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Executives, Secretaries and Officers

Key concerns for business leaders? The top three priorities for Australia's business leaders are digital transformation, innovation and disruption and regulation according to a new KPMG survey

KPMG's research practice, KPMG Acuity, sourced and analysed responses from 220 of Australia's senior leaders to identify the top issues facing Australian businesses in 2019.

Top ten priorities

1. Digital transformation	2. Innovation and disruption	3. Regulation	4. Political paralysis	5. Customer centricity
6. Cost competitivenes s	7. Public trust	8. Cybersecurity and data privacy	9. Big data	10. Infrastructure and liveable cities

Issues not identified as top priorities:

- Energy; government efficiencies; climate change; health, aged care and disability; education and the changing nature of work; and fiscal sustainability were not identified as top priorities.
- Other issues ranked outside the top ten included: trade and protectionism; tax reform; social cohesion and inequality; affordable housing; defence and security; and Indigenous engagement.

Commenting on the findings, KPMG Acuity partner Amanda Hicks said: 'The results highlight the increasingly tough agendas that CEOs are facing. They see a mandate for digital transformation, innovation, and changing their business models to better meet increasing customer needs and expectations – that is, to become more nimble and responsive; at the same time, they recognise this needs to be done in a period of potentially increasing regulation, political uncertainty, and with continued cost pressures. It can be seen as a difficult balancing act.'

The ABC suggests that the findings indicate that pressure to keep up with competitors rather than other risks (eg the federal election, the financial services royal commission's recommendations) is a key concern for business leaders.

The Australian comments that the fact that trust was identified in the top ten priorities echoes the recent focus on the issue at the Financial Services Royal Commission. The same article also quotes KPMG Chair Alison Kitchen as flagging this issue as a key theme to emerge from the survey.

About the survey: KPMG Acuity, engaged a 'broad spectrum' of 220 C-level leaders from a diversity of industries and a diversity of companies ranging from companies with fewer than 50 employees to companies with revenues of over $1bn. The Majority of respondents were drawn from the private sector.

[Sources: KPMG media release 05/12/2018; KPMG report: Keeping us up at night: the big issues facing business leaders in 2019; The ABC 05/12/2018; [registration required] The Australian 04/12/2018]

Diversity

France, Italy and Germany lead the way on gender board representation in Europe according to EWOB gender diversity index

European Women on Boards (EWOB) has released a gender diversity index which assesses gender representation at the 200 largest European listed companies in nine nations (Belgium, the Czech Republic, Finland, France, Germany, Italy, the Netherlands, Spain, and the UK). The purpose is to identify best practice.

According to the index:

- France leads the way on diversity with women making up, on average, 44.2% of boards
- Italy was ranked next with women making up 36.5% of boards (on average), and Germany was the next with 33.7%.
- The UK was ranked 7th (of the nine countries) with women making up 29.9% of boards on average.

In addition to singling out nations' overall progress on gender diversity, the report highlights 'award winning' companies:

- Kering (France), the parent of brands such as Gucci and Alexander McQueen, received the Board Gender Diversity Prize, with women making up 60% of its directors.
- Sodexo (France) won the Woman Chair Price 2018 (with the highest board diversity at 53.8% among firms with a female Chair).
- GlaxoSmithKline (UK) rece3obed the Women CEO Prize 2018 (with the highest board diversity at 45.5% among companies with a woman CEO).

The index notes that the top three countries in terms of gender diversity have all put in place quotas requiring certain levels of gender diversity on boards.

[Source: EWOB Ethics and Boards European Gender Diversity Index 2018 factsheet; European Women on Boards data and ranking: Ethics and Boards European Diversity Index 2018; European Women on Boards media release; [registration required] The FT 29/11/2018]

Meetings and Proxy Advisers

Board (gender) Diversity appears less important to shareholders than anticipated? No second 'strike' and no strong protest vote against the re-election of two male directors to the all-male five member board (despite media speculation to the contrary) at the TPG AGM

The TPG Telecom Ltd AGM was held on 5 December. Despite media speculation, and reports that proxy advisers planned to lodge protest votes against the reelection of the two male directors to the all-male board, the two directors were re-elected with 87.94% and 85.03% of votes in favour.

The AFR reports that Chair, David Teoh faced a number of questions in the meeting concerning the lack of diversity on the board, including from the Australian Shareholders Association. Mr Teoh reportedly said that appointing a female director to the board would be a 'priority' and that the proposed merger between TPG and Vodafone would afford an opportunity to do so. 'I have interviewed some candidates for the director post for the merged co[mpany]. And everyone I interview is a woman. So to answer your question, we put priority on that' he is quoted as stating.

The remuneration report was also approved by shareholders with over 93% support (after a first 'strike' last year). The Australian attributes this to shareholders giving the TPG board 'the benefit of the doubt' as they await the outcome of the ACCC's verdict on the proposed merger of TPG with Vodafone (expected 13 December).

[Sources: TPG Telecom Ltd ASX Announcements: Chairman's address to shareholders 05/12/2018; 2018 AGM presentation 05/12/2018; [registration required] The AFR 04/12/2018; 05/12/2018; [registration required] The AFR 06/12/2018; [registration required] The Australian 05/12/2018]

On track for a record year of 'strikes'? The AFR reports that already 2018 is shaping up to be a record year for shareholder protests

The AFR reports that this AGM season already looks set to surpass previous years in terms of the number of 'strikes' with 13 companies facing votes of 25% of more against their remuneration reports so far.

Mineral Resources: 63.6%	NRW holdings 49.1%	Karoon 37.1%
AMP 62.2%	QBE insurance 45.6%	Computershare 31.9%

Telstra 62%	Tabcorp Holdings 40.4%	Healthscope 29.3%
Goodman Group 55.6%	Myer 37.5%	
Harvey Norman 50.6%	Austal 37.2%	

Last year, only 11 of the top 300 companies received a strike. The average vote last year against the remuneration report when strikes were registered was 35.5%, but this has also increased this year to 45.7%.

In addition, The AFR reports that there has also been an uptick in the number of protest votes against.

The AFR quotes Australian Shareholders' Association CEO Judith Fox as stating that the high levels of shareholder dissatisfaction is attributable to the lack of urgency from directors in dealing with various issues, as evidenced in the Financial Services Royal Commission hearings. 'In the face of the royal commission hearings, where we have often seen a lack of urgency from directors about dealing with the issues that have come to light, shareholders seem to be expressing their concern through voting' she said.

The article suggests that further strikes are likely with a number of super funds including Australian Super, UniSuper, Cbus and Hostplus as well as proxy firm ISS, reportedly expected to vote against the remuneration report at Westpac, and the super funds reportedly also expected to vote against reports at NAB and ANZ.

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

Regulators

Australian Securities and Investments Commission (ASIC)

ASIC areas of focus for financial reporting: ASIC has called on companies to focus on new requirements including compliance with new accounting standards, in their 31 December financial reports

The Australian Securities and Investments Commission (ASIC) has announced its focus areas for 31 December 2018 financial reports. ASIC has called on companies to focus on new requirements that can materially affect reported assets, liabilities and profits.

New accounting standards

- New accounting standards (*AASB 9 Financial Instruments* (applies from years commencing 1 January 2018); *AASB 15 Revenue from Contracts with Customers* (applies from years commencing 1 January 2018); *AASB 16 Leases* (applies from years commencing 1 January 2019); *AASB 17 Insurance Contracts* (applies from years commencing 1 January 2021); and *Amendments to standards to apply the new definition and recognition criteria in the Conceptual Framework for Financial Reporting* (applies from years commencing 1 January 2020), may significantly affect how and when revenue can be recognised, the values of financial instruments (including loan provisioning and hedge accounting), reported assets and liabilities relating to leases, accounting by insurance companies, and the general identification and recognition of assets, liabilities, income and expenses. The standards also introduce new disclosure requirements ASIC states.
- Both full-year and half-year reports at 31 December 2018 must comply with new accounting standards on revenue recognition and financial instrument values (including hedge accounting and loan loss provisioning).
- The reports must also disclose the future impact of new lease accounting requirements. There are also new standards covering: accounting by insurers; and the definition and recognition criteria for assets, liabilities, income and expenses.
- It is important that directors and management ensure that companies are prepared for these new standards and inform investors and other financial report users of the impact on reported results.
- ASIC will review selected half-year reports, focusing on compliance with the new standards.

Operating and Financial Review (OFR)

- ASIC states that listed companies should provide useful and meaningful information in the OFR about underlying drivers of the results and financial position, as well as business strategies and prospects for future financial years. Risks and other matters that may have a material impact on the future financial position or performance of the entity should be disclosed. This could include: matters relating to digital disruption, new technologies, climate change, Brexit or cyber-security.

Other considerations

- Directors are primarily responsible for the quality of the financial report, including responsibility for ensuring management produces quality financial information on a timely basis. Companies must have appropriate processes, records and analysis to support information in the financial report.
- Companies should also apply appropriate experience and expertise, particularly in more difficult and complex areas such as accounting estimates (including impairment of non-financial assets), accounting policies (such as revenue recognition) and taxation.

[Source: ASIC media release 03/12/2018; ASIC Information Sheet 183 Directors and financial reporting; ASIC Information Sheet 203 Impairment of non-financial assets: Materials for directors]

ASIC has released a report outlining its decisions on relief applications for the period 1 April to 30 December 2018

The Australian Securities and Investments Commission (ASIC) has released *Report 602 Overview of decisions on relief applications (April 2018 to September 2018) (REP 602)* which outlines some of the regulator's decisions on relief applications during the period 1 April to 30 September 2018 and summarises examples of situations in which ASIC has exercised, or declined to exercise its modification powers from the financial reporting, managed investment, takeovers, fundraising or financial services provision of the *Corporations Act 2001* and the *National Consumer Protection Act 2009*.

Some Key Points

- **Outcomes of all relief applications received:** Overall, across all categories of relief applications received: 73% were approved, 4% were refused, 12% were withdrawn and 11% were decided outside the report period.
- **Outcomes of AFS licensing relief applications:** Of all applications received for relief under Ch 7 of the *Corporations Act 2001 (Cth)* from Australian Financial Services licensing requirements, 84% of applications were approved, 10% were withdrawn and 6% were refused.
- **Outcomes of disclosure relief applications:** Of all applications received for relief from the requirements in Ch 6D to provide prospectuses and other disclosure documents; and the Ch 7 requirements to provide Product Disclosure Statements (PDSs) and Financial Services Guides (FSGs) 82% were approved, 17% were withdrawn and 1% were refused.
- **Outcomes of managed investment applications:** 86% of applications were approved, 8% were refused and 7% were withdrawn.
- **Outcomes of mergers and acquisitions relief applications:** 87% were approved, 12% were withdrawn and 1% were refused.
- **Outcome of conduct relief applications:** 65% were approved, 16% were refused and 19% were withdrawn.
- **Outcome of credit relief applications:** 76% were approved, 23% were withdrawn and 1% were refused.

[Sources: ASIC media release 06/12/2018; ASIC Report 602 Overview of decisions on relief applications (April 2018 to September 2018) (REP 602)]

ASIC cost recovery levies for 2017-2018 finalised

The Australian Securities and Investments Commission (ASIC) has released its FY 2017-18 regulatory costs and has calculated levies payable by industry to recover these costs – which total $236.6M.

A summary of the 2017-18 levies is available on the ASIC Website

ASIC has indicated that it will issue invoices in early 2019. It will also issue invoices to those that did not meet their legal obligations to register and submit details via the portal. Entities are required to pay their levy invoice or 'face interest penalties' ASIC writes.

Small proprietary companies: ASIC states that in most cases, small proprietary companies do not have specific obligations relating to industry funding. ASIC will collect the associated regulatory costs for small proprietary companies through a $4 increase to their Annual Review Fee, which took effect 4 July 2018.

Registered charities: Charities registered with the Australian Charities and Not-for-profits Commission (ACNC) at 30 June 2018 are excluded from industry funding obligations and will not receive an invoice from ASIC.

[Sources: ASIC media release 05/12/2018; Summary of industry funding levies payable by industry; More information about industry funding; FAQs]

In Brief | New ASIC Deputy Chair announced: The government has appointed Ms Karen Chester as a full time Deputy Chair to the Australian Securities and Investments Commission. Ms Chester will commence with ASIC for a five year period from 28 January 2019, replacing Peter Kell. Ms Chester has been the Deputy Chair of the Productivity Commission since May 2016, having been appointed a Commissioner in December 2013.

[Source: Treasurer Josh Frydenberg media release 07/12/2018]

Corporate Social Responsibility and Sustainability

The FT reports that Royal Dutch Shell has changed its stance on climate issues following engagement with investors

The FT reports that under pressure from shareholders, including institutional investors, Royal Dutch Shell (Shell) has committed to:

- **Setting carbon emissions reduction targets from next year:** Shell reportedly aims to curb its net carbon footprint, including emissions of its consumers, by around 20% by 2035, and will start setting specific targets each year from 2020 for the next 3-5 year period. The company also plans to increase the share of gas in its production mix from 50 to 75%, is investing more in low carbon energies and has sought to reduce the leakage of methane from wells, pipes and pumps.
- **Link achievement of the targets to executive remuneration**: Subject to a shareholder vote in 2020, Shell has reportedly committed to linking energy transition targets to executives' long term incentive plans.
- **The company has also pledged to review its membership of industry lobbying groups** which may take a stance on climate-related topics that undermine the goals of the Paris deal, which the FT identifies as a key concern for investors.

The FT quotes Shell CEO Ben van Beurden as saying that the shift in approach is a result of engagement with investors, with the short-term targets creating a more effective and flexible way to manage the company through an uncertain, multi-decade energy transition. Reportedly Climate Action 100+ (a group of international investors with more than $32tn in assets under management, including Calpers, Legal & General Investment Management and UBS Asset Management) has welcomed the move.

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

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Financial Services Royal Commission)

Top Story | Financial Services Royal Commission Round 7 Week 2, Part 2

Week 2 Round 7 hearings: Week 2, Monday 26 November – 30 November Part 2

Introduction

The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Financial Services Royal Commission) seventh and final round of public hearings commenced on 19 November and ran until 30 November. The focus of the hearings was on the causes of misconduct and conduct falling below community standards and expectations by financial services entities (including culture, governance, remuneration and risk management practices), and on possible responses, including regulatory reform. In addition, the hearings considered the role of the regulators, the Australian Securities and Investments Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) in supervising the actions of financial services entities, deterring misconduct by those entities, and taking action when misconduct may have occurred.

A high level overview of some of the issues explored in the course of questions to ANZ CEO Shayne Elliott, Chair of Bendigo and Adelaide Bank Ltd (Bendigo) Robert Johanson and APRA Chair Wayne Byres is below.

[Note: For coverage of the some of the issues to arise in the first week of Round 7 hearings (see: Governance News 26/11/2018; and week 2 see: 03/12/2018]

No submissions: Unlike in previous rounds of hearings, Counsel Assisting did not identify any particular findings as being open on the evidence. There is also no process for the entities involved in this round of hearings to make further submissions to the Commission. Rather, Counsel Assisting said that the matters raised over the course of found 7 would inform the recommendations in the Commission's final report.

Timeline: The Commission is due to release its final report on 1 February 2019.

ANZ

Questions to ANZ CEO Shayne Elliott included questions concerning the need (or not) for regulatory reform in relation to breach reporting and remediation, the topic of bank closures (and whether lenders have any obligation to keep uneconomical branches open) and remuneration (among other issues).

Breach Reporting (need for regulatory intervention or not)

- **More specific guidance from ASIC on what constitutes a significant breach would be useful:** Mr Elliott was asked a number of questions on the topic of breach reporting, remediation and changes being implemented at the lender to address past issues. Counsel Assisting asked for his views on whether amending s912D of the *Corporations Act 2001 (Cth*) in line with the ASIC Enforcement Taskforce Recommendation would address 'uncertainty' around when breaches should be reported. Mr Elliott said that this would 'certainly help' in that it would make it 'far easier if there was an objective measure of significance' though he qualified this by adding 'I don't want for a minute to suggest that that's the only solution. I mean, I think as an organisation there's an onus on us to be clear about how we define significance'. Noting that number of customers and financial impact are 'all matters referred to in the legislation already', Counsel Assisting queried what further information he would like to be included in a 'formal definition' of a significant breach. Mr Elliott responded that he would like to see more specificity, 'it does not give me a number and suggest that is significant…Those I believe, is what we're talking about when we're talking about more objective measures, given some guidance to help us determine that this has now become significant' he said. Asked whether it would be 'unrealistic to legislate particular figures attached to number of customers' or to 'amount of remediation necessary' Mr Elliott agreed, stating 'I'm not suggesting that it necessarily needs to be legislative change, but perhaps just guidance from the regulator or some best practices, some guidelines. Anything that can give greater clarity would be helpful'.

- **Should banks form their own criteria, rather than relying on legislative/regulatory reform?** Commenting that 'control is in the drafting', Commissioner Hayne asked Mr Elliott whether it would be 'useful, important, desirable, for entities like ANZ to form their own criteria' for assessing the significance of a breach, to which Mr Elliott agreed. Asked whether formalising these sorts of criteria to assist the organisation in assessing the significance of a breach, going forward, was part of ANZ's existing breach reporting project, Mr Elliott said it would be one of the things considered. 'I believe we do need to do that work ourselves and then I think it would be responsible and prudent for us to share that with our regulators for comment' he added.
- **Shorter timeframes for reporting?** Counsel Assisting asked Mr Elliott for his views on other ASIC Enforcement Taskforce Review recommendations in relation to s912D. Asked for his views on shortening the timeframes for reporting (to require that significant breaches and suspected breach investigations be reported within 30 days) Mr Elliot said that 'we support the concept…whether it's 30 days or 20 or 40, I – you know, I don't know. But the general idea, I think, is a good one'.
- **Expanding the range of penalties?** Asked for his view on increasing criminal penalties and adding a civil penalty option for noncompliance with s912D, Mr Elliott said that 'there is a role for penalties in any governance system. And if they are balanced and if they are thoughtful in terms of their – the setting of the appropriate levels, then I completely understand that there's a role for increasing the penalties'. He added that 'if we set penalty too high and too draconian we always run the risk of driving behaviour underground. That people are less reluctant to speak up because they now fear personal penalty'.
- **Approach to remediation:** The Commission heard that historically it has taken the lender on average more than four years to identify an incident that's later determined to be a significant breach, which Mr Elliott attributed in the main to the complexity and decentralised structure of the business, and limitations of the systems and processes in place to proactively identify breaches. The Commission also heard that the lender has not met remediation timelines given to the Commission. Mr Elliott then described changes being implemented to address this, including moving towards a three month timeframe for remediating customers.

Product design processes: could improvements at design stage, prevent future issues?

Commissioner Hayne questioned whether the work of reviewing and decommissioning certain products had assisted the lender 'in product design processes within the organisation to redesign products', which Mr Elliott agreed to be the case. The Commissioner then queried whether issues could be resolved at product design stage, 'I am struck by both the number and size – industry-wide, not confining this to ANZ Banking Group – I am struck by the number and size of so called processing or administrative errors. Now, the immediate response I have is why was this not fixed before the event, why is it coming out after the event. Now, is that – no doubt it is a naive and simple approach to it but are these things that can and should be picked off at product design level?' he asked. Mr Elliott agreed that they could be, adding that having a 'single point of accountability' will also assist (in the case of ANZ).

Branch closures

- **Factors in determining whether branches should be closed:** Mr Elliott was asked a number of questions in relation to the closure of branches and the factors taken into account by the lender when determining when a branch should be closed. The Commission heard that there is little economic justification for keeping branches open. Asked whether the demographics of an area, or the availability of internet services are factors in determining whether to close a branch Mr Elliott said that the assumption that older people are less comfortable with technology was not necessarily true, and that consideration is not currently given to the availability of internet services though he added 'I think we should take it into account'.
- **Public interest reasons for keeping branches open?** Counsel Assisting asked whether there are 'circumstances in which banks should continue to operate branches in regional or remote locations, even when those branches are not profitable?' Mr Elliot responded that though consideration had been given to the question, it's 'not an easy topic'. He went on to say, 'I'm not convinced that ANZ is very good at it, in terms of running regional and remote branches' due to the complexity of

understanding customer needs in remote communities, and the difficulties of finding 'appropriate' employees.

- **Actions to assist Aboriginal and Torres Strait Islander customers living in remote regions:** Mr Elliott was asked a number of questions in relation to ANZ's commitments to improving services to remote Indigenous customers. Planned changes include: reworking security questions, provision of training to assist staff in assisting Indigenous customers, the decision to cease providing informal overdraft facilities on transaction accounts where the customer is in receipt of certain Centrelink benefits (so that certain Centrelink recipients will be unable to unintentionally overdraw their transaction accounts except in limited circumstances), the decision to cease charging dishonour fees on pensioner advantage accounts and taking additional steps in relation to ensuring compliance with the 90% arrangements (the principle that recipients of government benefits should be able to retain at least 90% of those benefits in any fortnightly period).

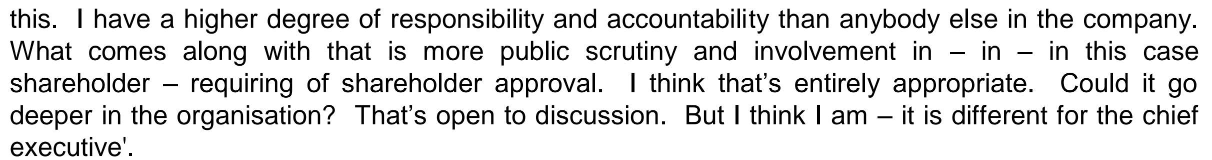
Remuneration and incentives

Mr Elliott was asked a number of questions in relation to the approach ANZ takes to remuneration, including in relation to a project to implement the Sedgwick recommendations. The Commission heard that there is an 'unapproved plan' across the ANZ group to decrease variable remuneration and to increase fixed remuneration 'for everybody at ANZ. This is not just frontline'.

- **Frontline remuneration:**
  - **Move from individual to group financial targets for frontline staff:** The Commission heard that ANZ is conducting a pilot to test whether having team financial targets (rather than individual targets) would improve customer experience and banker experience without negatively impacting business performance. The Commission heard that the results are 'encouraging' in that: a) there was 'no material drop in financial performance, b) customers 'appear to be achieving better outcomes or certainly better experience' and; c) frontline staff 'say they prefer it'. He went on to say that moving away from individual targets would require a 'shift' in thinking for some staff and that investment in 'mechanisms' to recognise team achievement, and reward individuals in a 'broader sense rather than just money' would be needed to support the change. The Commissioner suggested that the success of the change would depend on the 'quality of your junior leaders' to which Mr Elliott agreed.
  - **There is a role for sales targets/incentives:** The Commission heard that ANZ has undertaken a number of pilot programs to test the impact of removing and/or reducing variable remuneration for frontline staff. In the pilot where all financial metrics were removed (for frontline staff and their managers), the commission heard that while customer outcomes were good, financial performance 'fell off'. Mr Elliot explained that customer outcomes is not the only measure of the right outcome, given the bank is a commercial enterprise, 'I would rather our customers were happy with the experience than not but that in and of itself does not define the right outcome' he said. He added that as a commercial enterprise, ANZ's position is that there is a role for sales targets and incentive plans that take into account 'whole of role performance through a balanced scorecard approach'.

Executive remuneration:

- **Level of detail in the remuneration report — should remuneration reports include information about why remuneration was reduced?** A number of questions to Mr Elliott concerned the level of detail appropriate to include in remuneration reports concerning decisions to reduce executive remuneration due to compliance issues. Counsel Assisting suggested that remuneration reports should include more information about why executive remuneration had been reduced, as an accountability mechanism and as a means of communicating the consequences of misconduct. Mr Elliott said that though he could 'understand that perspective to give a richer evaluation or – or a summation of how decisions were made or how to make linkages between the outcomes and performance', there 'could be unintended consequences' of publishing the information. He maintained that there is a distinction between publishing the reasons for reducing CEO remuneration, and publishing the reasons for reducing the remuneration of senior executives on the basis that the CEO is ultimately accountable. He said: 'I'm the ultimate accountable person beside our board for



this. I have a higher degree of responsibility and accountability than anybody else in the company. What comes along with that is more public scrutiny and involvement in – in – in this case shareholder – requiring of shareholder approval. I think that's entirely appropriate. Could it go deeper in the organisation? That's open to discussion. But I think I am – it is different for the chief executive'.

- **No clawback mechanism:** The Commission heard that ANZ does not currently have a clawback mechanism to reclaim remuneration already delivered/paid to executives, but that it is 'the subject of debate at the moment' within the lender. 'I can't tell you there's an active working group on it but I know that we talk about it at that – at that review group and certainly at the HR committee I'm sure we will continue to – to do so' he said.
- **The two strike rule:** Asked for his views on whether the two strike rule impedes creating a remuneration structure that prioritises, in the view of the organisation, good customer outcomes, Mr Elliott said that he is 'concerned that shareholders today, irrespective of their size, have very few avenues for expressing their perspectives to a company. And understandably, I think we've seen shareholders use that to have a voice on other issues. So I am concerned about – about that'.
- **Broker remuneration:** The Commission heard that Mr Elliot supported considering alternative models for broker remuneration to ensure that the current model remains appropriate and better than any alternative. However, Mr Elliot said that moving to a flat fee model would incur the risk that people seeking smaller loans would no longer use a broker (because it would not be economical to do so) and that as a result, 'a broker becomes a service for the wealthy, much like financial planning has become).

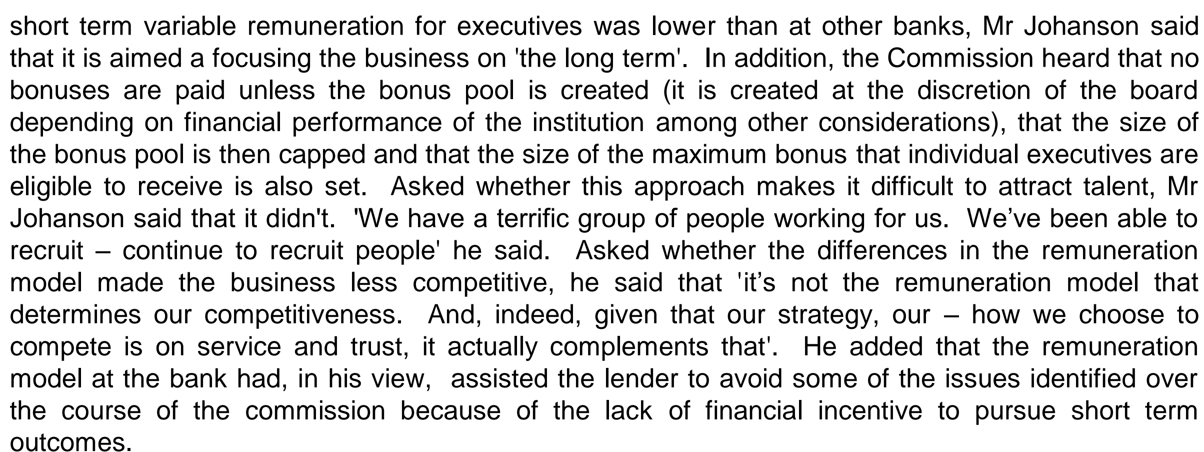
Culture

- **Benchmarking information**: Mr Elliott was asked a number of questions in relation to the culture at ANZ, the work being undertaken to create a 'speak up culture' and measures being implemented to assess and monitor culture at the lender. Among other things, Counsel Assisting asked for his views on whether 'benchmarking information' in relation to culture — 'information how your culture compares to the culture of other banks' — would be useful. Mr Elliott said that there's 'always value in getting external data. I think there's a danger – and, again, only hearing this, essentially, for the first time – I think there's a danger in some benchmark reviews, in that they imply there is the right answer, that – that somehow there is – we've defined perfection and we measure you. Culture is situational. It depends on your business and your strategy and what you are trying to achieve'.
- **Role of the regulators in 'assisting' with culture:** Asked for his views on the role of regulators in 'assisting' entities in relation to culture, Mr Elliott said that they have a role in 'giving us guidance and a – a perspective. I don't know that they – again, given that culture is situational, it does depend on what you are trying to achieve. I think their role should be more advisory and perhaps giving guide rails, rather than being prescriptive, like they might well be with capital, for example'. Asked whether they should have a role in 'calling out poor culture', Mr Elliott agreed that they should. Asked at what level of the organisation, regulators should be providing this feedback, Mr Elliott said that it should be provided to the board and the executive committee level but that 'at the end of the day, the executives are the ones who have to operationalise [any feedback]…so that feedback should also be direct to them.'

Bendigo and Adelaide Bank Ltd

Questions to Chair of Bendigo and Adelaide Bank Ltd (Bendigo) Robert Johanson focused on the theme of remuneration at both executive and frontline level, and more particularly, the way in which remuneration is structured at Bendigo.

- **Executive remuneration:** The Commission heard that the approach taken to remuneration at Bendigo differs from that of other banks in that: a) Bendigo has historically, and continues to weight its executive remuneration not towards variable remuneration but towards the base pay or fixed pay of executives; b) includes a non-financial 'hurdle'; and c) part of executives' fixed remuneration (base salary) (as well as part of short term, and long term incentives) is deferred, and can be clawed back by the board, during the deferral period. Asked whether there are disadvantages flowing from this system, Mr Johanson said that there were none, 'it has worked very well for us' he said. Asked why



short term variable remuneration for executives was lower than at other banks, Mr Johanson said that it is aimed a focusing the business on 'the long term'. In addition, the Commission heard that no bonuses are paid unless the bonus pool is created (it is created at the discretion of the board depending on financial performance of the institution among other considerations), that the size of the bonus pool is then capped and that the size of the maximum bonus that individual executives are eligible to receive is also set. Asked whether this approach makes it difficult to attract talent, Mr Johanson said that it didn't. 'We have a terrific group of people working for us. We've been able to recruit – continue to recruit people' he said. Asked whether the differences in the remuneration model made the business less competitive, he said that 'it's not the remuneration model that determines our competitiveness. And, indeed, given that our strategy, our – how we choose to compete is on service and trust, it actually complements that'. He added that the remuneration model at the bank had, in his view, assisted the lender to avoid some of the issues identified over the course of the commission because of the lack of financial incentive to pursue short term outcomes.

- **Why pay variable remuneration at all?** Asked why variable remuneration is paid at all at Bendigo given the 'strong views' that the bank appears to have about the risks associated with remuneration weighted towards short term performance, Mr Johanson 'I think it's seen as it we've had a good year, then it's appropriate that we share…that — some of the financial outcomes of that amongst other stakeholders' he said.

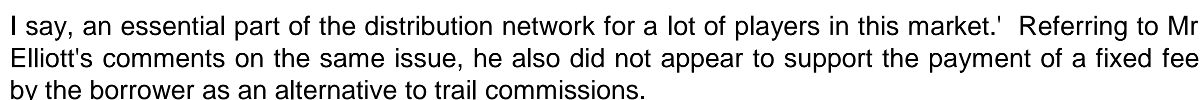
- **Long term incentives:** The Commission heard that eligibility for long term incentives is limited to the senior management group (15-20 people). Mr Johanson maintained that they have a role in this context, stating: 'it has become accepted through the…corporate world that incentive programs are an essential part of packages for senior executives. But I think, properly structured and properly managed, they can provide the – the mechanism to get employees to think about not just their job and their particular concerns, but also the interests of other stakeholders. Now, the way we structure our long-term incentive program, of course, for senior – is not the only way we give them exposure to that, but it's one way and it's an important way'. Asked whether he would consider reducing variable incentives, Mr Johanson said that it is considered 'every year' by the organisation. 'I'm sure we will continue to – to check that the behaviours we're measuring and rewarding are the ones that are really the ones we want for the long-term growth of the business' he said.

- **Shareholder support for Bendigo's approach to executive remuneration**: A number of questions to Mr Johanson focused on the issue of shareholder support for the approach taken to remuneration at the bank, including whether investors supported the inclusion of non-financial measures. Mr Johanson maintained that the approach had been supported, though the Commission heard that proxy firm ISS has not been supportive.

- **Two strikes rule:** Asked for his views on whether the two strikes rule should be modified, Mr Johanson said that he agreed it should be, but qualified this, by saying that it has some value, 'my caution is that it has turned out to be a very effective way to have people [within companies] focus on this stuff' through for example, engaging with shareholders, proxy advisers, shareholder groups.

- **Removal of sales based incentives for frontline staff:** The Commission heard that the Sedgwick recommendations to remove all sales-based incentives and commissions to frontline staff were implemented in 2004 or 2006. Asked whether this was a 'significant decision' for the lender Mr Johanson said: 'I don't think it was, at the time, particularly shocking. It was consistent with the way we had run the business' he added that the change had not negatively impacted employee motivation stating: 'They get – they get their satisfaction from being trusted and customers, you know, feeling they're doing a good job'.

- **Mortgage brokers:** The Commission heard that a low proportion of loans come through mortgage brokers (less than 10%), and that Bendigo remunerates mortgage brokers by paying upfront and trail commissions. Mr Johanson said that changes need to be made to these arrangements to address the inherent conflicts but did not appear to agree that they should be banned outright. Asked whether there was a reason to keep trail commissions he said: 'if a result of banning trails we force customers only to deal through banks and bank branches, I think that would be a very bad outcome...Let's not have those other extreme outcomes.' He went on to say that he was 'not defending trails to brokers. But I – but the package for brokers in their current form have become, as



I say, an essential part of the distribution network for a lot of players in this market.' Referring to Mr Elliott's comments on the same issue, he also did not appear to support the payment of a fixed fee by the borrower as an alternative to trail commissions.

Australian Prudential Regulation Authority (APRA)

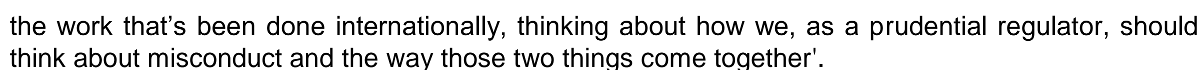
Questions to APRA Chair Wayne Byres included (among others) questions in relation to the way in which the regulator manages/delegates its responsibilities internally, the role of the regulator in overseeing culture and remuneration in the entities it regulates and the approach the regulator has taken and should take in future to oversight/enforcement.

APRA's internal governance structures

- **Dealing with overlapping issues/broader view of risk?** A number of questions concerned the approach taken to delegation of responsibility, and oversight of issues within APRA, and APRA's internal governance more generally. The Commission heard that APRA presently commissioners within the regulator have responsibility for particular areas and that APRA does not have any processes or guidelines to determine whether a matter in one member's area of responsibility should be considered by the whole board. However, increasingly, the regulator is finding that issues overlap: 'I mean, I think some of the issues – you know, one of the issues we're grappling with is actually prudential issues and conduct issues, I think, in the – what I call the traditional view. They sat in different boxes. And, increasingly, it's clear that, in fact, issues overlap with one another, and that prudential requirements – and you've said we're going to come back to BEAR – and this might be a good example – where a prudential requirement potentially also has significant benefits in relation to limiting or helping mitigate the risk of misconduct' Mr Byres said. The Commissioner suggested that 'there's a chicken and egg problem…Whether remuneration is reflecting culture, whether culture is reflecting remuneration, whether governance is reflecting culture, culture is reflecting governance. They're all intermeshed, at least to some extent aren't they?' he queried, to which Mr Byres agreed.
- **Rethink/evaluation of APRA's governance structure?** Counsel Assisting drew a comparison between APRA's structure and the structure of other prudential regulators, in particular, the UK Prudential Regulation Authority (PRA) which has the equivalent of a CEO, and a board that includes non-executive directors. Asked whether APRA would benefit from having non-executive directors or members of the board, Mr Byres responded that APRA had had non-executive members of the board in the past but that it was 'deemed not to be an effective governance structure'. Counsel Assisting suggested that an external review (capability review) of the governance structure at the regulator to evaluate whether the current approach is 'the optimal way to govern APRA' would be of use. Mr Byres said that APRA is 'always open to having helpful advice'. APRA's decision to conduct a review of its enforcement approach internally was also questioned, Counsel Assisting querying why the review work itself is not being conducted by an external group. APRA Chair Wayne Byres said that this is because it is viewed as the most 'efficient and effective way to do it' and that though the external advisory panel (comprising former NSW Supreme Court Judge Robert Austin, ACCC Commissioner Sarah Court and MinterEllison Chair of Risk, Professor Dimity Kingsford Smith) would not be conducting the review they will be 'challenging what's coming out of the…team and the process.' Mr Byres reiterated that he has no objection to 'opening APRA up to eternal scrutiny in the form of an external capability and enforcement review'. Mr Byres said: 'We've said many – we've been asked this many times, do we have a fundamental objection to a capability review. The answer is no.'

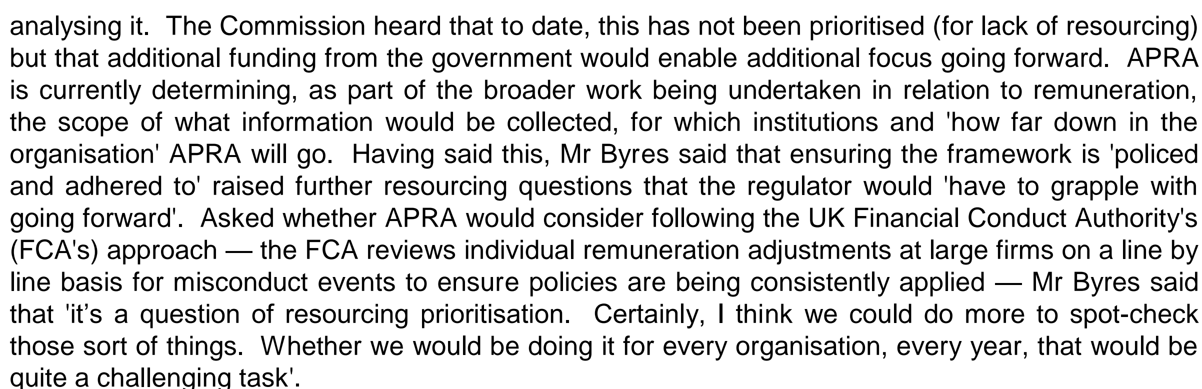
Remuneration

- **APRA's role in supervising culture/remuneration is evolving:** The Commission heard that APRA's role in supervising culture is 'evolving'. Though APRA believes that it is important that it continues to ensure prudential considerations are a primary consideration in remuneration design and decision-making, Mr Byers acknowledged that 'thinking needs to continue to evolve and a broader examination of the issue is required'. Commenting on the current guidance on remuneration, Mr Byres said that APRA had in the past 'had a very traditional…focus on traditional financial soundness issues. We've expanded our thinking into risk culture and how to think about culture within organisations and the connection between remuneration and risk culture. And, consistent with



the work that's been done internationally, thinking about how we, as a prudential regulator, should think about misconduct and the way those two things come together'.

- **Review and rewrite of prudential standards:** The Commission heard that APRA is currently reviewing its prudential standards and guidance to 'expressly address the potential for poorly designed and implemented remuneration systems to increase the risk of misconduct'. Counsel Assisting queried whether the review would entail 'rewriting the prudential standards in order to limit the extent of links between long-term variable remuneration and financial returns or pure financial returns' to which Mr Byres answered in the affirmative. Mr Byres also said that the revised standards would 'probably' be 'more prescriptive than it is today'.
- **Long Term Incentive (LTI) plans:** Mr Byres said that in APRA's view there remain too much focus on total shareholder returns (TSR) as a performance measure, and that a shift towards use of non-financial metrics would be preferable: 'I think that there is still too much focus, particularly in the long-term incentive measures, on particularly the relative TSR measure. I don't think that's conducive to the broader more holistic assessment of performance that I think we all would think was desirable. So that's a specific issue to Australia. And then in relation to internationally, we are seeing a shift away from financial metrics towards a greater weighting given to non-financial metrics. Sometimes voluntarily, but often because of new regulation that's imposing that shift'.
- **Two strikes rule:** Asked to comment on whether the two strikes rule is contributing to performance hurdles for long-term variable remuneration being excessively weighted towards financial metrics, Mr Byres said: 'I don't know if I could blame the two strikes rule, but it is – when we talk to boards – and most of my engagement has been with the large banks – we talk to them about the findings that were in that April 2018 paper. They didn't push back greatly. Many actually recognised they would like to move. But many – some have had a strike, obviously. Some are in the process of moving. And, you know, it's a likely prospect that they will get a strike. And others are very wary a strike. There's – to use a phrase that has appeared in this Commission elsewhere, no one wants to go first. There's a first mover disadvantage here. So it's a problem'. Ultimately, the Commission heard that in APRA's view, change could be accomplished through issuing a 'more prescriptive' prudential standard.
- **Level of detail that should be included in remuneration reports:** Asked for his views on whether boards should disclose more information in remuneration reports about risk related adjustments to executive remuneration, Mr Byres responded that 'there are pros and cons. It – it's a bit of a double-edged sword. So on one hand you would say if there's – if there's an expectation that rewards are disclosed, it might be reasonable to have more information to explain how those awards were determined… And my reservation about more and more and more disclosure would be that question of whether it may actually lead boards to be more reticent to exercise discretion'. Mr Byres went on to say in his view, the benefit of additional disclosure (instilling an ethical standard within a company) could be achieved without the need to name executives, if it is 'clear on the numbers' that the 'relevant executive had clearly been penalised' it would not be necessary 'to write chapter and verse' in the remuneration report he said.
- **Lack of willingness to act?** A number of questions were asked in relation to APRA's approach to oversight and enforcement of remuneration practices, Counsel Assisting questioning APRA's delay in responding. Mr Byres said that in the past, the regulator 'didn't actually have a good enough view of what good practice was' and 'didn't have a lot of expertise in remuneration' as it is 'not the natural forte of a prudential supervisor'. Given this, he said, APRA was not (in the past) in a position to challenge remuneration practices with confidence. Counsel Assisting alleged that a lack of willingness at senior leadership level within the regulator to support aggressive action in this context, meant that action on the issue was delayed. Mr Byres maintained that this was due to lack of 'confidence about the judgement about remuneration practices' and agreed that 'it's important for leadership to signal, if – if there is to be a ratcheting up of supervisory aggression, for want of a better term, it has got to be clear that when there's pushback from institutions, that the organisation from the top down will back that'.
- **Oversight of remuneration practices:** In terms of oversight of remuneration practices more generally, the Commission heard that if APRA were to 'systematically analyse' compensation practices, it would need to collect considerable more data and devote significantly more resources to


analysing it. The Commission heard that to date, this has not been prioritised (for lack of resourcing) but that additional funding from the government would enable additional focus going forward. APRA is currently determining, as part of the broader work being undertaken in relation to remuneration, the scope of what information would be collected, for which institutions and 'how far down in the organisation' APRA will go. Having said this, Mr Byres said that ensuring the framework is 'policed and adhered to' raised further resourcing questions that the regulator would 'have to grapple with going forward'. Asked whether APRA would consider following the UK Financial Conduct Authority's (FCA's) approach — the FCA reviews individual remuneration adjustments at large firms on a line by line basis for misconduct events to ensure policies are being consistently applied — Mr Byres said that 'it's a question of resourcing prioritisation. Certainly, I think we could do more to spot-check those sort of things. Whether we would be doing it for every organisation, every year, that would be quite a challenging task'.

Culture

- **Role of boards and management in 'ensuring' appropriate culture — need for APRA to provide more explicit guidance on the role of management:** A number of questions to Mr Byres centred around APRA's approach to overseeing culture, and the efficacy of that approach including relation to the development, and monitoring/enforcement of compliance with *Prudential Standard CPS220: Risk Management* (CPS 220). The Commission heard that directors had raised concerns regarding APRA's initial proposal in relation to the role of the board and more particularly the board's role in 'ensuring' culture, and that in response, APRA had amended the standard to recognise that as 'part-time non-executive directors, it will be management ultimately that sets the tone from the top, manages the business day-to-day, sets and has the most influence on the culture'. Asked how APRA approaches enforcing compliance with the standard, Mr Byres said that 'as with remuneration' APRA is 'trying to learn ourselves in this area because it's not an area where we had the – the natural great wealth of knowledge'. Asked by the Commissioner, whether APRA is at a point where it 'could, should, needs to, must – let's not hook ourselves up on the particular verb – do something about prudential standards concerning risk beyond existential financial risk?' Mr Byres agreed that this is the case. More particularly, he acknowledged that in the current standard, there is 'nothing that explicitly articulates that role of management. So it has got a role for board in overseeing something, but the "something" is not clear. It's sort of taken for granted. And maybe, if you want to start more firmly enforcing an obligation, you've got to be clear about what the obligation is' he said. The Commissioner commented, 'If you – if you're going to be enforcing the obligation, there has got to be no doubt about what the obligation is'.

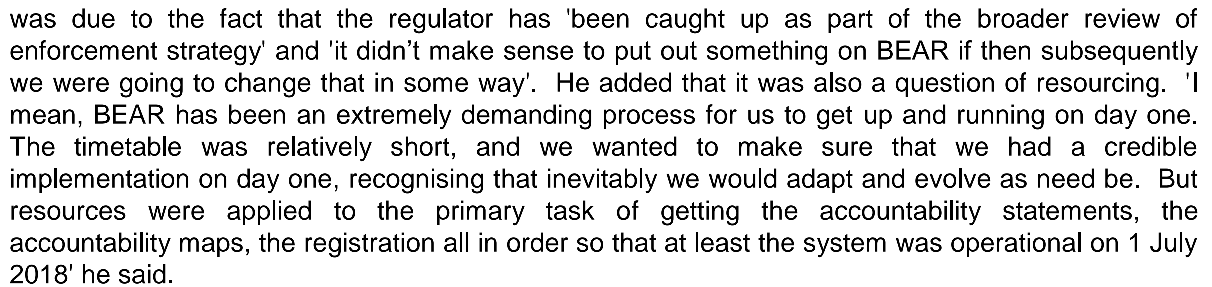
- **'Long journey to repair' culture and conduct in Australia's financial institutions?** Referencing the latest paper from the G30, the Commissioner asked Mr Byres to comment on whether he agreed that repairing the culture/conduct of Australia's financial institutions would be a 'long journey' and for his views on APRA's role in that process. Mr Byres agreed that 'there is a long journey to go' and highlighted a number of ways in which APRA will play a role through:

  - 'thinking harder' about the issue of accountability and strengthening accountability (eg in relation to BEAR);
  - strengthening the focus on audit and compliance within the prudential framework to help ensure issues are identified more quickly, 'It's probably fair to say that the prudential framework, if you look for references to compliance and internal audit, they're fairly cursory and short and we will need to think about how we give them more prominence in our assessment of risk management… audit and compliance have to be at the very forefront';
  - a stronger focus on incentives and consequences.

  In identifying these areas of focus, Mr Byres noted that APRA 'can't find all this stuff. We can't be the first line of defence'.

Banking Executive Accountability Regime (BEAR)

- **No information on how APRA will approach breaches of BEAR?** Counsel Assisting questioned why APRA had not released or explained its approach to breaches of the BEAR before 1 July 2018 (when it came into effect for the big four). Mr Byres said though it 'would be been nice to do', that it



was due to the fact that the regulator has 'been caught up as part of the broader review of enforcement strategy' and 'it didn't make sense to put out something on BEAR if then subsequently we were going to change that in some way'. He added that it was also a question of resourcing. 'I mean, BEAR has been an extremely demanding process for us to get up and running on day one. The timetable was relatively short, and we wanted to make sure that we had a credible implementation on day one, recognising that inevitably we would adapt and evolve as need be. But resources were applied to the primary task of getting the accountability statements, the accountability maps, the registration all in order so that at least the system was operational on 1 July 2018' he said.

- **Adoption of the UK model?** Noting that APRA's submission to the Commission's Interim report advocated the extension of the BEAR in line with the UK model (i.e. to apply to a broader range of financial services entities and to a wider range of misconduct), Mr Byres was asked whether it would necessitate in his view, joint administration between ASIC and APRA. Mr Byres responded that joint administration would be required were the regime broadened. Asked by the Commissioner whether the arrangements could be left at a 'high level' of whether it 'requires a deal of refinement' Mr Byres said that it could be left at a high level.

- **Learnings from the commission in terms of APRA's enforcement approach?** Mr Byres was asked to reflect on some of the issues identified over the course of the Commission (eg fee for no service issues) and the implications for the regulator, in terms of the effectiveness of its role. Mr Byres said that in the past the primary focus had been on the existence of policies and procedures, and a reliance on audit and compliance functions, rather than a focus on testing/monitoring outcomes, 'I think there's a sense that we have looked at robustness of frameworks, we've looked at policy documents, we've looked at procedures, and we've relied on audit and compliance functions to do the detailed testing, both internal and external. And – and conceptually, that if you have a good set of frameworks and policies and you – your audit and compliance function are doing their job to make sure that exceptions to those are being picked up, then actually things should broadly work as intended. But – so my general lesson, which applies to fees for no service but I think also applies to some of those other issues I have talked about is we have to think more about how do we get deeper, potentially doing more transaction testing or other things, or asking other people to do it on our behalf that would help us more readily identify these issues earlier' he said. Counsel Assisting suggested that after the Round 5 hearings, APRA amended its approach to focus more on the 'actual outcome of the application of those processes and identifying that the outcome is deficient' which Mr Byres agreed was the case.

Superannuation

- **Narrowing of APRA's remit?** Counsel Assisting was critical of the regulator's approach to supervision, and more particularly the regulator's approach to enforcement, in the superannuation sector, suggesting that 'it's difficult to believe [given the lack of enforcement action] that any superannuation entity thinks there's a credible threat that APRA would ever launch any proceeding against them'. Counsel suggested particularly in relation to BEAR and to superannuation, whether there 'are tensions between, on the one hand, being a good prudential regulator and on the other hand being a good conduct regulator' and if so, whether 'it would be better to make some shift so that you only need to be one or the other rather than being in that position of tension'. Mr Byres acknowledged there was tension, but maintained that ultimately, in the context of superannuation no narrowing of APRA's remit was necessary, 'There will inevitably be issues that have both prudential and conduct dimensions to them. And in the superannuation space, it has been said, well, APRA should take carriage of those' he said.

- **Appropriate to leave FFNS issues to ASIC?** Counsel Assisting asked a number of questions in relation to APRA's lack of action on fee for no service issues (among others) and the reasons behind it. Counsel Assisting questioned why APRA made the decision to take no action given ASIC has no mandate in respect of breaches of relevant duties under the legislation and given breaches were reported to APRA. Mr Byres said where there is already another regulator investigating the same facts, documents, actions and people, it's 'actually inefficient and sometimes unhelpful to have two regulators' investigating. Mr Byres denied that there was a 'failing' to analyse or evaluate the industry-wide issue given while ASIC has been investigating, APRA has been continuing to 'focus on

strengthening governance, strengthening risk management, pushing trustees to give more attention to what are the learnings from these exercises'.

- **Lack of public action?** Asked whether the lack of public enforcement action against superannuation entities for breach of s52 of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) is an issue, Mr Byres said that the limited sanctions available (eg no civil penalties to accompany a declaration of breach) are a factor in APRA's approach, and that APRA's focus is primarily on preventing the problems occurring. Counsel Assisting questioned whether if civil penalties were available, taking that form of enforcement action would 'fit very readily with APRA's approach. Mr Byres said 'There are obvious tensions there. And if we were – if we were taking lots and lots of enforcement action, I would probably have to conclude we were a poor prudential supervisor because ideally we should be trying to head these things off'.

[Sources: 28 November 2018 - Draft Transcript for Day 67; 29 November 2018 - Draft Transcript for Day 68; 30 November 2018 - Draft Transcript for Day 69]

Other Developments

Top Story | APRA has announced it will take enforcement action against IOOF entities, directors and executives for alleged failure to act in the best interests of superannuation members

The Australian Prudential Regulation Authority (APRA) has announced that it has commenced actions against IOOF entities and certain directors and executives for alleged failure to act in the best interests of superannuation members.

Key Points

APRA has issued a show cause notice setting out its intention to direct IOOF Investment Management Limited (IIML) to comply with its Registrable Superannuation Entity (RSE) Licence and impose additional conditions on the licenses of IIML, Australian Executor Trustees Limited (AET) and IOOF Ltd (IL). APRA's concerns relate to alleged issues in relation to 'the adequacy of the organisational structure, governance and conflicts management frameworks' within the IOOF group. More particularly, APRA alleges (among other things) that the group structure 'presented an inherent conflict of interest, as the same individuals were responsible for making decisions in respect of issues where the interests of the investors or members of the different entities within the IOOF group were likely to give rise to conflicts of interests or duty' and that these conflicts were not adequately managed. APRA also alleges that there has been insufficient progress towards addressing its concerns to date.

The additional licence conditions proposed by APRA include (among other things): the restructure of certain entities to meet its SIS Act obligations, the implementation of an action plan to address APRA's concerns within set timeframes, the provision of fortnightly progress reports and the appointment of an independent reviewer or reviewers to report every three months to APRA until all items in the action plan are completed. The entities have 14 days to respond.

APRA has also commenced proceedings in the Federal Court to seek disqualification orders and declarations in relation to five individuals (IOOF Managing Director, Chair, CFO, General Manager and Company Secretary and Group General Counsel) for alleged breaches of sections 52 and 55 of the *Superannuation Industry (Supervision) Act (1993)* (SIS Act), Prudential Standards, and associated conduct.

APRA alleges that IIML, Questor and the relevant individuals did not appropriately acknowledge and address issues concerning conflicts of interest raised by APRA from 2015 to date. More particularly, APRA alleges that on three occasions in 2015, Questor and IIML contravened the SIS Act by compensating superannuation beneficiaries and other non-superannuation investors for losses caused by Questor, IIML or their service providers, from their [ie the superannuation members'] own reserve funds rather than the trustees' own funds or third-party compensation.

If successful, the disqualification proceedings would prohibit the individuals from being or acting as a responsible person of a trustee of a superannuation entity. The court filing states that due to their involvement in the alleged 'contraventions of the SIS Act and failure to appropriately engage with and respond to APRA's prudential supervision…they should no longer remain responsible officers of a superannuation trustee'.

[Note: Round 5 of the Financial Services Royal Commission Hearings included a case study concerning IOOF. Counsel Assisting suggested in closing submissions, that it may (or may not) be open to the Commission to find that Questor and IIML breached s52 of the SIS Act. See: D.3 para 228-230 Financial Services Royal Commission Round 5 (Superannuation) Closing Submissions]

APRA Deputy Chair, Helen Rowell said that the regulator had sought to resolve its concerns with IOOF over several years but considered it was 'necessary to take stronger action after concluding the company was not making adequate progress, or likely to do so in an acceptable period of time'. She added that 'The actions we are now taking are aimed at achieving enduring change to ensure that the trustees of the superannuation funds operated by IOOF fully meet their obligation to put the interests of members ahead of all other interests. Furthermore, the individuals included in the proceedings have shown a lack of understanding of their personal and trustee obligations under the SIS Act and at law, and a lack of contrition in relation to the breaches of the SIS Act identified by APRA.'

IOOF Response

In a statement to the ASX, IOOF writes that the 'allegations are misconceived and it and its executives intend to vigorously defend the proceedings'.

The statement adds that IOOF has been 'working cooperatively with APRA to actively implement various agreed initiatives, which were most recently outlined at the 2018 Annual General Meeting. The historical matters the subject of the proceedings were disclosed to APRA a number of years ago. IOOF has already addressed or is addressing them, and it has been constructively working with APRA to this end. IOOF will continue to actively progress the agreed initiatives and will further consider the allegations raised by APRA'.

Media Response

Media reports have speculated that APRA's actions could signal a more general shift in the approach to enforcement now to be expected not only of APRA but also the Australian Securities and Investments Commission (ASIC) in the wake of the Financial Services Royal Commission and the criticism levelled at both regulators over the course of the hearings. The AFR suggests that this may be the beginning of a 'likely flood' of court cases in the coming year.

The AFR also reports that some investors, including IOOF's major investor Legg Mason, are calling for board change are applying pressure for the current Chair and Managing Director to step aside. Media reports also speculate that APRA's actions could have implications for the planned sale of ANZ's OnePath superannuation fund to IOOF. The ABC quotes ANZ deputy CEO Alexis George as stating 'Given the significance of APRA's action, we will assess the various options available to us while we seek urgent information from both IOOF and APRA'.

[Sources: APRA media release 07/12/2018; Concise statement; Show Cause notice; Financial Standard 07/12/2018; ASX Announcement: IOOF response to APRA notice and action 07/12/2018; The ABC 07/12/2018; [registration required] The AFR 07/12/2018; 07/12/2018; 07/12/2018; 07/12/2018]

The Superannuation Guarantee Bill has passed the senate (with amendments) and will now go back to the House of Representatives.

Treasury Laws Amendment (2018 Measures No 4) Bill 2018 passed the Senate on the 5 December (with amendments) and will now go back to the House of Representatives.

The Bill contains a range of measures targeting employer non-compliance with superannuation guarantee (SGC) obligations.

Some Key Points

Among other things, the legislation will:

- enable the Commissioner of Taxation to issue directions to employers to pay unpaid superannuation guarantee and undertake superannuation guarantee education courses, and to disclose more information about superannuation guarantee non-compliance to affected employees;
- extend Single Touch Payroll (STP) to all employers, regardless of the number of employees, from 1 July 2019;

- require more regular reporting by superannuation funds;
- strengthen the commissioner's ability to collect superannuation guarantee charge and pay as you go withholding liabilities;
- enable the pre-filling of an individual's tax file number declaration and superannuation standard choice force form by the commissioner to the individual's employer; and
- enable the sharing and verification of tax file numbers between the commissioner and Commonwealth agencies.

[Note: This legislation was one of the five superannuation reform Bills identified by Assistant Treasurer Stuart Robert as priorities for the government. The remaining Bills are yet to pass. See: Governance News 19/11/2018]

[Sources: Treasury Laws Amendment (2018 Measures No. 4) Bill 2018; Supplementary explanatory memorandum; Government amendments]

Superannuation law reform needed? A new report commissioned by the AIST argues there is a case for structural reform of the superannuation sector, and a case for enhanced disclosure.

A study commissioned by the Australian Institute of Superannuation Trustees (AIST): *Serious failures in superannuation governance and critical omissions in superannuation regulation*, has found that regulatory carve outs given to the for-profit super sector have resulted in 'serious omissions and exemptions in superannuation reforms that have impacted badly on the interests of super fund members'.

Some Key Points

According to the report, there is evidence that Choice products erode members' super in a number of ways. These include:

- **Choice products have higher fees and lower returns than profit to member funds:** According to the report, in the bank and retail owned funds charges are between 117-182% higher than the profit to member funds. Returns in the for profit funds were also lower than in the profit to member funds. The median profit-to-member MySuper product delivered 8.33% pa to members over 3 years as compared with 6.66% per annum by bank and retail owned funds.
- **Lack of disclosure and comparability** (as Choice products and MySuper products have different reporting requirements) was also identified in the report as negatively impacting on members by causing confusion.
- **Focus on generating profits for the corporations that own them, rather than on delivering returns to members was identified as eroding member benefits:** The report argues that evidence at the Financial Services Royal Commission has demonstrated that 'the interests of shareholder returns systemically predominate in for-profit retails funds rather than superannuation fund members' best interests'.
- **Carve-outs and exemptions over time have enabled issues to continue:** The report argues that over time, carve outs/exemptions have enabled practices that negatively impact members, to continue in the for-profit superannuation sector. For example, exemptions in relation to grandfathered commissions, and in relation to conflicted remuneration. 'This panoply of self-interested exemption exhibited by the for-profit superannuation sector has arisen over time, incrementally and without any ostensible rationale other than to benefit the providers' the report argues.
- **Need for structural change to address conflicts of interests issues?** The report argues that structural change and the extension of the best interest duty are warranted: 'The weight of the evidence gathered by the Royal Commission clearly demonstrates that structural problems are inhibiting trustees from complying with their fiduciary duties; and that structural change of entities is required by legislation to eliminate these problems. It would be a further reform of profound significance if the obligation to act in the best interest of members was extended, with contravention attracting civil penalties, and included the shareholders of trustees and any related bodies corporate

of the trustee with respect to conduct affecting the interests of the members of a superannuation fund'.

- **Calls for more transparency as a first step to addressing the issue:** AIST CEO Eva Scheerlinck said that uniform disclosure requirements across the super system are needed as the first step towards improving regulation in superannuation. This would require extending current 'product dashboard' requirements for MySuper products to Choice products. AIST has also called on the Australian Prudential Regulation Authority (APRA) to publish comparative data to help consumers more easily compare and choose super funds and to help regulators and other stakeholders have a better understanding of the efficiency of the super system as a whole.

[Sources: AIST media release 03/12/2018; Serious failures in superannuation governance and critical omissions in superannuation regulation; [registration required] The Australian 03/12/2018; Financial Standard 03/12/2018]

Open Banking progress update: No CDR Bill introduced before parliament rose for the year, but the Treasurer has reiterated that the 1 July 2019 date for open banking is unchanged

On 5 December, Treasurer Josh Frydenberg announced the government's intention to introduce legislation to enact the consumer data right (CDR) which will not only give individuals and small businesses the right to access their own data, but also allow them to authorise accredited third parties to access it.

Timeline: The Treasurer reiterated that the CDR will first apply in the banking sector (where it is referred to as Open Banking) from 1 July 2019. It will then be applied to the energy and telecommunications sectors.

However, Parliament has risen for the year, and the Bill was not introduced.

[Note: On 9 May 2018, the Government agreed to the recommendations of the Farrell Review, both for the framework of the overarching Consumer Data Right (CDR) and for the application of the right to Open Banking, with a phased implementation from July 2019. For further background information see: Governance News 11/05/2018; Exposure draft legislation: 17/08/2018; Proposed rules framework to implement the CDR: 17/09/2018]

[Sources: Treasurer Josh Frydenberg media release 05/12/2018; [registration required] The AFR 12/05/2018]

In Brief | The AFR reports that former Labor minister and ACTU secretary Greg Combet has succeeded Garry Weaven as chairman of IFM Investors, overseeing $630 billion in industry superannuation. Mr Combet has reportedly flagged a stronger push to use workers' retirement savings to take direct stakes in companies.

[Source: [registration required] The AFR 04/12/2018]

In Brief | ABA appointments: Shayne Elliott (ANZ CEO) has been reappointed Chair and David Carter (Suncorp CEO) reappointed as Deputy Chair of the Australian Banking Association for a further 12 months.

[Source: ABA media release 05/12/2018]

In Brief | ASIC has issued a reminder that the Asia Region Funds Passport (ARFP) (a multilaterally agreed framework to facilitate the cross border marketing of managed funds across participating economies (Australia, New Zealand, Thailand, Japan and South Korea) in the Asia region) will launch on 1 February 2019.

[Sources: ASIC InFocus December 2018 - Volume 27 Issue 11; Asia Funds Passport website]

Accounting and Audit

United Kingdom | The FRC has called on auditors to improve their work outside of financial statements in company reports

The UK Reporting Council has issued the results of its first thematic review of the quality of auditors' work in relation to 'other information' in company reports. The FRC found that auditor's work in relation to 'other

information' —all financial and non-financial information included in an entity's annual report other than the financial statements and the audited parts of the Directors' Remuneration Report (DRR) eg the strategic report and the directors' report — does not meet the requirements of Auditing Standards consistently.

Under current requirements, the auditor's opinion on the financial statement does not cover 'other information' in the report, but auditors are required to consider whether the other information is materially inconsistent with the audited financial statements or the auditor's knowledge and to report on this in the auditor's report. Where this requirement is not met, the FRC writes, it can mean that information is misstated, and can potentially undermine the credibility of the audited financial statements or inappropriately influence the decisions of users of the annual report.

The FRC attributes the inconsistency in the extent and quality of work in relation to 'other information' to:

- the non-prescriptive requirements in the Audit Standards;
- lack of 'prescription' in firms' own guidance to their auditors, which the FRC writes has led to varying approaches being taken to this work, even by different audit teams within the same firm.

FRC expectations of auditors

To improve the quality and consistency of their work on other information, the FRC expects auditors to:

- 'increase their scepticism and pay more attention to the completeness of information', particularly in relation to principal risk disclosures and their linkage to Viability Statements;
- ensure staff with appropriate experience and knowledge to identify potential material misstatements and inconsistencies are assigned to review the other information;
- undertake more targeted procedures, based upon more prescriptive guidance from audit firms;
- place greater emphasis on their review of key non-financial information; and
- require Boards to prepare, on a timely basis, appropriate documentation to support key areas of the other information (eg the viability statement).

Context of the review: Addressing the 'expectation gap'?

The FRC writes that the purpose of the review is not to address the 'expectation gap' between the work auditors are required to perform and the expectations of users of the annual report. Rather, the review is aimed at ascertaining the extent to which the work auditors at six major UK audit firms are currently performing on other information meets existing requirements. The outcomes of the review will however, inform further work by the FRC in this area.

Outcomes of will feed into the broader review of auditing standards: FRC Acting Executive Director for Audit Mike Suffield called on auditors to improve the extent and quality of their work in relation to the 'front end' of the annual report and added that the FRC intends to review the requirements on auditors in this area in Auditing Standards, as part of its current project reviewing Auditing Standards, to see what changes are necessary to help improve the work carried out. 'We will also consider in detail the requirements for assurance over information included in the front end as part of our recently announced project on the future of corporate reporting' he said.

[Sources: FRC media release 06/12/2018; Review of other information in the annual report December 2018]

Risk Management

Supply Chain Risk

UK government to report on steps to identify and prevent modern slavery in its own supply chains from 2019

In a speech to the House of Commons on the G20 summit, UK Prime Minister Theresa May said that her government will publish a transparency statement in 2019, outlining steps taken to identify and prevent

modern slavery in its own supply chains. 'I announced that next year the government will publish the steps we are taking to identify and prevent slavery in the UK Government's supply chains in our own transparency statement' Ms May said, describing the commitment as a 'huge challenge'.

The *Modern Slavery Act 2015* UK requires firms whose turnover exceeds £36 million to produce an annual statement detailing the actions they have taken to combat slavery in their operations, but does not presently include public bodies. Reuters reports that labour experts and campaigners have welcomed the Prime Minister's plan but have cautioned that it will be a huge undertaking considering that many companies, including many government suppliers are presently 'ignoring the law'. According to Reuters, just over 50% of the 19,000 companies required to comply with the law have issued modern slavery statements to date, and 42% of the government's top suppliers failed to comply with the requirement last year.

[Note: A report released in October 2017 by the UK Business and Human Rights Resource Centre: *First Year of FTSE 100 Reports Under the UK modern Slavery Act: Towards Elimination?* found that 43% of companies do not meet the minimum requirements set out by the *Modern Slavery Act 2015* (UK) and that the majority of companies do not provide details on the complexity of their supply chains and risks they have identified. The report also found that 'Only a handful of leading companies' were demonstrating rigorous action while the rest produced weak statements, indicating little action. See: Governance News 20/10/2017]

Is the Australian Federal Modern Slavery legislation tougher than the UK equivalent? Reuters comments that though Britain was the first to enact a modern slavery law, it is currently under review amid criticism that it 'is not being used effectively to jail traffickers, help victims or drive firms to stop forced labour.' Commenting on the passage of Australia's Federal *Modern Slavery Bill* (see: Governance News 03/12/2018), the article suggests that 'some activists say it is tougher on both the private and public sector than Britain's legislation'.

[Sources: Transcript of speech by Prime Minister Theresa May on the G20 Summit 03/12/2018; Reuters 05/12/2018]

Climate Risk

Insurers globally are transitioning away from coal according to a new study by Unfriend Coal, but some are slower to act than others.

Unfriend Coal has released its second annual survey: *The 2018 Scorecard on Insurance, Coal and Climate Change.* The scorecard ranks 24 of the world's biggest insurers on their action on coal and climate change, assessing and scoring their policies on underwriting, divestment and other aspects of climate leadership. It is based on responses to a questionnaire from 18 companies, including all European and Asia-Pacific insurers, and on publicly available information.

According to the report, moves to transition away from coal are gaining momentum with four of the world's biggest insurers announcing new restrictions on coal insurance this year. However, the report also found that insurers in the US, Japan and Australia are still supporting an industry that is undermining efforts to avoid dangerous climate change

Some Key Points

- **Trend towards transitioning away from coal:** At least 19 major insurers with more than $6 trillion in assets, 20% of the industry's global assets, have divested from coal over the last 12 months (up from $4 trillion and 13% a year ago). Generali, Lloyd's, Hannover Re, AG2R La Mondiale and Groupama announced new divestment policies this year while AXA, Allianz and Munich Re strengthened their policies.
- **Swiss Re ranks highest** for the most comprehensive policies on both coal insurance and divestment. The insurer has divested from companies relying on coal for more than 30% of their mining income or power generation, and it announced in July that it would no longer offer them insurance cover. The policy applies to both existing and new projects and across all lines of business worldwide. Its underwriting and divestment policies also cover tar sands and other extreme fossil fuels.
- **Europe's four biggest primary insurers have now restricted insurance for coal.** Allianz and Generali limited underwriting and AXA tightened its policy this year, while Zurich announced restrictions in November 2017.

- **One third of the reinsurance market has now restricted cover for coal.** Swiss Re and Munich Re announced underwriting restrictions this year, going beyond those already announced by SCOR.

Peter Bosshard, Unfriend Coal coordinator, said 'Some of the world's biggest and most trusted insurers are now exiting the coal sector, sending a strong message to governments and investors that the dirtiest fossil fuel has no future. Going forward we will focus attention on the laggards in order to reach critical mass and make coal uninsurable.'

Pressure grows on US, Japan and Australia to follow Europe's lead? The report found that Asia-Pacific insurers continue to insure and invest in coal, although there are the first signs of change. Three of Japan's largest life insurance companies, Nippon, Dai-ichi and Meiji Life, have announced they will no longer fund new coal projects. The report adds that Australia's QBE is currently reviewing its coal underwriting and investment policies.

The AFR reports that Market Forces, has called on QBE to follow the lead of the larger insurers in moving away from coal.

[Sources: Unfriend coal media release 03/12/2018; [registration required] Insuring Coal No More: The 2018 Scorecard on Insurance, Coal and Climate Change; [registration required] The AFR 03/12/2018]

In Brief | NZ climate initiative: SBS reports that New Zealand Prime Minister Jacinda Ardern has announced a new NZ$100 million green investment fund intended to encourage private-sector participation in a campaign to achieve zero net carbon emissions by 2050.

[Source: SBS 05/12/2018]

Whistleblowing

Progress update: *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017* has passed the senate (with amendments) having stalled for a year.

Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017, passed the senate with amendments on 6 December and will now move to the House of Representatives. The 58 government amendments agreed to include changes in relation to detrimental conduct and civil remedies, eligible recipients, public interest and emergency disclosures.

The Bill will now move to the House of representatives.

[Sources: Senator Mathias Cormann second reading speech 07/12/2018; Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017; Government amendments [numbers 1-6 and 8 were agreed to, the Greens amendments sheet 8421 were negatived; SBS 06/12/2018]

Cybersecurity and Privacy

Singapore | MAS has announced the launch of a new S$30m cybersecurity capabilities grant and is calling on eligible financial institutions to make applications

The Monetary Authority of Singapore (MAS) has announced the launch of a new S$30 million Cybersecurity Capabilities Grant (grant) to strengthen the cyber resilience of the financial sector in Singapore and help financial institutions develop local talent in cybersecurity.

The grant is intended to support the development of advanced cybersecurity functions in Singapore-based financial institutions, to encourage Singapore-based financial institutions to upskill their local workforce through cybersecurity-related training programs and to expand the local talent pool by attracting more cybersecurity professionals.

Specifically, the grant will co-fund up to 50% of qualifying expenses, capped at S$3 million, for:

- financial institutions to establish their global or regional cybersecurity centres of excellence in Singapore; and
- financial institutions with key global or regional cybersecurity functions and operations in Singapore to expand and deepen their cybersecurity capabilities locally.

Applications for the grant are now open for financial institutions.

[Source: Monetary Authority of Singapore media release 03/12/2018]

Cybersecurity funding announced: Eligible small businesses invited to apply for a new government grant to cover 50% of the cost of a cybersecurity assessment by an approved provider; separately, the government has announced that three cyber security projects promoting international competitiveness and strengthening Australia's cyber resilience will receive nearly $4 million in funding.

The Cyber Security Small Business Program (part of Australia's cybersecurity strategy) is designed to support small businesses across Australia in strengthening their cybersecurity posture by covering 50% of the cost (capped at $2100) of a cybersecurity assessment conducted by an approved provider (CREST). The assessment is designed to determine business risk and areas that need attention. Grants will be awarded to eligible small businesses on a first-come first-served basis, subject to the availability of funds. The program will close by 30 June 2020 (or earlier if funding is fully committed).

Eligibility criteria:

- have a certified small business health check undertaken by a certified CREST approved provider
- have an Australian Business Number (ABN)
- be registered for the Goods and Services Tax (GST)
- employ 19 or fewer full-time equivalent employees
- and be one of the following: an entity incorporated in Australia or a partnership or a sole trader.

Minister for Industry, Science and Technology Karen Andrews said the 'cost of cyber-crime to the Australian economy is estimated at about $1 billion annually and this initiative, along with the comprehensive suite of measures under the Cyber Security Strategy, is designed to ensure all players in our economy, large and small, remain resilient and competitive in the face of growing and constantly evolving online threats'.

Three cyber security projects promoting international competitiveness and strengthening Australia's cyber resilience will receive nearly $4 million in funding

Minister Karen Andrews announced three cybersecurity projects promoting international competitiveness and strengthening Australia's cyber resilience will receive nearly $4 million in funding. The Cyber Security Growth Centre, AustCyber, selected the three recipients as the second allocation of matched funding under its Project Fund.

The funding recipients are:

- $1,594,400 to Sydney-based Laava ID for a Smart Fingerprint project that enables people to identify and verify the quality of the products they buy through their smartphone, as well as a wide range of other uses.
- $1,285,450 to Melbourne company Forticode to create a highly scalable cryptographic-based technology that will allow for the independent authentication of personal data stored and managed on mobile devices.
- $995,500 to Sydney-based Cog Systems for a project that improves cyber security methods and techniques for Internet of Things device makers. The project includes convenient software to incorporate secure-by-design techniques into hardware platforms.

Speaking at the Industry Growth Centres Showcase, Minister Andrews also announced that the government will extend funding to all six Growth Centres for a further two years. The $60 million conditional investment was announced in the 2018-19 Budget and is made up of up to $5 million per year for each Growth Centre.

[Sources: ITNews 03/12/2018; Cyber Security Small Business Program 03/12/2018; Factsheet; Minister for Industry, Science and Technology Karen Andrews media release 03/12/2018; 04/12/2018]

The government's encryption access Bill has passed, but media reports suggest it looks likely to be amended in the new year

The encryption access Bill: *Telecommunications and Other Legislation Amendment (Assistance and Access) Bill 2018* passed both houses on 6 December and some elements of the legislation are now in force.

President of the Law Council of Australia Morry Bailes is quoted as commenting that 'the half-amended encryption access laws rammed through the senate are better than the original but serious concerns remain…Next year, as well as passing the remaining amendments, the intelligence and security committee needs to be brought back into the frame to get these laws right'.

Reportedly, the Bill was passed, subject to the government agreeing to consider Labor's amendments to the Bill in the new year. Attorney General Chistian Porter is quoted as commenting that the passage of the legislation 'ensures that our national security and law enforcement agencies have the modern tools they need, with appropriate authority and oversight, to access the encrypted conversations of those who seek to do us harm.' He added: 'To ensure the passage of the bill through the Senate tonight, the government has agreed to consider Labor's proposed amendments in the new year if any genuinely reflect the recommendations of the parliamentary joint committee on intelligence and security.'

[Sources: Telecommunications and Other Legislation Amendment (Assistance and Access) Act 2018; Telecommunications and Other Legislation Amendment (Assistance and Access) Bill 2018; IT News 06/12/2018; The Guardian 07/12/2018]

In Brief | At odds with the stated mission of the company? Reportedly, UK MPs have publicly released old emails that show that Facebook considered selling data to developers and used access to user data as a bargaining chip with companies and competitors, even though it appears to have understood the risks of making the data available. Chair of the UK committee inquiring into the Cambridge Analytica breach Damian Collins is quoted as stating 'I believe there is considerable public interest in releasing these documents…They raise important questions about how Facebook treats users data [sic], their policies for working with app developers, and how they exercise their dominant position in the social media market.'

[Source: Recode 05/12/2018]

Conduct Risk

UK fashion retailer Ted Baker has reportedly launched an internal investigation into allegations of misconduct by CEO and founder Ray Kelvin

UK fashion retailer Ted Baker has announced it has appointed an independent committee of non-executive directors to investigate staff allegations of workplace harassment by CEO and founder Ray Kelvin. Allegations reportedly include: sexual innuendo, asking female members of staff to sit on his knee and massaging ears or necks.

The company said in a response to media reports about the claims and a petition started by staff members calling for the company to address the issues, that 'Ray, and the company's leadership, have always prided themselves on Ted Baker being a great employer and business to work with…Accordingly, they and the board take these concerns very seriously and the board has directed a thorough and urgent independent external investigation carried out into these matters'.

The announcement followed a petition on the website organize.org.uk, signed by 2500 people (members of the public and staff members), which called for the company to put an end to the 'hugging policy' and to the wide media coverage the petition received. In a media release, organize wrote: 'Together our pressure exposed what was happening at the highest level. Now, over 100 anonymised reports of harassment are sat with Ted Baker's board'. The FT reports that the shares in company fell more than 13% following the announcement of the internal investigation.

In an interview with Retail Week, Mr Kelvin said that he hugs people because his psoriatic arthritis makes it painful to shake hands, 'You can't expect my life to change because today people are particular about certain things that we grew up quite naturally with' he is quoted as stating. The FT reports that Mr Kelvin will not be stepping aside during the investigation.

[Sources: Organise media release; Ted Baker media release 03/12/2018; [registration required] The FT 03/12/2018; Inside Retail 04/12/2018;

Other Developments

Further allegations against former Nissan Chair Carlos Ghosn?

Nikkei Asian Review reports that Japanese prosecutors are planning to rearrest former Nissan Motor Chairman Carlos Ghosn and director Greg Kelly on suspicion that Mr Ghosn underreported his compensation by 4 billion yen ($35.4 million) over the past three fiscal years. Reportedly, these allegation are in addition to, and separate from, the initial allegations of under-reporting/misreporting of Mr Ghosn's pay which led to his arrest and detention earlier in the month (see: Governance News 26/11/2018).

Reportedly, both Mr Ghosn and Mr Kelly deny the allegations, and they have yet to be charged with any crime.

[Source: Nikkei Asian Review 05/12/2018]

In Brief | Brexit looking uncertain? The AFR reports that UK MPs have voted against the draft Brexit deal, casting it further in doubt.

[Source: [registration required] The AFR 05/12/2018]

Corporate Misconduct and Liability

Energy divestment Bill: *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018* proposes to introduce a range of penalties and remedies for energy companies that engage in misconduct

Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018 was introduced into the House of Representatives on the 5 December. The Bill proposes to introduce a range of penalties and remedies for energy companies that engage in specific forms of misconduct.

The legislation follows a review conducted by the Australian Competition and Consumer Commission (ACCC) which identified problems in the retail, wholesale and the contract market which called the situation 'unacceptable and unsustainable' the Treasurer said.

Specifics

Prohibited misconduct

The Bill proposes to amend the *Competition and Consumer Act 2010* (CCA) to define the energy market misconduct to be prohibited and to provide a series of remedies.

Prohibited misconduct in the electricity sector includes:

- A retail pricing prohibition focussed on conduct by retailers where they fail to 'reasonably pass through sustained and substantial electricity supply chain cost savings to end consumers'.
- A contract liquidity prohibition to prevent energy companies from withholding hedge contracts for the purpose of substantially lessening competition.
- A wholesale conduct prohibition to stop generators from manipulating the spot market, such as withholding supply.

Remedies

Where prohibited misconduct is found by the ACCC to have occurred, the following remedies will be available:

- **Warnings/infringement notices:** ACCC issued warning notices and infringement notices.

- **Civil penalties:** Court-ordered civil penalties up to the greatest of: $10 million; three times the value of the total benefit attributable to the conduct or 10% of the annual turnover of the corporation in the 12 months before the conduct occurred.
- **Contracting orders:** In the event that the ACCC reasonably believes that a person has engaged in certain prohibited conduct in relation to the electricity financial contract market or the wholesale electricity market, the ACCC may recommend that the Treasurer make an order with contracting obligations that would require an electricity company to offer electricity financial contracts to third parties.
- **Divestiture Orders:** If the ACCC reasonably believes that a person has engaged in certain prohibited conduct in relation to the wholesale electricity market, then the ACCC may recommend that the Treasurer make an application to the Federal Court seeking an order directing the person to divest specified assets. It's proposed that the Treasurer can only make an application to the court where both the ACCC and Treasurer are satisfied the order would result in a net public benefit and further, that the court ordered Divestiture Orders can only be made where the corporation's conduct is fraudulent, dishonest or in bad faith, for the purpose of distorting or manipulating prices, and the Divestiture Order is proportionate and targeted to the conduct. In his second reading speech, Mr Frydenberg said that both contracting orders and divestiture orders are 'both sanctions of last resort'.
- **Compulsory information gathering powers:** Schedule 2 to the Bill confers new compulsory information gathering powers on the AER, allows the AER to share information with other agencies and facilitates the conferral on the AER of functions related to the regulation of retail electricity prices.
- **Sunset:** The legislation will sunset in 2025, at the conclusion of the ACCC monitoring inquiry. There will be a Government led review of the legislation in 2024.
- **Application:** The measures are intended to apply to both government owned and privately owned corporations.
- **Implementation date?** It's proposed that the measures will come into effect the day after it receives Royal Assent i.e. it will apply in relation to prohibited conduct that is engaged in on and after the commencement of those provisions, or to conduct that continues to be engaged in on and after commencement. The provisions do not apply to prohibited conduct that is conducted before the date of commencement.

Commenting on the measures, Mr Frydenberg said it 'applies to divestment is industry limited, sunsetted and requires a court order. It is consistent with similar laws in the United Kingdom which permit divestiture under the Enterprise Act and the United States which permits divestiture under the Sherman Anti-Trust Act'.

Status of the Bill: The Bill is currently at second reading stage in the House of Representatives and is yet to pass the Senate. The AFR suggests that the Bill is unlikely to pass in its current form, and speculates that it is unlikely to pass at all if a Labor government is elected.

Industry response

Reportedly, business has not responded positively to the proposed legislation and the Bill faces opposition parliament from Labor. The Greens have also reportedly said they will oppose it, unless the government reverses its position on underwriting coal power stations. Reportedly, former Prime Minister Malcolm Turnbull has called on the Morrison government to reconsider its opposition to the National Energy Guarantee (NEG).

[Source: Treasurer Josh Frydenberg media release 04/12/2018; Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018; Treasurer's second reading speech: Explanatory Memorandum; [registration required] The AFR 05/12/2018; 06/12/2018; 07/12/2018]

Former managing director of Murray Goulburn has been penalised $200,000 for being involved in the cooperative's false or misleading representations about the expected farm gate milk price

The ACCC has announced that a former managing director has been penalised $200,000 for being involved in Murray Goulburn Co-operative's false or misleading representations about the expected farm gate milk price.

Murray Goulburn admitted to making false or misleading representations in breach of the Australian Consumer Law when it represented to farmers in Victoria, South Australia and southern New South Wales on 29 February 2016, and subsequently until 27 April 2016, that it could maintain its opening milk price of $5.60/kgms. The former managing director admitted he was involved in the misleading representations made by Murray Goulburn including not informing farmers of known risks (ie the likelihood the final milk price would fall below the opening price) and making 'unfounded assumptions' that Murray Goulburn could achieve its milk powder sachet sales targets.

The ACCC writes that it did not seek a penalty against Murray Goulburn because as it was a co-operative, any penalty imposed against it could end up being paid by the very farmers that were misled. 'We were conscious not to seek penalty orders that would adversely affect farmers for the wrongs committed by Murray Goulburn, so we focused on obtaining appropriate orders against the individuals involved in the conduct' ACCC Deputy Chair Mick Keogh said. The penalty against the former managing director reflected his seniority, The ACCC states.

The former managing director undertook to the Federal Court that he will not be involved in the dairy industry for three years. The court ordered, by consent, that Murray Goulburn and the managing director pay a portion of the ACCC's legal costs.

[Sources: ACCC media release 06/12/2018; [registration required] The AFR 06/12/2018]

In Brief | The Bill to introduce stronger penalties for white collar crime: *Treasury Laws Amendment (Strengthening Corporate and Financial Sector Penalties) Bill 2018* has progressed to second reading stage in the senate, having passed the House with amendments. Labor Senator Clare O'Neil has proposed a number of amendments that would further strengthen penalties. The Business Council has released a statement opposing Labor's proposed amendments on the basis that increasing penalties would increase regulatory risk and run the risk of 'harming business confidence'.

[Sources: Treasury Laws Amendment (Strengthening Corporate and Financial Sector Penalties) Bill 2018; Business Council of Australia media release 05/12/2018; [registration required] The AFR 06/12/2018]

In Brief | While progress has been made, improvements to companies' anti-bribery and corruption strategies are still needed, according to a global study by the University of Manchester: *2018 Global White Collar Crime Survey*.

[Sources: University of Manchester media release 03/12/2018; Global White Collar Crime Survey: Anti-bribery and Corruption]