies' ie that SEC 'confirm that proposals requesting that a company set targets or improve its performance on significant policy issues (eg disclosure and action on ESG strategy) are not considered micromanagement unless they attempt to 'direct minutiae of operations'.
- Establish a rebuttable presumption against a 'conflict' with a shareholder proposal when a management seeks ratification of an existing policy.
- Provide additional detail in no-action decisions, applying the decision-making rule to the facts and language of the proposal to clarify the dispositive issues.
- Identify categories of proposals that SEC views as 'governance' proposals exempt from relevance and significance challenges.
- Clarify the need for the board section of a no-action request to include analysis of the substance and significance of the proposal, as well as documentation regarding the content of the board process.

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 26/07/2018]

## Disclosure and Reporting

**United Kingdom | The FRC has issued revised guidance on the integration of non-financial information into the strategic report. The guidance encourages companies to consider wider stakeholders and broader matters that impact performance over the longer term.**

The UK Financial Reporting Council (FRC) has released revised guidance on the strategic report with the aim of encouraging companies to 'consider wider stakeholders and broader matters' impacting long term performance. The FRC adds that the guidance has been 'enhanced to recognise the increasing importance of non-financial reporting while maintaining the key principles of existing guidance. The FRC believes that the integration of non-financial information into the strategic report is a key part of telling a company's story'.

The FRC writes that the revised guidance:

- Places a greater focus on the directors' duty to promote the success of the company under s172 of the *Companies Act 2006 (UK)*.
- The FRC has clarified that the primary audience of the strategic report as set out in legislation 'remains the shareholders but encourages directors to consider how they have had regard to the interests of wider stakeholders as part of their section 172 duty'.
- Additional guidance on how directors should have regard to broader matters when performing their duty, including considering the interests of employees, suppliers, customers and other stakeholders as well as impacts on the community and environment. This is in line with new legislation requiring directors to have regard to broader issues when fulfilling their duties.

The update is applicable for large companies for the financial year beginning on or after 1 January 2019.

FRC Executive Director Corporate Governance and Reporting Paul George said: 'The revised guidance underpinned by legislation will improve the effectiveness of section 172 and stimulate Board discussions on how companies are considering various factors to ensure their business is sustainable over the long-term including the impacts on the company's key stakeholders. The revisions to the Guidance on the Strategic Report complement the recent changes to the FRC's Corporate Governance Code and as a package will contribute to enhancing trust and transparency in business.'

[Sources: Financial Reporting Council media release 31/07/2018; Feedback Statement Amendments to Guidance on the Strategic Report Non-financial reporting; Board Agenda 31/07/2018]





## Regulators

### Australian Securities and Investments Commission (ASIC)

**ASIC has issued new and updated guidance for the funds management industry to reflect changes arising from the Asia Region Funds Passport.**

---

The Australian Securities and Investments Commission (ASIC) has released new and updated regulatory guides for the funds management industry to reflect changes arising from the Asia Region Funds Passport.

The new and updated regulatory guides are: [Regulatory Guide 131 Funds management: Establishing and registering a fund](#); [Regulatory Guide 132 Funds management: Compliance and oversight](#); [Regulatory Guide 133 Funds management and custodial services: Holding assets](#); [Regulatory Guide 134 Funds management: Constitutions](#); [Regulatory Guide 136 Funds management: Discretionary powers](#); [Regulatory Guide 137 Constitution requirements for schemes registered before 1 October 2013](#); and [Regulatory Guide 138 Foreign passport funds](#).

#### Key Changes

ASIC highlights the following as of particular relevance.

- The guidance provides information on ASIC's decision-making process for registering a managed investment scheme or passport fund and good practice examples/case studies on a range of compliance issues including previous ASIC decision on relief.
- RG 132 has guidance on compliance management systems consistent with *Australian Standard AS ISO 19600:2015: Compliance management systems—Guidelines* (AS ISO 19600:2015). The changes outline the type of compliance management system ASIC 'believe can be adopted to enhance compliance with legal and regulatory obligations'. ASIC notes that legal requirements for the contents of a registered scheme's compliance plan and its audit have not changed.
- ASIC notes that the updates do not include changes arising from corporate collective investment vehicles (CCIVs), as the legislation has not yet passed through Parliament. ASIC states that it will review and re-release these seven regulatory guides to include material for the new CCIV regime after this regime is implemented into Australian law.

*[Source: 18-222MR ASIC updates guidance for funds management industry]*

**In Brief | From 1 July 2019 the government will reduce and remove the fees for accessing certain information from ASIC business registries. Existing search fees of \$40 will be cut to \$19 to reduce the burden on individuals and businesses that need to access company roles and relationship extracts from the online registries. The government will also extend the fee exemption that is currently available to some journalists for certain registry searches, to all journalists, for all registry searches.**

---

*[Source: Minister for Revenue and Financial Resources Kelly O'Dwyer media release 30/07/2018]*

**In Brief | ASIC Report 583: Review of Exchange traded products and retail investors has found that the Australian ETP market is 'generally functioning well' and delivering promises to investors but there are potential risks that require monitoring by issuers and oversight by market operators.**

---

*[Sources: 18-226MR ASIC's review of exchange traded products identifies areas for improvement; Report 583: Review of exchange traded products and retail investors]*

**In Brief | ASIC has announced changes to reporting dates for certain required notifications in the transition to the new financial adviser professional standards reforms and has clarified the process for recognising advisers as 'existing providers'.**

---

*[Source: 18-225MR Professional standards reforms for financial advisers - ASIC update]*



## Australian Prudential Regulation Authority (APRA)

### APRA is reportedly conducting a climate risk survey of regulated institutions.

---

The Australian reports that the Australian Prudential Regulation Authority (APRA) is conducting a climate risk survey of banks, insurers and superannuation funds to assess the level of institutional awareness of climate-change risks, and the measures taken so far.

According to the report, reassurance has been sought as to the measures implemented to address institutions' exposure to climate change, overall appetite for risk, and risk management processes put in place to limit vulnerabilities and capitalise on opportunities. Reportedly, best practice will be shared as industry guidance.

The Australian comments that this latest move is another indication that APRA is sharpening its focus on the issue and notes that the regulator has been focused on lifting awareness of the risks flowing from climate change for some time. The report adds that the survey will add to the work already being undertaken by the regulator in this space, for example APRA has already established an internal climate change financial risk working group to develop its supervisory response and has also developed an a cross industry heat map to identify the key climate risks of each APRA-regulated industry.

*[Source: [registration required] The Australian 31/07/2018]*

### APRA has released the final two short topic papers on insurance in superannuation and member flows and products as part of its review of the superannuation prudential framework.

---

As previously reported in Governance News [28/05/2018](#) and [09/07/2018](#); the Australian Prudential Regulation Authority (APRA) is currently undertaking a comprehensive post-implementation review of the superannuation prudential framework introduced in 2013.

The review has been conducted in three 'tranches' and short topic papers were released this week. The two papers are:

- *Short topic paper 5: Insurance in superannuation.* This includes a review of Prudential Standard SPS 250 (Insurance in Superannuation), Reporting Standard SRS 161.0 (Self-Insurance) and Reporting Standard SRS 250.0 (Acquired Insurance).
- *Short topic paper 6: Member flows and products.* This covers a review of Prudential Standard SPS 160 and Reporting Standard SRS 160.1 (Defined Benefit Matters), amongst other prudential and reporting standards.

**Timeline:** Submissions on all three tranches are requested by 26 September. The final report on the superannuation post-implementation review is expected to be released by early 2019.

*[Sources: Short topic paper three: financial requirements, operational risk and outsourcing; Short topic paper four: Investments]*

**In Brief | APRA has released its response to industry feedback on the proposed replacement of Direct to APRA (D2A) with a new Data Collection Solution. A second phase of industry engagement is now underway to help finalise the choice of the system and the transition and roll-out plan. APRA intends to finalise the design of the new Data Collection Solution this year. The roll-out and transition period is expected to start in the first quarter of 2020.**

---

*[Sources: APRA media release 30/07/2018; APRA is replacing D2A]*

### In Brief | APRA has released monthly banking statistics for June 2018.

---

*[Source: Monthly Banking Statistics June 2018]*



## Other Developments

### United Kingdom | The FCA will take no action against RBS following an investigation into its treatment of business customers.

---

The Financial Conduct Authority (FCA) has issued a statement confirming that following an investigation, no further action will be taken against the Royal Bank of Scotland (RBS) concerning its treatment of small and medium sized enterprise customers transferred to its global restructuring group. RBS CEO Andrew Bailey is quoted as stating: 'It is important to recognise that the business of GRG was largely unregulated and the FCA's powers to take action in such circumstances, even where the mistreatment of customers has been identified and accepted, are very limited. Taking action was therefore always going to be difficult and challenging but after carefully considering all the evidence we have concluded that our powers to discipline for misconduct do not apply and that an action in relation to senior management for lack of fitness and propriety would not have reasonable prospects of success'.

Mr Bailey went on to acknowledge the 'frustration' that many GRG customers would likely feel as a result of the decision and emphasised that the 'fact that we can't take action in no way condones the behaviour of RBS.' He added that 'Although commercial lending to SMEs is not regulated by the FCA, the Senior Managers Regime (introduced in 2016) means that we are now able to hold senior management of banks to account for the way that they treat their SME customers and the FCA will do that'.

The FCA has reportedly faced criticism for its decision and there have been calls for the regulator to be given greater powers to act on such cases. Treasury Select Committee Chair, Nicky Morgan has reportedly said that the government urgently needs to examine 'what additional powers the FCA require' calling yesterday's decision deeply disappointing for victims of the GRG.

The Guardian quotes RBS Chair Howard Davies as commenting: 'The board welcomes the FCA's confirmation that it has concluded its investigation into the bank and that no further action will be taken. We await the publication of the FCA's full account and will reflect carefully on its findings to learn any further lessons from what was a hugely challenging time for the bank, its customers and the wider economy. The board continues to focus on putting things right for customers through our complaints process and ensuring that past mistakes cannot be repeated. The way the bank deals with business customers in financial difficulty is fundamentally different now.'

*[Sources: FCA media release 31/07/2018; City AM 31/07/2018; 31/07/2018; [registration required] The FT 31/07/2018; The Guardian 01/08/2018]*

**In Brief | SEC needs to take a collaborative approach to oversight of the cryptocurrency market? SEC Senior Advisor for Digital Assets and Innovation Valerie Szczepanik has reportedly said that the regulator's less confrontational approach to overseeing the cryptocurrency market, is necessary to ensure cooperation. 'We want people to come talk to us...When I'm in meetings with folks, I want them to see me as someone who's interested in communication and back and forth, and looking to encourage innovation that helps investors and the markets' she said.**

---

*[Source: [registration required] Bloomberg 30/07/2018]*

## Financial Services

### Superannuation

**Time to adopt APRA and PC recommendations for raising governance standards in the superannuation sector (or not)? AICD managing director and CEO Angus Armour has argued in favour of adopting an 'enhanced set of mandatory governance practices for the superannuation sector'.**

---

Ahead of the commencement of the Financial Services Royal Commission Round 5 Hearings into Superannuation, there has been strong media focus on governance standards generally, and within the superannuation sector more particularly.

Writing for The Australian Financial Review, Australian Institute of Company Directors (AICD) Managing Director and CEO Angus Armour has argued there is a need for the sector to adopt an 'enhanced set of



mandatory governance practices' including a 'stronger focus on board composition, particularly the value of independent directors as part of a mix of knowledge, skills and experience, would help address the concerns identified by the Productivity Commission and APRA [in recent reports]'.

[Note: Mr Armour appears to be referencing the concerns raised by APRA in two thematic reviews released by the regulator into governance and outsourcing arrangements released earlier this year. See: Governance News [18/05/2018](#); [04/06/2018](#). The reference to concerns raised by the Productivity Commission appears to refer to the draft final report into superannuation released by the Productivity Commission on 29 May. See Governance News [04/06/2018](#).]

Mr Armour adds that both APRA reports recommended governance improvements which he said is 'a concern given the importance of superannuation funds and the compulsory nature of superannuation. It requires higher, less flexible standards of governance; standards that should be set and rigorously enforced by the regulator'.

He went on to express support for the recommendations put forward in both APRA reports and for the removal of restrictions on the ability of superannuation funds to appoint independent directors to trustee boards on the basis that in his view, it 'would enhance the ability of superannuation entities to appoint directors who have the necessary skills and experience to bring value to the board, and help address concerns – whether real or perceived – regarding "insider favours"'.

Mr Armour emphasised the role and value of independent directors commenting that 'after all, a key component of good governance is managing real and perceived conflicts of interests, and the accountability and transparency of decision-making processes. Independent directors contribute positively to the decision-making of boards, as has long been recognised in the ASX context, and should be a basic part of the governance framework of a sector so intertwined with the future prosperity of Australians'.

Mr Armour concluded that: 'We already have good options on the table from the Productivity Commission report. We have reached a point when an enhanced set of mandatory governance practices for the superannuation sector should be adopted'.

[Sources: [registration required] The AFR 31/07/2018; Australian Institute of Company Directors: 'We're all in this together, so higher standards are needed' Angus Armour FAICD, Managing Director and CEO, Australian Institute of Company Directors 01/08/2018]

**Do independent directors necessarily add value?** In an interview for the same publication, University of NSW Professor Peter Swan has taken a different view on the issue, questioning the value that independent directors bring to companies and deliver to shareholders and suggesting that the lack of independent directors on industry superannuation fund boards is a factor in their strong performance. Mr Swan's views are outlined in a separate post on the debate on raising standards of governance more generally, in this issue of Governance News. See: *Corporate governance stocktake* above.

**APRA's submission in response to the PC Draft Report into the competition and effectiveness of the superannuation sector rejects the view that current regulatory arrangements are 'confusing or opaque'.**

---

The Australian Prudential Regulation Authority (APRA) has released its submission in response to the Productivity Commission's draft report *Superannuation: Assessing Efficiency and Competitiveness* (PC draft report) (See: Governance News [04/06/2018](#)). APRA Deputy Chair Helen Rowell writes that 'APRA agrees with a number of the Commission's findings and the direction of many, but not all, of the recommendations in the Draft Report'.

Ms Rowell agreed that:

- **There is room to improve the quality of superannuation data:** Deputy Chair Helen Rowell expressed agreement with the PC that there is 'room for improvement in both the range of data that APRA collects and the quality of data that RSE licensees submit' to the regulator.
- **Room to improve industry practices:** Ms Rowell states that though industry had made substantial progress since 2012 in implementing prudential standards, progress has been 'somewhat variable with some trustees taking significant strides towards better practice while others have (in some cases considerable) room for improvement. Similarly, the quality of the outcomes being provided for members varies widely across the industry'. She added that though the regulatory framework has been improved



by recent legislative reforms, the absence of certain powers inhibits APRA's ability to take timely and proactive action. In this regard, Ms Rowell expressed support for proposed reforms (specifically: *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Bill 2017*) currently before parliament which she said would support 'the achievement of enhanced supervision outcomes, usually without needing to resort to the use of those powers.

- **Key areas for improvement:** Ms Rowell states that 'Key areas where APRA considers that improvement in industry practices is needed are strategic and business planning, assessment of outcomes for members, and the oversight and monitoring of expenditure'. She notes that proposals aimed at strengthening prudential requirements and promoting improved practices (in alignment with the PC findings) in these areas were outlined in APRA's discussion paper: *Strengthening Superannuation Member Outcomes* (see: Governance News 18/12/2018) and that these will be finalised 'over the coming months'.

## APRA's role and powers

- **Regulatory arrangements are not 'confusing or opaque':** Ms Rowell writes that 'APRA does not agree with the Commission's observation that APRA's powers to set prudential standards, and its role in MySuper authorisation, have resulted in regulatory arrangements that are confusing and opaque, with significant overlap with the Australian Securities and Investments Commission (ASIC) resulting in poor accountability and lack of strategic regulation'.
- **ASIC and APRA have distinct roles:** Ms Rowell states that APRA's role is to administer the prudential and retirement income provisions of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) and that its primary responsibility in this regard is to ensure that RSE Licensees manage their business operations to deliver quality member outcomes. By contrast, she writes, ASIC's role is to oversee specific conduct obligations applying to RSE licensees in dealing with individuals in relation to disclosure, financial product advice and complaints.
- **Commonality does not necessarily result in duplication of regulatory activity:** Ms Rowell adds 'Given the nature of these distinct but complementary responsibilities, there is a clear role for both APRA and ASIC in undertaking strategic regulation and supervision of their respective responsibilities across the superannuation industry' but that this does not 'necessarily mean there will be duplication in regulatory activity'.

[Sources: APRA submission to the Productivity Commission Draft Report – Superannuation: assessing efficiency and competitiveness 03/08/2018; Letter: APRA submission to the Productivity Commission draft report - Superannuation: assessing efficiency and competitiveness - August 2018]

**In Brief | The Superannuation Complaints Tribunal's latest newsletter has provided an update on preparations for the transition to the Australian Financial Complaints Authority (AFCA) transition, and has cautioned that it anticipates an escalation in the number of enquiries and complaints following the Financial Services Royal Commission hearings into Superannuation (commencing 6 August).**

[Source: Superannuation Complaints Tribunal Quarterly — Q2 2018]

## Other Developments

**Top Story | Final PC Report into competition in the Australian Financial System released. The report found there is a lack of competition in the sector and recommends (among other things) that the ACCC be mandated as competition champion.**

The Productivity Commission's final report into competition in the Australian financial system was publicly released on 3 August. The findings relate to the state of competition, new entrants in banking, the role of vertical integration; consumers capacity to put competitive pressure on providers; mortgage brokers and home loan markets; general insurance; financial advice; the payments system and the role of the regulators. A high level overview of the key findings and recommendations in the report is below.

### Overall Findings

- **Limited competition generally:** The report found that overall, there is limited competition in the financial sector and the 'the larger financial institutions, particularly but not only in banking, have the ability to exercise market power over their competitors and consumers'. This is attributed to: 'persistently opaque pricing; conflicted advice and remuneration arrangements; layers of public





policy and regulatory requirements that support larger incumbents; and a lack of easily accessible information, inducing unaware customers to maintain loyalty to unsuitable products'.

- **Limited ability for customers to apply competitive pressure on providers:** 'Poor advice and complex information supports persistent attachment to high margin products that boost institutional profits, with product features that may well be of no benefit'. This is attributed to the failure of 'channels for the provision of information and advice (including regulator information flow, adviser effort and broker activity)'.
- **Competition issues are not 'clearly caused' by vertical integration and 'forced separation is not a panacea':** Findings 9.1-9.2 state that the PC found no clear causal link between competition issues in either mortgage or wealth management markets that are 'clearly associated with integration' and that 'forced structural separation is not likely to provide an effective regulatory response to competition concerns in the financial system, specifically not in either home loan or wealth management markets'.
- **ACCC should act as a competition champion for the financial sector:** Recommendation 19.1 states that 'To address gaps in the regulatory architecture related to lack of effective consideration of competitive outcomes in financial markets, the ACCC should be given a mandate by the Australian Government to champion competition in the financial system, including in decisions taken by regulators that have or may have the outcome of restricting competition.'

## Key findings and recommendations


### Banking sector

Among the findings in the report were the following.

- **Price competition in the banking system is limited:** 'Although institutions claim that they compete in loan markets by discounting, such behaviour is not indicative of a competitive market when price obfuscation is common and discounts are specific to groups of customers'.  
Lack of competition in home loan markets: 'The mortgage brokers who once revitalised price competition and revolutionised product delivery have become part of the banking establishment. Fees and trail commissions have no evident link to customer best interests. Conflicts of interest created by ownership are obvious but unaddressed'.
- **The Four Pillars policy is 'redundant':** 'The Four Pillars policy is unnecessary as a means of ensuring either competitive or prudential outcomes given the strong existing laws in place'. The report adds that it 'potentially erodes competition. It also removes the potential threat of discipline by the market on the management of the four banks covered by it, undermining effective corporate governance. At best, it is a redundant policy that does not achieve its stated objectives.'
- **Trail commissions should be 'banned':** 'There is little if any evidence to substantiate the claim that trail commissions are a payment for the ongoing provision of services to borrowers. In practice, trail commissions have the effect of aligning the broker's interests with those of the lender, rather than those of the borrower'.

To address these (and other issues identified) the report makes a number of recommendations including the following.

- **To encourage new entrants into the market,** the report recommends that ASIC should expand the scope of products eligible for testing under ASIC's regulatory sandbox beyond the proposed enhanced regulatory sandbox, take a 'more hands-on approach' to approving and supporting fintechs and consider requests from existing institutions to access the sandbox on a case by case basis. In addition, an 'ongoing program of regulatory improvement in support of the sandbox' should be a 'standing item for the Commonwealth Treasury's legislative program' (recommendation 4.1).  
**Mortgage broking reforms — reform of commission structures and increased reporting requirements:** Recommendations 11.1-11.4 relate specifically to mortgage broking. They include the proposed reform of mortgage broker commission structures via an 'enforceable Code' to be created and imposed by ASIC to ban the payment of trail commissions in mortgage broking for all loans originated after the end of 2018 as well as a ban on the payment of volume based commissions,



campaign based commissions and volume based payments. It's also proposed that the ban on early exit fees be extended to explicitly prohibit commission clawbacks being passed on to borrowers. The report recommends that ASIC's powers should be expanded to allow it to enforce the ban. In addition, it's recommended that increased broker reporting that 'accords with it being the dominant home loan distribution channel' be imposed.

- **Best interest obligation for credit licensees that facilitate home loans:** Recommendation 11.4 proposes that the government should amend the National Consumer Credit Protection Act 2009 (Cth) to impose best interest obligations on licensees that provide credit or credit services in relation to home loans. These obligations should comprise: 'a duty to act in the best interest of the client; a requirement that any resulting recommendations must be appropriate to the client, having regard to the duty to act in the best interest of the client; a duty to prioritise the interests of the client, in the event of a conflict; a duty to ensure that certain information is disclosed to the client.' The report adds that 'Where the lenders have an ownership interest in firms that provide the credit assistance services, those lenders should also have a legal responsibility to ensure that the licensee discharges its best interest obligations'.
- **Principal Integrity Officer:** Recommendation 9.2 proposes that the government should legislate the appointment of a Principal Integrity Officer (PIO) in authorised deposit taking institutions (ADIs) initially, but 'with potential extension to other Australian Credit licensees and Australian Financial Service Licensees'.
  - The PIO would have 'independent status within the entity' and a 'direct reporting line to its board'. More particularly, The PIO would have a 'statutory duty to advise the entity's board on performance related to remuneration and practices that may be inconsistent with serving a customer's best interests, including breaches of commission or other remuneration benchmarks and regulations'.
  - In addition, the PIO would 'also review internal business practices as they develop over time that may be inconsistent with the entity's obligation to act in the customer's best interests'.
  - The PIO would be required to report independently to ASIC on unsatisfactory responses to its reports, 'including persistent failure of its board to observe standards supporting consumer best interest obligations'.
  - The report recommends that the PIO should 'be protected from adverse action by statute where they do so report'.
  - The report recommends that consultation on the details of the PIO, related legislative changes and penalties should be determined through a consultation process commencing by the end of 2018.

**PIO concept 'convincing'?** Commenting on this Treasurer Scott Morrison said that the recommendation 'has potentially far greater application than recommended and can work in well with the BEAR regime. These roles are effectively already being performed in banks reporting through to the Chair of Audit and Risk Committees. But as we have seen in the Laker Report into CBA, where the Board drops the ball, what happens then? I do find the Chief Pilot analogy convincing. A statutory obligation to pick up the phone direct to the regulators to an assigned senior executive within the bank with these responsibilities, spelled out in the accountability map as part of the BEAR, is a very worthy idea'. He added that 'as with all the recommendations in the PC report we will look carefully at them, consult, and consider our response in concert with any further matters coming forward, in particular from the Royal Commission. And I note this report had already been shared with Royal Commission'.

- **Interest rate transparency for home loans – ASIC online report:** Recommendation 12.1 proposes that ASIC should collect data from mortgage lenders (ADIs only) on interest rates of new residential home loans and develop an 'online calculator that reports, with an elapsed time of no more than 6 weeks, median interest rates for loans issued according to different combinations of loan and borrower characteristics. The underlying data should be published in a way that is accessible to third parties such as web application developers. At a minimum, data should be published in a machine readable format'.

- **Borrowers should be offered more choice for lenders mortgage insurance:** Recommendation 13.2 proposes that ASIC should require all lenders to provide borrowers that are levied with lenders mortgage insurance with the option of being levied once at the commencement of their home loan or being levied annually over the first six years of their loan with transparency around the comparison of these options.
- **Data Access:** The report recommends that the Open Banking System should be implemented 'in a manner that enables the full suite of rights for consumers to access and use digital data' (recommendation 5.1).

## Financial Advice

In relation to financial advice, the report made a number of findings including the following.

- **Enabling financial advisers to provide personal advice on home loans would increase competition:** The report suggests that allowing financial advisers to compete with mortgage brokers in offering personal advice on home loans would expand the sources of competition in home loan distribution as well as provide more holistic personal financial advice services to consumers. But notes that 'more work is required before this could become a reality'.
- **The term 'general advice' is problematic:** Commenting on 'General advice' the report found that 'some consumers unduly rely on general advice, and in particular, sales and marketing material'.
- **More transparency is needed around use of approved product lists (APLs):** The report found that 'Better information is needed on how financial advisers make product recommendations through the use of approved product lists. Australian Financial Service Licensees should disclose a range of data indicators to assist ASIC enforce the standard of conduct required of financial advisers. The Commission recommends annual public reporting of this information'. The report makes a number of recommendations to address these concerns. These include the following.
  - **Creation of a new Australian Financial Services Licence:** The report recommends that ASIC should assess the feasibility of financial advisers providing advice on home loans and other credit products, via a new Australian Financial Services Licence that would not require a separate Australian Credit Licence to be obtained. This assessment should examine the costs and benefits of a new licence, the consequences of various remuneration models and the applicability of a Principal Integrity Officer (recommendation 10.1).
  - **'General advice' should be renamed and a new term should be in effect by mid-2020:** The report states that general advice, as defined in the Corporations Act 2001 (Cth), is a 'misleading term and should be renamed'. The report adds that 'Any replacement must ensure that the term "advice" can only be used in association with "personal advice" — that is, advice that takes into consideration personal circumstances'. The report recommends that consumer testing of alternative terminology should be undertaken to 'ensure that misinterpretation and excessive reliance on this type of information is minimised'. The report states that 'Including time for consumer testing and a transition period to enable industry training and adjustment, a new term should be in effect by mid-2020' (recommendation 10.2).
  - **ASIC to publish approved product lists and conduct audits:** The report recommends that Australian Financial Service Licensees should disclose to ASIC (for each broad class of financial product): the number of products on their approved product list (APL); the proportion of in-house products on their APL; the proportion of products recommended that are in-house the proportion of products recommended that are off-APL and ASIC should publish this information annually. ASIC should also conduct selected audits of the information received to facilitate assessment of the effectiveness of advisers in meeting clients' best interests (recommendation 10.3).

## Regulators

The report found that the lack of an advocate for competition is a 'mistake' and APRA is 'not well placed to consider competition effects'.

The report adds that: 'Given the size and importance of Australia's financial system, and the increasing



emphasis on stability since the global financial crisis, the lack of an advocate for competition when financial system regulatory interventions are being determined is a mistake that should now be corrected’.

Among the recommendations to address this and other concerns in the report are the following.

- **ACCC should act as a competition champion for the financial sector:** Recommendation 19.1 states that ‘To address gaps in the regulatory architecture related to lack of effective consideration of competitive outcomes in financial markets, the ACCC should be given a mandate by the Australian Government to champion competition in the financial system, including in decisions taken by regulators that have or may have the outcome of restricting competition. To minimise cost and disruption, this role should be implemented in substantial part through the Council of Financial Regulators (CFR) by making the ACCC a permanent member of the CFR’. The report adds that ‘there should be no change under this recommendation to the current legislated responsibilities of the regulators. Rather, the Australian Government should include in its Statement of Expectations for each of the financial regulator members of the CFR that the ACCC should be given the opportunity as a member of the CFR to advise the Council on regulator actions that may have material effects on competition, before they are implemented’.
- **Statements of expectations for regulators:** Recommendation 18.1 proposes that statements of expectations for regulators should be published as a matter of priority and regulators should publish Statements of Intent within three months of receiving the Statements of Expectations. In their annual reports, the financial regulators should provide information on the actions they have taken in line with their Statements of Intent and outcomes on performance measures.
- **Transparency of regulatory decision making:** Recommendation 19.2 states that the CFR should apply the ‘ACCC analysis in a discussion amongst members on interventions that may have a material impact on competition in a product market. The ACCC assessment of competition impacts should be published in a simple form and timely manner as part of a new commitment to publish Minutes of CFR meetings’.
- **ACCC should regularly review the effect of vertical and horizontal integration:** Though the report found no clear causal link between integration and competition issues in the mortgage or wealth management markets and does not recommend ‘structural separation’, the report does recommend that the ‘ACCC should undertake 5-yearly market studies on the effect of vertical and horizontal integration on competition in the financial system. The first of these studies should commence in 2019 and include establishing a robust evidence base of integration activity in the financial system’ (recommendation 9.1).
- **Publication of ASIC data:** The report states that the financial regulators ‘already collect large amounts of data, which is a valuable public resource. Subject to privacy requirements, much more such data should be made publicly available. As a first step towards improving the availability of data, ASIC should publish a list of the datasets collected and used in its research projects and reports and release any non-sensitive datasets’ (recommendation 18.2).
- **APRA should conduct post-implementation evaluations of its material interventions:** The report recommends that APRA should conduct and publish annually quantitative post-implementation evaluations of its material prudential interventions, including costs and benefits to market participants and the effects on competition (recommendation 19.3). The report specifically recommends that APRA should conduct a post-implementation review on how the changes in Prudential Standard APS 120 have affected the costs of funds and competitiveness of non-authorized (smaller) deposit-taking institutions (recommendation 8.1). In addition, the report recommends that instead of applying a single risk weight to all small and medium business lending not secured by a residence, APRA should provide for a broader schedule of risk weights in its Australian Prudential Standard (APS 112) (recommendation 16.1).

## General insurance

The report found that there was a lack of competition in general insurance/lack of transparent consumer information. The PC writes that ‘General insurance markets are concentrated’ and ‘there is a proliferation of brands but far fewer actual insurers, poor quality information provided to consumers, and sharp practices



adopted by some sellers of add-on insurance products. A Treasury working group should examine the introduction of a deferred sales model to all sales of add-on insurance'.


To address this, the report makes a number of recommendations including the following.

- **Clearer disclosure:**
  - The report recommends that renewal notices for general insurance products should transparently include the previous year's premium and the percentage change to the new premium. This policy should commence by the end of 2019 and be enforced by ASIC (recommendation 14.1).
  - In addition to specifying which insurer underwrites their products, each insurance brand should specify on their website any other brands that are underwritten by the same insurer, for that particular form of insurance. Insurers should provide an up-to-date list of the brands they underwrite to ASIC. ASIC should transparently publish this information as a list on its website (Recommendation 14.2).
- **State and territory taxes and levies on general insurance should be phased out** consistent with the Productivity Commission's 2014 Natural Disaster Funding Inquiry (recommendation 14.3).
- **ASIC should proceed as soon as possible with its proposal to mandate a deferred sales model** for all sales of add on insurance by car dealerships. The deferral period should be a minimum of 7 days from when the consumer applies for or purchases the primary product. Following implementation, the Australian Government should establish a Treasury-led working group with the objective of comprehensively extending the deferred sales model to all other add on insurance products, with the model set in legislation and ASIC empowered to offer exceptions on a case-by-case basis (Recommendation 15.1).
- **Removal of the NCCP exemption?** The Treasury should complete its 2013 review into the current exemption of retailers from the *National Consumer Credit Protection Act 2009* (Cth), with a view to removing or reforming the exemption. The report should be made publicly available on completion (recommendation 15.2).

## Payments System

- **The Payments System Board should introduce a ban on card payment interchange fees** by the end of 2019. Any other fees should be made transparent and published. (Recommendation 17.1)
- **Review of current interchange fee regulation:** The ACCC, with input from the Payments System Board, should investigate: whether current or recommended interchange fee regulation favours three party card schemes. This investigation should be completed by no later than mid-2019. (Recommendation 17.2)
- **Choice of default network:** The Payments System Board should set a regulatory standard that gives merchants the ability to choose the default network to route transactions for dual network cards. The report adds that as the technology is readily available, this reform should be in force by 1 January 2019 at the latest. (Recommendation 17.3).
- **ePayments Code made mandatory:** The Australian Government should give ASIC the power, by end 2018, to make the ePayments Code mandatory for any organisation that sends or receives electronic payments (recommendation 17.6) ASIC should review the ePayments Code and update it to reflect changes in technology, innovative business models and developments in Open Banking. ASIC should more clearly define the liability provisions for unauthorised transactions when third parties are involved, including participation in financial dispute resolution schemes. ASIC should update the ePayments Code by end 2019 and commit to 3 yearly reviews.
- **Review of PPFs:** The Council of Financial Regulators should review the current regulation of Purchased Payment Facilities (PPFs). The review should develop an approach to simplify the regime, develop clear thresholds for regulatory responsibility and reduce barriers to growth in this sector. The review should consult on and design a tiered regulatory structure for PPFs, including one





tier that does not attract prudential regulation. The review should be completed by end 2018 at the latest and provide a path forward for regulators by mid-2019 (recommendation 17.5).

- **Access regime for the new payments platform (NPP)/improved functionality of the NPP:** Recommendations 17.7 and 17.8 relate to the new payments platform. Recommendation 17.7 recommends that the platform should be subject to an access regime imposed by the Payments System Board. Recommendation 17.8 recommends that the ACCC in consultation with the Payments System Board should investigate ways to improve the functionality of the NPP to promote competition within the NPP and across the payments system more broadly. The investigation should be completed by mid 2019, with a view to implementing additional functionality by end 2019.

[Sources: Productivity Commission media release 03/08/2018; Overview — Competition in the Australian Financial System; Competition in the Australian Financial System — Inquiry Report; [registration required] The SMH 03/08/2018; Treasurer Scott Morrison speech to the Australian British Chamber of Commerce: 'Consumer powered competition in our banking sector' 03/08/2018]

## Top Story | ASIC has approved the Australian Banking Association's (ABA's) new Banking Code of Practice (the Code).

---

The Australian Securities and Investments Commission approved the Australian Banking Association's (ABA's) new Banking Code of Practice (the Code) on 31 July. The revised Code applies to all consumers and to small businesses borrowing up to \$3m and replaces the previous version, *The Code of Banking Practice 2013*. The Code will commence operation from 1 July 2019.


### Key Points

- **New Code is mandatory for ABA members:** It is a condition of ABA membership that member banks with a retail presence in Australia are required to sign up to the Code (formally, the signing onto the Code was voluntary). The Code will be administered and enforced by an independent monitoring body, the Banking Code Compliance Committee (BCCC) and consumers and small businesses with disputes about the Code protections will be able to have those disputes heard by the new Australian Financial Complaints Authority.
- **Definition of small business:** The \$3 million limit for small business is lower than the \$5 million than ASBFEO, the independent reviewer of the Code (Philip Khoury) and ASIC had previously argued for (see: Governance News [08/06/2018](#)). However, ASIC said in a statement announcing its approval of the Code that it would cover 92-97% of Australian business borrowers.
- **Review of the definition of small business within 18 months/ASIC approval may be reviewed in light of any findings from the Royal Commission:** ASIC's approval is conditional upon an independent review of the operation of the new Code (focusing on the adequacy of the Code's definition of small business and investigate the Code's small business coverage in practice) within 18 months of its commencement. In addition, a comprehensive review of the Code is scheduled for three years after commencement. ASIC has also noted that it may review its approval of the Code in light of any findings made by the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

### Other changes

Among the changes highlighted by ASIC as significant are the following.

- **Extension of protection against unfair contract terms to businesses who borrow up to \$3m:** ASIC states that the 'new Code provides for improved protections for small business borrowers and expands the reach and impact of legal protections against unfair contract terms'. More particularly, for small businesses that borrow up to \$3 million, the Code provides that lending contracts should not contain a range of potentially unfair and one-sided terms. ASIC comments that 'at its current setting of applying to small businesses who borrow up to \$3 million, the Code will cover the considerable majority – between 92-97% – of businesses in Australia'.
- **Expanded protections for consumers** include: provisions for inclusive and accessible banking, including for vulnerable customers (and training for staff to assist); protections relating to the sale of consumer credit insurance including a deferred sales period of four days for CCI for credit cards and personal loans sold in branches and over the phone; protections for guarantors of loans (eg giving prospective guarantors generally a three day cooling off period and requiring banks to only enforce a



guarantee once they have taken action against the borrower); rules requiring credit card customers to receive reminders about balance transfer promotional periods ending, as well as more consistent treatment about how repayments are applied; and enhanced processes for assisting customers in financial difficulty and processes for resolving complaints.

- **Review of the definition of small business within 18 months:** In addition to the independent review of the Code within 18 months, and the review of the Code 3 years after commencement ASIC states that it will collect quarterly data from banks and the Australian Financial Complaints Authority to monitor the extent of the Code's coverage of small business. This information will be made public every six months and provide 'ongoing transparency about the coverage of the Code' ASIC writes.

Commenting on the approval of the Code Australian Banking Association CEO Anna Bligh said: ' It represents a stronger commitment to ethical behaviour, responsible lending, greater financial protection and increased transparency...Customers will see real tangible benefits, including more information about changes to their accounts, delay in offering on add-on insurance products and simpler contracts, with fewer conditions for small business loans...For the first time there is a new dedicated section on small business lending and another on inclusive and accessible banking. In addition, when required, a small business and or agribusiness expert, will be asked to assist the independent Banking Code Compliance Committee, which is responsible for monitoring Code compliance'. Ms Bligh added that though signatory banks have until July 2019 to implement the Code, some are expected to be compliant earlier.

### Initial response

- **Treasurer Scott Morrison welcomed the revised code as** 'a significant step the banks are taking to alter their behaviour'. In particular, Mr Morrison highlighted changes to sales of add-on insurance being (deferred for at least four days when a customer applies for a credit card or loan) the requirement for banks to provide customers a list of direct debits and recurring payments, the extension of the code to small businesses, changes to non-monetary default clauses as examples of 'tangible' benefits for customers. Mr Morrison added that 'It is encouraging that the banks are starting to listen to the public and are looking to lift their game when it comes to how they behave and treat their customers....While they [the banks] have a long way to go, the new code is a step in the right direction'
- **The Australian Small Business and Family Enterprise Ombudsman, Kate Carnell** issued a statement welcoming the ABA Banking Code of Practice but expressing disappointment that 'the cap for small business loans was set at a total loan facility of \$3 million, as we had recommended a credit facility of at least \$5 million which would encompass capital intensive small businesses such as farms, building and manufacturing'. Ms Carnell also welcomed the fact that ASIC will monitor the extent of the Code's coverage of small business and publish data every six months adding that 'We will be keeping a close eye on those figures, with particular focus on industries we think require a higher lending cap, and also on ASIC's work on the review of the small business definition.'
- **CBA CEO Matt Comyn** issued a statement welcoming the Code as 'another positive step by the industry to listen to our customers and undertake genuine change'. Mr Comyn added that the Code 'has the full support of everyone at Commonwealth Bank and it represents one of the steps we are taking to be a better bank for our customers and to build community trust'.
- **NAB CEO Andrew Thorburn** said: 'The Code raises the bar that banks must meet every day for our customers to deliver the service they can and should expect...We will prioritise implementing the Code as quickly as possible as part of our determination to be better.'
- **Westpac CEO Brian Hartzler** is quoted by The SMH as welcoming the approval, saying the industry had worked with the regulator to 'completely rewrite' the industry's commitments to customers. 'Westpac fully supports the new banking code which is one part of how we are strengthening transparency and relationships with our customers' Mr Hartzler reportedly said.
- **ANZ chief executive Shayne Elliott** reportedly said via Twitter the bank would implement the code ahead of schedule.
- **Bank of Queensland CEO Jon Sutton** is quoted in The SMH as stating that the Code means that the community can 'look forward to a more customer-focused and sustainable banking industry'.



The New Daily and The Conversation have both separately queried whether self-regulation via The Code is likely to address/be effective in addressing the sorts of issues uncovered by the Financial Services Royal Commission.

[Note: Self-regulation of the SME lending sector is one of the issues that has emerged during the Financial Services Royal Commission Round 3 hearings. Among other things, comment was invited on whether the (then proposed) Code is 'adequate to address any residual concerns about the coverage of obligations imposed on the banks'. See: Governance News [28/05/2018](#); [08/06/2018](#).]

[Sources: 18-223MR ASIC approves the Banking Code of Practice; ABA media release 31/07/2018; Australian Banking Association Banking Code of Practice 2018; [registration required] The Australian 31/07/2018; 01/08/2018; CBA media release 31/07/2018; NAB media release 31/07/2018; [registration required] The SMH 31/07/2018; Australian Small Business and Family Enterprise Ombudsman media release 01/08/2018; [registration required] The AFR 02/08/2018; The Conversation 02/08/2018; The New Daily 31/07/2018; Treasurer Scott Morrison speech to the Australian British Chamber of Commerce: 'Consumer powered competition in our banking sector' 03/08/2018]

## **United States | Wells Fargo has agreed to Pay a \$2.09bn penalty for allegedly misrepresenting the quality of loans used in residential mortgage-backed securities.**

---

The US Department of Justice (DOJ) has announced that Wells Fargo Bank and several of its affiliates (Wells Fargo) will pay a civil penalty of \$2.09bn under the *Financial Institutions Reform, Recovery, and Enforcement Act of 1989* (FIRREA) in connection with the bank's alleged origination and sale of residential mortgage loans that it knew to contain misstated income information and which it allegedly knew did not meet the quality that Wells Fargo represented.

The DOJ notes that the allegations resolved by the settlement 'are allegations only, and there has been no admission of liability'.

**Allegations:** The DOJ alleged that:

- In 2005, Wells Fargo began an initiative to double its production of subprime and Alt-A loans. As part of that initiative, Wells Fargo loosened its requirements for originating stated income loans – loans where a borrower simply states his or her income without providing any supporting income documentation.
- To evaluate the integrity of its increasing volume of stated income loans, Wells Fargo subjected a sample of these loans to testing. This testing revealed that more than 70% of the loans that Wells Fargo sampled had an 'unacceptable' variance (greater than 20% discrepancy between the borrower's stated income and the income information reflected in the borrower's most recent tax returns filed with the IRS), and the average variance was approximately 65%. After receiving these results further internal testing was conducted determine if 'plausible' explanations existed for the 'unacceptable' variances over 20%. This additional step allegedly revealed that nearly half of the stated income loans that Wells Fargo tested had both an unacceptable variance and the absence of a plausible explanation for that variance.
- The DOJ alleges that Wells Fargo reported to investors false debt-to-income ratios in connection with the loans it sold and failed to disclose the results of the testing. Wells Fargo also allegedly heralded its fraud controls while failing to disclose the income discrepancies its controls had identified.
- The DOJ also alleged that Wells Fargo took steps to insulate itself from the risks of its stated income loans, by screening out many of these loans from its own loan portfolio held for investment and by limiting its liability to third parties for the accuracy of its stated income loans. Wells Fargo sold at least 73,539 stated income loans that were included in RMBS between 2005 to 2007, and nearly half of those loans have defaulted, resulting in billions of dollars in losses to investors.
- According to the DOJ investors, including federally insured financial institutions, suffered billions of dollars in losses from investing in residential mortgage-backed securities (RMBS) containing loans originated by Wells Fargo.

Acting Associate Attorney General Jesse Panuccio commented: 'This settlement holds Wells Fargo accountable for actions that contributed to the financial crisis'.



Acting US Attorney for the Northern District of California, Alex G Tse said: 'Abuses in the mortgage-backed securities industry led to a financial crisis that devastated millions of Americans... Today's agreement holds Wells Fargo responsible for originating and selling tens of thousands of loans that were packaged into securities and subsequently defaulted. Our office is steadfast in pursuing those who engage in wrongful conduct that hurts the public.'

Commenting on the settlement, The AFR writes the settlement of the Wells Fargo investigation may 'ultimately mark the Justice Department's last multibillion-dollar penalty against a US company for creating or selling crisis-era mortgages' but notes that US investigations into other banks' lending practices before the global financial crisis are ongoing eg UBS and HSBC are 'yet to resolve significant probes'.

*[Sources: US Department of Justice media release 01/08/2018; Settlement Agreement; [registration required] The AFR 02/08/2018]*

---

**An Australian Yukom? The age reports that ASIC has succeeded in securing freezing orders over nearly \$18m in investor money after alleging AGM Markets, OT Markets and Ozfin ran an unlicensed business that allegedly employed high pressure sales techniques to 'lure' investors to deposit funds on the promise of bonus payments.**

---

ASIC has reportedly been granted freezing orders over nearly \$18m of investor money held in accounts linked to Australian company AGM Markets after alleging AGM Markets, OT Markets and Ozfin deployed high-pressure sales techniques including luring investors to deposit tens of thousands of dollars on the promise of bonus payments.

According to The Age, ASIC alleges AGM Markets, OT Markets and Ozfin ran an unlicensed business selling exotic products to inexperienced, and sometimes unemployed, Australians through the websites Alphatrade and Trade Financial and is seeking to have the three businesses wound up. ASIC also reportedly alleges investors have had difficulty withdrawing their funds when they wanted to stop using the investment platforms of the websites, according to the judgment.

The Age comments that the tactics used appear to be similar to those of Israeli online trading group Yukom Communication. Yukom CEO Lee Elbaz is reportedly facing up to 40 years imprisonment for alleged fraud following an FBI investigation.

*[Source: [registration required] The Age 30/07/2018]*

---

**APRA has released its annual Private Health Insurance annual coverage survey for December 2017: Overall there were decreases in hospital treatment membership across younger age groups and increases across older age groups in the year to December 2017.**

---

The Australian Prudential Regulation Authority (APRA) has released its annual Private Health Insurance annual coverage survey for December 2017. The survey provides a snapshot at December each year of the number of people, by age, gender and state of residence, with hospital insurance.

- Overall there were decreases in hospital treatment membership across younger age groups and increases across older age groups in the year to December 2017.
- The largest decline over 2017 was in the age group 25 to 29 (down 5.3%), while the largest increase was in the age group 90 to 94 (up 8.2%).
- The 25 to 29 age group recorded the largest decline in insured persons over the year (down 27,536 people), while the 70 to 74 age group experienced the largest increase in insured persons (up 36,282 people).

The Australian comments that the figures represent the first annual fall in the number of Australians with private hospital cover since 2003 and attributes this to the above-inflation annual increases in the cost of private health insurance.

*[Sources: APRA media release 30/07/2018; Private Health Insurance Annual Coverage Survey December 2017 (released July 2018); [registration required] The Australian 31/07/2018]*



**In Brief | A clear drop in client trust? The 'clear trust deficit' between clients and the financial services sector is worsening, according to joint research from Deloitte Digital and Salesforce. According to the report, only 1 in 3 customers believe that the financial services industry can be trusted. This is attributed to a number of factors including: the Financial Services Royal Commission exposing significant failures of providers, rising customer expectations, technological advancements and new competition.**

[Sources: Accountants Daily 31/07/2018; Deloitte media release; [registration required] Restoring Trust in Financial Services in the Digital Era]

**In Brief | Is ASIC's push for the removal of grandfathered commissions an overreaction? Reportedly, Association of Financial Advisers (AFA) head of policy, Phil Andersen has questioned the factual basis for ASIC's argument for the removal of grandfathered commissions on the basis that in his assessment, they constitute little of the overall income of financial advice practices.**

[Source: Financial Standard 26/07/2018]

## Accounting and Audit

**In Brief | Is ASIC's tough stance on auditing firms leading to a 'tick the box' culture? Academics suggest that ASIC's enforcement style has shifted from being more collaborative to being more coercive and in response, firms are adapting their audit process in ways aimed at minimising inspection risk and not necessarily at improving audit quality. 'There is an accusation by the auditors – which ASIC denies – that it is almost as if the regulator needs to keep finding something wrong every month or every year' Professor Moroney is quoted as stating.**

[Sources: [registration required] The AFR 29/07/2018; Monash Business School Insight newsletter 04/07/2018; [registration required] Dowling, C. , Knechel, W. R. and Moroney, R. (2018), Public Oversight of Audit Firms: The Slippery Slope of Enforcing Regulation. Abacus at Wiley Online:10.1111/abac.12130]

**In Brief | The UK FRC has announced the closure of its investigation into Grant Thornton UK's audits of Globo Plc. The investigation commenced in December 2015 one month after the company had gone into administration and focused on GTUK's group audit (specifically, its direction, supervision and performance of the group audit engagement). The FRC writes that following consideration; Executive Counsel concluded that 'there was no realistic prospect of a finding of Misconduct' and that the matter would be closed without further action.**

[Source: FRC media release 30/07/2018]

## Risk Management

### Supply Chain Risk

**Second only to homicide in terms of the cost to UK society? The UK government has commissioned an independent review of the *Modern Slavery Act 2015* after the release of a report into the social and economic cost.**

The UK government has commissioned an independent review of the *Modern Slavery Act 2015* following the release of a report into the economic and social costs of the issue. The report estimated that it costs the UK up to £4.3bn a year making modern slavery second only to homicide in terms of its cost to British society. The review aims to strengthen the UK's ongoing response and accelerate progress from Government and businesses in eradicating the problem.

Reuters writes that critics have said that the law lacks teeth and as such has been ineffective in requiring businesses to address the issue with many companies (up to 50%) yet to report as required.

[Sources: Home Office media release 30/07/2018; The Economic and social costs of modern slavery: research report; Reuters 30/07/2018]





## Cybersecurity

### Notifiable data breaches update | Cyber attacks are the largest source of data breaches, and the health sector reported the largest number of breaches, according to the latest OAIC report.

---

The Office of the Australian Information Commissioner (OAIC) has released a report on notifications received under the Notifiable Data Breaches (NDB) scheme between 1 April and 30 June 2018.

#### Key Points

- **OAIC received 242 notifications in the first full quarter** of the NDB scheme's operation.
- **Most data breaches (61%) in the period involved the personal information of 100 individuals or fewer.** Data breaches impacting between 1 and 10 individuals comprised 38% of the notifications.
- **The majority of data breaches involved 'contact information'**, such as an individual's home address, phone number or email address.
- **Malicious or criminal attacks accounted for 59%** of data breaches for the period. The largest source of attacks was cyber incidents (97 notifications) such as phishing (29%), malware, ransomware, brute-force attack (14%), or by unknown methods (34 per cent). Theft of paperwork or storage devices was a significant source of malicious or criminal attacks. Other sources included social engineering or impersonation (7 notifications) and actions taken by a rogue employee or insider threat (7 notifications).
- **Human error accounted for 36% of breaches** (the second largest source of data breaches after malicious or criminal attacks). OAIC comments that many cyber incidents appear to have exploited vulnerabilities involving a human factor with examples including sending personal information to the wrong recipient via email (22 notifications), mail (10 notifications) or in other ways (8 notifications), and unintended release or publication of personal information (12 notifications).
- **Human error data breaches involving the loss of storage devices impacted the largest numbers of people** (an average of 1199 affected individuals per breach). Failures to use the 'blind carbon copy' (BCC) function when sending group emails impacted an average of 571 affected individuals per data breach. By contrast, human errors involving sending personal information to the wrong recipient generally impacted small groups or single individuals.
- **System faults accounted for 5% of data breaches.**
- **The largest source of reported data breaches was the private health service provider sector (health sector) (20% or 49 notifications).** Of those notifications, 59 per cent of reportable data breaches resulted from human error (29 notifications).
- **The second largest source was the finance sector (15%).** Of those notifications, 50% of reportable data breaches resulted from human error (36 notifications).
- **The third largest source was the legal, accounting and management services sector (8%),** followed by the private education sector (8%), and the business and professional associations sector (6%). Legal, accounting and management and business and professional associations notified the majority of breaches resulting from malicious or criminal attacks.

[Note: The first quarterly statistics report, released six weeks after the commencement of the scheme reported there were 63 breach notifications during that period, health service providers were the largest source of breaches (24% of reported breaches) and contact information was the most common form of personal information involved in breaches. The first report also found that the majority of breaches were caused by human error. See: Governance News [16/04/2018](#)]

Commenting on the report findings, IT News writes that the health numbers are going to be particularly 'well watched' as privacy and data security concerns 'engulf' the implementation of My Health Record.

The SMH reports that Acting Privacy Commissioner Angelene Falk has raised concerns about the My Health Record system, and has raised them discussions with Health Minister Greg Hunt and the Australian Digital Health Agency, which administers the system. 'Australians rightly are asking questions around the security



and privacy of that information and this is a very important opportunity for there to be that debate and certainly I welcome it' Ms Falk said. The commissioner added that it was her 'expectation that' security requirements for the My Health Record System would 'continue to be reviewed and enhanced, as they should be'.

*[Sources: Office of the Australian Information Commissioner: Notifiable Data breaches Quarterly Statistics Report 1 April — 30 June 2018; ITNews 31/07/2018; [registration required] The SMH 31/07/2018; The ABC 01/08/2018]*

## **The case for 'algorithmic accountability': Is publishing the algorithms behind AI applications a solution for all forms and uses of AI?**

---

Noting the risks associated with the use algorithms when rolled out on a large scale (eg use of flawed facial recognition technology), The FT queries whether following France's lead on addressing 'bias'/flawed assumptions underpinning algorithms should be considered.

In France, the administration of Emmanuel Macron has reportedly announced that all algorithms developed for government use will be made publicly available with the aim of ensuring that society at large can verify their correct application. The FT suggests that while the 'radical openness' promoted by France might be a 'bridge too far for algorithmic accountability, the case for independent auditing of algorithms is clear' and should be considered in setting up an AI strategy for Europe. 'It is one thing to be surprised by an algorithm coming up with a novel solution to a theoretical problem. It is quite another to be surprised when an algorithm inadvertently destroys someone's life through bad decision-making' The FT argues.

*[Source: [registration required] The FT 30/07/2018]*

## **Whistleblowing**

**In Brief | The US Commodity Futures Trading Commission (CFTC) has announced multiple whistleblower awards totaling more than \$45 million. CFTC Director of the Division of Enforcement said that the awards demonstrate the growing success of the CFTC's Whistleblower Program, in particular the increasing volume and complexity of incoming whistleblower submissions and added that he expects 'this trend to continue as the Commission continues to receive increasing numbers of high-quality whistleblower tips'.**

---

*[Source: US CFTC media release 02/08/2018]*

## **Other Developments**

**#Metoo allegations against CBS Chair and CEO and more general allegations against the company have reportedly led to an immediate share price drop?**

---

Following the publication of allegations of sexual misconduct against the CBS CEO and Chair Lesley Moonves last week, and allegations more generally that the culture at the company is 'toxic' toward women, the CBS board have reportedly started an independent investigation into Mr Moonves' conduct. Mr Moonves has not been suspended, and has not elected to stand aside, pending the outcome (for which both the CBS board and Mr Moonves are facing criticism media reports suggest).

Separately, several women at CBS have reportedly come to Mr Moonves' defense stating that the allegations do not seem to reflect the man they knew.

Reportedly, the company's share price has fell 10% in the wake of the reports.

Media reports have also noted that the allegations have emerged at a time when CBS (and more particularly Les Moonves as CEO/Chair) are engaged in a battle with its former parent company Viacom. Shari Redstone, (daughter of Sumner Redstone, who still owns the majority of both companies), reportedly wants to reunite the businesses, but Mr Moonves reportedly is opposed.

*[Sources: The New Yorker August 6 & 13, 2018 Issue; The Los Angeles Times 30/07/2018; [registration required] The FT 31/07/2018; [registration required] The WSJ 29/07/2018; Fortune 27/07/2018]*

## **Other News**

---



**Progress update on constitutional recognition for Indigenous Australians | The Joint Select Committee on Constitutional Recognition Relation to Aboriginal and Torres Strait Islander Peoples has released its interim report and called for submissions on the proposed models and principles put forward. Submissions close 17 September.**

---

The Joint Select Committee on Constitutional Recognition Relation to Aboriginal and Torres Strait Islander Peoples released its interim report on 30 July 2018.

The report centres on the proposal for a First Nations Voice (ie considers evidence in relation to the constitutionality, structure, function, and establishment of The Voice) and examines past and existing advisory bodies and new proposals that might inform the design of The Voice.

The report also considers other proposals for constitutional change and proposals for truth-telling and agreement making.

The Committee is seeking additional submissions examining the principles and models outlined in the interim report by 17 September 2018. The final report is due to be delivered by 29 November 2018.

*[Sources: Joint Select Committee on Constitutional Recognition relating to Aboriginal and Torres Strait Islander Peoples media release 30/07/2018; Interim Report 30/07/2018]*