Governance News

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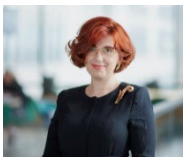

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Remuneration

United Kingdom | Ahead of the commencement of the new UK Corporate Governance Code on 1 January the UK Investment Association has issued revised Principles of Remuneration and written to remuneration committee chairs to flag specific areas of investor concern

In November, the UK Investment Association (IA) issued revised Principles of Remuneration (Principles). The changes are intended, the IA states, to make the Principles 'clearer and sharper', to bring them into alignment with the new UK Corporate Governance Code (See: Governance News 23/07/2018; 15/12/2017) (which comes into effect from 1 January 2019) and to reflect member expectations and current best practice.

Changes to the IA Principles include changes in relation to: leaver provisions, restricted shares, pensions, shareholding requirements and post employment holding periods and malus and clawback.

Areas of particular concern

In a letter to remuneration chairs, the IA flagged a number of issues as being of particular concern to IA members which it suggests, should be considered for 2019 AGMs.

These include the following.

- **Expectation that remuneration committees will be responsive to shareholders:** IA members are concerned that some remuneration committees have been unresponsive or have argued that they are operating in exceptional circumstances. Citing the uptick in protest votes against individual remuneration committee members, remuneration committee chairs and against executive recipients over the course of the 2018 AGM season, the IA writes that its members are increasingly voting against individuals where they believe that the remuneration committee's decision is not in alignment with their expectations. This is especially the case where they feel that that the remuneration committee has given undue weight to the views of management at the expense of shareholder views.
- **Expectation that fairness will be taken into account:** Members expect that remuneration committees will take 'fairness' into account when reaching their decisions. 'Executives and non executive directors can no longer rely solely on the contractual nature of a remuneration payment, investors and wider stakeholders are looking to directors to consider the issue of fairness' the IA writes. In addition, there is an expectation that the wider employee pay context will considered in the context of remuneration decisions. 'As the new UK Corporate Governance Code and pay ratio reporting requirements demonstrate, the company's approach to all employee pay is an important factor. Remuneration committees should ensure that they consider the wider employee pay context when taking their executive remuneration decisions' the IA writes.
- **Expectation that remuneration committee show restraint on overall pay levels:** The IA writes that the level of remuneration paid remains a key concern for investors. In particular, IA members are concerned about incremental increases to both fixed and variable pay, which can lead to substantial increases in overall remuneration. Given this, the IA writes that it is important that companies 'adequately justify' the level of pay (and any increases) and that members expect that remuneration committees show restraint in relation to overall pay levels.
- **Clear link between pay and performance:** The IA writes that members seek 'robust transparency on financial and non financial targets' so that the link between pay and performance is clear in order to support remuneration payouts.
- **Early adoption of new reporting requirements (pay ratios):** The IA would 'encourage' companies to report their pay ratios in 2019 (rather than in 2020 as required in most cases) using option A. In addition, the IA states that it supports the GC100 and Investor Group Remuneration reporting Guidance (currently being updated) and has called on companies to also follow it.
- **Shareholder engagement should focus on major strategic remuneration issues:** The IA writes that members have expressed concern that some companies treat shareholder consultation as a 'validation exercise' rather than as a process for obtaining the views of their major shareholders. The IA writes that consultations should focus on major strategic remuneration issues rather than on

minor details of pay and that companies should ensure that they have been sufficiently transparent and clear to ensure that the final proposals hold 'no surprises' for investors. In addition, the IA writes that full details of the remuneration structure, rather than just the proposed changes, should be provided to investors to ensure that they have a complete picture.

[Sources: Investment Association Principles of Remuneration November 2018; IA Statement on the changes 22/11/2018]

Institutional Investors and Stewardship

Institutional Investors are supportive of the development of 'prescriptive' accounting style standards to standardise ESG reporting according to an EY global survey

Ernst and Young (EY) has released the findings of its fourth survey of institutional investors' views on the use of nonfinancial information in investment decision making. The survey found that globally, there is 'consensus' that non financial information is now critical to investor decision making which reflects a shift, EY suggests, towards greater focus on forward looking disclosures and measurement of long-term value creation on the part of institutional investors. However, respondents indicated that currently there is variation in the quality and scope of information reported, particularly regarding the quality of reporting in the environmental and social categories. To address this, the report found that there is strong support among institutional investors for the development and adoption of 'prescriptive', accounting style standards to improve the quality of disclosure on environmental, social and governance (ESG) issues.

Some Key Points

- **There is 'consensus' that non-finanical information is now critical to investor decision making**: 97% of respondents said that they conduct an evaluation of target companies' nonfinancial disclosures and 96% indicated that such information plays a pivotal role in investment decision making.
- **Triggers to avoid investment?** The primary ESG factors in investment decision making were identified by respondents as risks related to supply chain, human rights and climate change risks. According to the survey, a history or risk of poor practices/poor record in relation to these issues would cause a substantial number of respondents to either rule out an investment immediately or to reconsider their decision.
  - **Risk or history of poor governance practices:** 63% of respondents said that this would cause them to decide against investing (as compared with 38% in 2017); 32% said it would cause them to reconsider (as compared with 59% in 2017) and 5% said it would not make a difference (as compared with 3% in 2017).
  - **Risks in supply chain tied to ESG factors:** 52% of respondents said that this would cause them to decide against investing (as compared with 15% in 2017); 38% said it would cause them to reconsider (as compared with 68% in 2017) and 10% said it would not make a difference (as compared with 17% in 2017).
  - **Risk or history of poor human rights practices:** 49% of respondents said that this would cause them to decide against investing (as compared with 32% in 2017); 44% said it would cause them to reconsider (as compared with 57% in 2017) and 7% said it would not make a difference (as compared with 11% in 2017).
  - **Risk from climate change:** 48% of respondents said that this would cause them to decide against investing (as compared with 8% in 2017); 44% said it would cause them to reconsider (as compared with 71% in 2017) and 8% said it would not make a difference (as compared with 21% in 2017). EY comments that respondents indicated that they are more concerned about the physical implications of climate change risk (eg the implications for disruption to supply chains) than with the transitional risks such as those tied to adapting to new regulations, practices and processes (though both types of risk remain important and which might take precedence depends on the investment strategy and timeframe in question).

- **Investors are increasingly reliant on integrated and annual reports:**
  - **Integrated reports are viewed as the most valuable source of non-financial information:** 89% of respondents said that integrated reports were very useful, 4% said that they are 'somewhat useful' and 6% indicated that integrated reports were essential sources of non-financial information. Only 1% said that integrated reports were 'not very useful'. EY notes that these numbers represent an increase in the perceived value of integrated reports on 2017 where only 57% of respondents said that integrated reports were very useful or essential.
  - **Annual reports were identified as the next most valuable source of non-financial information** with 82% of respondents identifying them as very useful and 12% of respondents identifying them as essential (up from 63% who viewed them as essential or very useful in 2017).
  - **The CSR or sustainability report was identified as the next most valuable source of non-financial information** with 2% of respondents indicating they view it as essential, 51% identifying it as very useful, 43% of respondents identifying it as somewhat useful. Only 1% identified it as 'not very useful'.
- **Investor demand for the development of 'prescriptive nonfinancial accounting standards' to standardise and improve the quality of reporting is rising:** According to the survey, investor demand for 'prescriptive nonfinancial accounting standards' to support investment decision making is rising with 59% of survey respondents indicating that accounting standards for nonfinancial information would be 'very beneficial' (a 26% increase on the last survey) and a further 30% indicating that they would be 'somewhat beneficial'. Standardising and improving the quality of the way in which companies report on non-financial risk in this way, would better enable investors to compare, benchmark and mark trends the report states. Interestingly, only 5% of respondents indicated that disclosure in line with the Task Force on Climate related Financial Disclosures (TCFD) recommendations would be 'very beneficial', though 66% of respondents said that they considered it would be 'somewhat beneficial'.
- **70% of respondents said that national regulators are best placed to lead efforts to address the expectation gap** between investors' expectations of nonfinancial information and the actual information provided, but that collaboration (between institutional investors, regulators, and other organisations (eg non-government organisations) would be desirable.

[Sources: EY blog: Does your nonfinancial reporting tell your value creation story? 29/11/2018; [registration required] The AFR 11/12/2018]

Shareholder Activism

The FT reports that Dutch activist Follow This, is pressuring BP to change its stance on climate risk having (partially) succeeded in its campaign to achieve the same result at Royal Dutch Shell

The FT reports that Dutch shareholder group Follow This (which represents 2300 retail shareholders), has filed a shareholder resolution at BP ahead of the 2019 AGM, calling for the company to set hard targets for cutting carbon emissions in line with the Paris climate agreement, including emissions of third parties, such as cars that burn BP's petrol and diesel. The resolution follows successful engagement with Royal Dutch Shell, which resulted in Shell setting targets, and tying them to executive incentives (see: Governance News 10/12/2018).

Follow This has reportedly said it plans to file similar resolutions at Chevron and ExxonMobil (unless other shareholders do so).

The FT quotes BP as stating that it 'will consider the resolution carefully and make a response and recommendation to our shareholders as part of our Notice of Meeting prior to the AGM'. The FT notes that BP has already outlined targets for reducing carbon emissions from its own processes, but that these do not include those from its customers (a key element of the Follow This resolution).

[Source: [registration required] The FT 10/12/2018]

Other Shareholder News

United Kingdom | The Wates Corporate Governance Principles for large private companies have been released

The UK Financial Reporting Council has announced the launch of the *Wates Principles* (a new, voluntary code for the corporate governance of large private companies) (see: Governance News 15/06/2018). The Principles are designed to help companies not only meet legal requirements but to promote a focus on long-term success. They will also enable, The FRC writes, companies to meet their obligations under *The Companies (Miscellaneous Reporting) Regulations 2018* which require large private businesses to include a statement about their corporate governance in their annual reports, by explaining the application of the Principles.

James Wates (who led the design of the Principles) is quoted in the FT as stating that they are designed to be 'guidelines rather than prescriptions' and are not designed to 'dictate' how companies run their businesses. Rather, Mr Wates said that they should be used as a 'tool for large private companies' to assist them in 'looking at themselves in the mirror. Good corporate governance can only be achieved if companies think seriously about why they exist and how they exist and how they deliver on their purpose'.

The six principles

1. **Purpose and Leadership** – An effective board develops and promotes the purpose of a company and ensures that its values, strategy and culture align with that purpose.
2. **Board Composition** - Effective board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual directors having sufficient capacity to make a valuable contribution. The size of a board should be guided by the scale and complexity of the company.
3. **Board Responsibilities** - The board and individual directors should have a clear understanding of their accountability and responsibilities. The board's policies and procedures should support effective decision-making and independent challenge.
4. **Opportunity and Risk** - A board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value and establishing oversight for the identification and mitigation of risks.
5. **Remuneration** - A board should promote executive remuneration structures aligned to the long-term sustainable success of a company, taking into account pay and conditions elsewhere in the company.
6. **Stakeholder Relationships and Engagement** - Directors should foster effective stakeholder relationships aligned to the company's purpose. The board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions.

Reporting against these principles will take effect on 1 January 2019.

It has not yet been confirmed who will monitor compliance with the Wates principles, although Mr Wates has reportedly said the FRC, is the 'natural' choice to do so.

[Sources: FRC media release 10/12/2018; [registration required] The FT 11/12/2018]

In Brief | The Qatar Financial Markets Authority (QFMA) has released unified listing rules for funds and a new draft governance code for listed funds for consultation. No deadline is provided for submissions on the draft governance code or draft listing rules.

[Sources: Qatar Financial Markets Authority media release 01/12/2018; Draft Governance Code for listed funds [English translation]; Proposed Listing Rules for Funds' Units [English translation]]

Meetings and Proxy Advisers

An expectation of zero short term bonuses? Westpac shareholders have delivered a first strike against the remuneration report

Westpac shareholders have delivered a first strike against lender's remuneration report (64% against vote), a protest vote (27.87%) against the grant of equity to managing director and CEO Brian Hartzer and a protest vote (35.56%) against the re-election of non-executive director Craig Dunn (who was formerly the CEO of AMP).

Remuneration Report: Media reports suggest that the vote against the remuneration report was largely a reflection of shareholder's belief that the board did not cut executive bonuses sufficiently in light of issues raised at the Financial Services Royal Commission. In his AGM address, Westpac Chair Lindsay Maxsted appeared to acknowledge this, saying that though feedback from shareholders varied, he understood that 'the key point from those voting against the remuneration report' was concern that 'although the board took events over the year into account, many have questioned whether we went far enough, particularly in reducing short term variable reward paid to the CEO and other executives'.

Mr Maxsted told the meeting that the board's decision to reduce bonuses, to the extent that it did, was in line with the performance overall. 'Our decisions were a considered view based on total outcomes for the year. While earnings were flat, and we have fallen short in areas such as financial advice and managing customer complaints, our performance across other dimensions such as balance sheet strength, customer growth and employee satisfaction has exceeded expectations' he said. He went on to say that the reductions in variable remuneration — CEO Brian Hartzer's bonus was cut by 30% and bonuses were on average 25% lower than last year — reflected, the 'collective accountability for risk and reputation matters'.

Acknowledging the high level of shareholder dissatisfaction, Mr Maxsted said that the board 'takes your feedback very seriously' and committed to 'reaching out to more shareholders' this year to 'fully capture and understand your views' adding that a review of reward frameworks is already on foot and that this would take into consideration the concerns raised.

Reportedly, Institutional Shareholder Services, the Australian Council of Superannuation Investors and the Australian Shareholders Association all advised against voting in favour of the remuneration report.

The Financial Services Royal Commission: Commenting on the Financial Services Royal Commission, and acknowledging the importance of the issues raised and shareholder concern around it, Mr Maxsted said that shareholders need to be 'mindful in generalising what the Royal Commission is finding and reporting, including across different organisations' adding that 'there is also a risk that the misconduct raised that the Royal Commission may inadvertently come to define the culture of the sector. Speaking for Westpac, that is not the case'. He went on to give examples of the positive work Westpac is doing as well as to identify specific 'lessons' that had emerged for the lender out of the commission.

Protest Vote against Mr Dunn: The protest vote against the reelection of non-executive director Craig Dunn has been attributed in media reports to shareholder concerns over his as AMP CEO during the period 2008-2013 (a period the Financial Services Royal Commission heard included instances of (alleged) misconduct). This was reportedly cited as the reason for the Australian Shareholder Associations' recommendation against his reelection.

Media reports

The result at the AGM has received wide media coverage with some reports speculating that the result at Westpac is likely to be replicated at upcoming ANZ and NAB AGMs in the coming week given the apparent level of shareholder discontent.

Expectation that bonuses be reduced to zero? The ABC reports that the Australian Council of Superannuation Investors (ACSI) CEO Louise Davidson has suggested that it would have been more appropriate for Westpac (and for other banks) to follow CBA's example and reduce executive short term bonuses to zero, 'The first question that this raises in our minds is what do you have to do not to get your bonus' she is quoted as saying. 'The really key thing here is, from our perspective, boards need to be able to exercise discretion not to pay bonuses when that is warranted'.

[Note: The CBA elected to reduce bonuses to zero ahead of the AGM on 7 November. The remuneration report was approved by 94.2% of shareholders. See: CBA ASX Announcement 07/11/2018; Chair's address 07/11/2018]

'Hell-bent on punishing' boards? The SMH suggests that shareholders appears to be increasingly willing to deliver a 'strike' as a mechanism for protesting on a range of issues such as poor financial performance or ESG issues, rather than as a means of registering discontent with the approach taken to remuneration by the organisation per se. As such, the article speculates that shareholder anger over issues raised at the Financial Services Royal Commission could result in similar results at the upcoming ANZ and NAB AGMs.

The ABC reports that ACSI CEO Louise Davidson has denied that ACSI's recommendations that members vote against the remuneration reports at Westpac, NAB and ANZ is a protest against any broader issues, stating that it is purely about the 'structure and the way remuneration's been handled, not to do with other issues…In our view, the real key is that remuneration should reflect outcomes for the organisation … if things have not been done well by the company over the year, we would expect that to be reflected in the remuneration report that they put forward' she reportedly said.

[Note: The operation and effectiveness of the two strikes rule (the question of whether it contributes to performance hurdles being excessively weighted towards financial metrics, rather than positive customer outcomes) was a topic explored with a number of witnesses during the Financial Services Royal Commission Round 7 (Policy) hearings. Asked whether the rule should be changed, APRA Chair Wayne Byres appeared to acknowledge the value of the rule as a means for shareholders to 'express dissatisfaction' and suggested that change to address the challenges of moving away from excessive weighting on financial metrics could be accomplished through other means (ie changes to prudential regulation). See: Financial Services Royal Commission Transcript 29/11/2018 at p 7404-7405; Governance News 10/12/2018]

Climate issues were reportedly a theme of shareholder questions at the meeting: The Australian reports that a number of questions to Westpac Chair Lindsay Maxsted were not focused on remuneration but on the bank's approach to climate change and more particularly, to the bank's continued investment in coal (though there was no shareholder proposal concerning this issue considered).

[Note: A resolution lodged by ESG group the ACCR seeking clarification of Westpac's position on climate advocacy was withdrawn ahead of the meeting following successful engagement with the lender on the issue. See: Governance News 23/10/2018. Separately, BankTrack has recently called on signatories to the UN Principles for Responsible Banking (including Westpac) to end investment in fossil fuel projects and develop phase out plans for their existing fossil fuel portfolios. See: Governance News 03/12/2018]

[Sources: Westpac ASX Announcements Results of 2018 AGM 12/12/2018; 2018 AGM CEO's address 12/12/2018; 2018 AGM Chair's address 12/12/2018; [registration required] The AFR 12/12/2018; The SMH 13/12/2018; The ABC 12/12/2018; [registration required] The Australian 13/12/2018; [registration required] The AFR 12/12/2018; 12/12/2018; 12/12/2018; The SMH 12/12/2018; 13/12/2018]

Regulators

Australian Prudential Regulation Authority (APRA)

Top Story | APRA sets 'higher bar' for RSE licensees: APRA has announced new measures to strengthen outcomes for superannuation members to apply from 1 January 2020.

The Australian Prudential Regulation Authority (APRA) has released a package of changes to prudential requirements intended to strengthen the focus of registrable superannuation entity (RSE) licensees on the delivery of quality outcomes for their members. In a statement announcing the changes, APRA deputy Chair Helen Rowell said they 'set a higher bar for RSE licensees by requiring a robust assessment of the outcomes delivered for members, to be reflected in strategic and business planning'.

Key change: Annual outcomes assessment

APRA highlights the introduction of an annual outcomes assessment, which requires RSE licensees to annually benchmark and evaluate their performance in delivering quality outcomes to all members as part of their business planning cycles, as a key change.

- **Application:** The outcomes assessment applies to 'all types of superannuation products' including defined benefit and legacy products.
- **Further changes possible (pending the outcome of the Bill)?** APRA comments that the introduction of the outcomes assessment requirement is consistent with the proposed outcomes assessment in legislation currently before parliament: *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No 1) Bill 2017* (currently before the senate) and notes that it will review whether any further changes are needed to the prudential standards and guidance to maintain consistency with the Bill if/when it is passed.

Changes: further detail

The final package of changes includes the following.

1. New Prudential Standard SPS 515 Strategic Planning and Member Outcomes: The new standard applies to all registrable superannuation entity (RSE) licensees (RSE licensees) and commences on 1 January 2020. The standard requires that RSE licensees must:
    - have strategic objectives that support it in achieving the outcomes it seeks for beneficiaries and the sound and prudent management of the RSE licensee's business operations;
    - maintain a board-approved business plan that sets out the approach for implementation of the RSE licensee's strategic objectives;
    - ensure that decisions to incur significant fund expenditure support the RSE licensee achieving its strategic objectives and that those decisions are monitored against their expected outcomes; and
    - as part of the annual review of its business plan, conduct an outcomes assessment and incorporate, where appropriate, any actions arising from that assessment.
2. **New Prudential Practice Guide SPG 515 Strategic and Business Planning:** SPG 515 outlines APRA's requirements for an RSE Licensee to set strategic objectives for its business operations and to maintain a written business plan that articulates the RSE licensee's approach to achieving them. Among other things, SPS 515 requires an 'RSE licensee to have a rolling business plan of at least three years duration that is reviewed annually'. APRA states the plan must 'set out details on how the strategic objectives will be achieved' and that the 'the business planning process would be the responsibility of the Board and senior management and any decision-making delegations relating to the business plan would be clearly articulated'.

    SPG 515 also contains prudential requirements to ensure that fund expenditure is in the best interests of members and ensure that there is a comprehensive decision making and monitoring process for expenditure that is 'determined by its size or nature to be extraordinary'.
3. **New Prudential Practice Guide SPG 516 Outcomes Assessment:** SPG 516 outlines APRA's requirements for an RSE licensee to annually assess the outcomes provided to members (outcomes assessment) and determine whether these outcomes can be improved into the future. More particularly, it provides guidance in relation to articulating outcomes, designing the outcomes assessment, undertaking the outcomes assessment, interpreting the outcomes of the assessment results and linking them to strategic objectives.
4. **Amendments to Prudential Standard SPS 220 Risk Management** to align it with the cross-industry risk management standard CPS 220 by requiring an RSE licensee to have a management information system (MIS) as a component of its risk management framework. APRA comments that an effective MIS is central to the management of risk and the monitoring of performance and outcomes, including business planning activity outcomes, across an entities' operations. APRA adds that it expects that for many RSE licensees the addition of the MIS requirement to SPS 220 will not require significant changes to existing systems and processes.

Timeline: new requirements commence 1 January 2020

Revised SPS 220 and new SPS 515 will commence on 1 January 2020 which means that RSE licensee's first outcomes assessment will need to be conducted by 31 December 2020. APRA notes that the timing of an RSE licensee's review of its business plan will determine when in 2020, the first outcomes assessment will need to be undertaken.

APRA states that it considers the 12 month implementation timeframe to be appropriate given industry's advance notice of the likelihood of the changes.

Preparation required

APRA writes that compliance with SPS 515 on 1 January 2020 will require RSE licences to prepare over the course of 2019. APRA's response paper includes a suggested implementation timeline in relation to this which suggests that starting 1 January 2019 RSEs should:

- conduct a gap analysis of existing practices against business planning and expenditure management requirements in SPS515 and address the gaps identified;
- design the outcomes assessment and discuss it with APRA; and
- plan to undertake their first outcomes assessments in conjunction with their 2020 annual reviews of their business plans.

APRA's expectations during the first year

APRA writes that the outcomes assessment represents a new prudential requirement and 'that there will be a period of learning for the industry' in implementing the changes. Consequently, in the first year APRA states that supervisors will look for 'reasonable efforts by RSE licensees to conduct the assessment in a comprehensive way and align it with their business planning processes'. Having said this, APRA states that it expects 'some preliminary assessment of outcomes for all products and members', though the regulator notes that for some RSE licensees, segmentation in the first year may be at a relatively high level and may have a primary focus on MySuper members due to greater availability of MySuper data.

Other proposed changes deferred?

- **Changes to make it easier to opt out of life insurance:** APRA states that it has determined to defer proposed changes to *Prudential Standard SPS 250 Insurance in Superannuation* (SPS 250) until 'the final form of any related legislative changes arising out of the government's Protecting Your Super package in the 2018-2019 Budget are known' as the reforms are likely to require 'extensive changes' to SPS 250. According to the response paper, industry stakeholders were generally supportive of the proposal to make a minor amendment to SPS 250 regarding implementation of straightforward insurance opt out processes. APRA adds that it will monitor opt-out processes and changes in insurance offerings following industry's adoption of the Code of Practice and assess whether industry developments should be reflected in any changes to SPS 250 and SPG 250.
- **Changes to reporting proposals (as outlined in the December discussion paper):** APRA states that it will be conducting further work to assess the scope and timeframes for amendments to the reporting collection. APRA adds that this will take into account the outcomes of APRA's post-implementation review of the prudential framework, the Productivity Commission's final report on its review of superannuation (due December 2018), and the Royal Commission's final report (due February 2019).

Media response

The AFR comments that the move by APRA to act to strengthen requirements, without waiting for the Bill (*Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No 1) Bill 2017*) to be passed, is further evidence of the shift towards a tougher approach on the part of the regulator. It's also suggested that APRA's acting ahead of the passage of the Bill is a positive development for members, given the lack of progress on a number of pending superannuation reforms.

The Australian suggests that the more stringent accountability requirements could 'hasten mergers' between smaller and poorly performing funds. The article adds that the passage of the Bill which would grant APRA powers to direct fund trustees to act or face court action, would give 'teeth' to the reforms.

[Sources: APRA media release 12/12/2018; APRA response to submissions: Strengthening superannuation member outcomes December 2018; Investment Magazine 12/12/2018; [registration required] The AFR 12/12/2018; The Australian 12/12/2018]

Australian Securities and Investments Commission (ASIC)

Top Story | Raising standards in financial services dispute resolution: ASIC to conduct onsite reviews of internal dispute resolution systems and consult on changes to IDR standards and guidance

Overview: Report 603 *The consumer journey through the Internal Dispute Resolution process of financial service providers*

The Australian Securities and Investments Commission (ASIC) has released the results of its report into the consumer experience of internal dispute resolution (IDR) procedures across the financial services sector.

The report looked into the experience of people thinking about, or making a complaint to, a financial services firm (firms operating in the banking, credit, general insurance, life insurance, financial advice and superannuation sectors). It also looked at the incidence of complaints, as well as the barriers and difficulties people face in approaching and navigating the complaints process. Overall, ASIC found that making a complaint is a stressful exercise for many people, and that there are clear opportunities for financial services firms to improve consumer experience and outcomes.

Some Key Points

- In the last 12 months, 3.2m Australian adults considered making a complaint about a financial services firm. Of this group, 1.7m did not proceed and 1.5m complained.
- Of those who complained 270,000 withdrew from the complaints process. 47% said that they didn't think it would make a difference, 38% said they felt it was not worth their time to proceed, and 26% said that they did not have enough time.
- Of those complaints that proceeded, 82% of complaints were concluded. 66% of finalised complaints were in favour of the complainant.
- The primary barriers or obstacles that consumers faced in the complaints process were:
  - 4 in 5 people experienced difficulty, decreased satisfaction or formed a negative impression of the firm
  - 1 in 2 people (whose complaint was not resolved in their favour) received no explanation as to why this was the case
  - 4 in 5 people (whose complaint took over 45 days to resolve) weren't told about external dispute resolution options
  - 1 in 3 people felt they spoke to too many contacts over the course of their complaint
  - 1 in 7 people found it difficult to locate the firm's contact details
  - 1 in 7 people withdrew from the complaints process due to inadequate response form the firm
- Of the group who didn't proceed with a complaint, 1 in 4 (408,000 people) expressed dissatisfaction to the firm (19% did so in person and 6% did so via social media). Some consumers expressed dissatisfaction to others: 55% expressed dissatisfaction to friends or family, 8% on social media, 8% on online forums, 4% approached a solicitor and 3% did so somewhere else.

Areas of particular concern

ASIC highlights two issues of particular concern:

1. the fact that only 45% of complainants who received an unfavourable outcome received an explanation of the decision made against them by the firm, and

2. the fact that only 21% of complainants whose complaints were not resolved in the timeframe set by ASIC guidance had the external dispute resolution (EDR) process explained to them.

ASIC writes that it considers that these steps are essential to assist consumers to effectively escalate their complaint to an independent and external forum (which since 1 November has been the Australian Financial Complaints Authority (AFCA)).

Commenting on the report findings ASIC Commissioner Ms Danielle Press said, 'As the first step in the financial dispute resolution system, IDR plays a vitally important role in Australia's consumer protection framework. Consumers and small businesses should have access to transparent, fair and timely complaints processes. Our research shows the strong connection between consumer satisfaction in how a firm deals with a problem, and their confidence in that financial firm. Making a complaint can be a stressful exercise for many people and that there are clear opportunities for financial services firms to improve consumer experience and outcomes'.

ASIC work on raising financial services IDR standards, outcomes and transparency

ASIC states that the release of the report is the 'first step' in a broader body of work aimed at improving financial services IDR standards and transparency.

- **Industry action:** ASIC has called on all financial firms to closely review the research findings and consider whether their complaints procedures need to be reformed to improve the experience for consumers and to ensure that identified problems are remedied effectively and promptly. Firms should also prepare to engage with ASIC about its review of the complaints handling standards and requirements.
- **IDR onsite visits:** ASIC states that a specialist ASIC team has been set up under ASIC's Close and Continuous Monitoring Program to conduct onsite monitoring of the IDR functions at NAB, CBA, Westpac, ANZ, and AMP. The team will review and assess target firms' IDR arrangements (including processes, practices, resourcing, communications, governance and reporting) and will map and evaluate their systems capabilities.
- **Review of ASIC standards and guidance:** From February 2019, ASIC will be consulting publicly on a review of existing IDR guidance set out in *Regulatory Guide 165, Licensing: Internal and external dispute resolution*. This review will consider, amongst other matters: the definition of 'complaint' ie what triggers the IDR process; requirements for complaints that are resolved immediately or within 5 business days; maximum IDR timeframes across all complaints including superannuation related complaints, and written reasons for decisions made by superannuation trustees about complaints. The review will also include consultation on the proposed data collection and reporting framework for financial firms to report on IDR performance. Both the broad IDR policy reforms and the proposed data collection framework will be informed by insights from the consumer research and findings of the IDR onsite program.

[Sources: ASIC media release 10/12/2018; Report 603, The consumer journey through the Internal Dispute Resolution process of financial service providers]

Delay in implementation of certain fee disclosure changes: ASIC has announced that the start date for updated superannuation fees and costs disclosure has been deferred to enable consultation on recommendations raised in ASIC Report 581.

The Australian Securities and Investments Commission (ASIC) has announced that it has extended the transition period for certain fees and costs disclosures for superannuation funds and managed investments schemes. ASIC states that this will enable additional time for consultation on proposals arising out of recommendations made in the review of the fees and costs disclosure regime in *Report 581 Review of ASIC Regulatory Guide 97: Disclosing fees and costs (Report 581).*

Details

ASIC Class Order [CO 14/1252] provided for certain disclosure obligations in relation to periodic statements for both superannuation and managed investment products for reporting periods prior to 30 June 2018 to operate differently for reporting periods after 30 June 2018. The class order also permitted superannuation

trustees to deal with property operating costs in product disclosure statements (PDSs) given before 30 September 2018 by providing details of these in the 'Additional explanation of fees and costs' part of the PDS rather than incorporating them into the figure disclosed as 'investment fees'.

In November 2017, ASIC appointed an external expert to conduct a review of the fees and costs disclosure in superannuation and managed investments. Given the review, in December 2017, ASIC extended the transition dates by one year to their equivalent dates in 2019.

ASIC Corporations (Amendment) Instrument 2018/1088, has amended Class Order [CO 14/1252] to extend the transition dates by one further year to their equivalent dates in 2020. This will ensure, ASIC states, that industry does not incur additional expense in complying with new requirements which may change as a result of the consultation (eg change the treatment of property operating costs). ASIC states that it expects publish a consultation paper in January 2019.

[Sources: ASIC media release 11/12/2018; [registration required] The Australian 12/12/2018]

In Brief | ASIC has released a consultation paper proposing to remake its class order regarding warrants and out of use notices. The new instrument would continue the relief, without significant changes, currently given by Class Order [CO 08/781] *Warrants: Out-of-use notices*, so that the ongoing effect will be preserved without any disruption to the entities that rely on it. The class order is due to expire on 1 April 2019. Consultation will close on 6 February 2019.

[Sources: ASIC media release 13/12/2018; Consultation Paper 307 Remaking ASIC class order on warrants: out-of-use notices (CP 307)]

Financial Services

New Zealand | The Reserve Bank of NZ is consulting on a proposal to raise the amount of capital that banks must hold as a means of 'having a safer banking system'.

The Reserve Bank of NZ is consulting on a proposal to raise the amount of capital that banks must hold.

The proposal would see banks' capital levels increase 'materially'. Generally, the RBNZ states, it will be an increase of between 20 and 60% which represents about 70% of the banking sector's expected profits over the proposed 5 year transition period for banks to meet the new requirements.

The RBNZ notes that 'In practice, actual changes to the amount that they hold will be less than double and will vary' as the increase will depend on their current levels of capital, how much extra they choose to hold above the required minimum, and whether they are a large or small bank'.

Deputy Governor and General Manager of Financial Stability Geoff Bascand said that 'While borrowing costs may increase a little, and bank shareholders may earn a lower return on their investment, we believe these impacts will be more than offset by having a safer banking system for all New Zealanders'.

The deadline for submissions on the proposal is 29 March 2019.

CBA response: The CBA has issued a statement acknowledging the RBNZ consultation and stating that it is reviewing the proposals to determine 'potential impacts on the Group's capital requirements'. CBA states that it will participate in the consultation process through its New Zealand-based subsidiary, ASB Bank (ASB).

[Sources: Consultation paper: How much capital is enough? Non-technical summary: How much capital is enough?; RBNZ media release 14/12/2018; CBA ASX Announcement 14/12/2018]

The ACCC has released its final report on the residential mortgage prices of the five major banks subject to the bank levy.

The Australian Competition and Consumer Commission (ACCC) has released its final report on the residential mortgage prices of the five banks subject to the Major Bank Levy.

The report found (among other things) that 'the accommodative and synchronised approach to pricing we have previously observed among the big four banks was again evident at this time' and more particularly,

that 'opaque and discretionary pricing' is causing inefficiency and stifling competition and that new borrowers are paying lower interest rates than existing borrowers on average.

In terms of the factors that drove the Inquiry Banks' decisions to make headline variable interest rate changes, the report found that 'APRA's interest-only benchmark…created a focal point for the Inquiry Banks, and in particular the big four banks, to increase headline variable interest rates for interest-only residential mortgages' and that though APRA's objective was to contribute to financial system stability, the introduction of the benchmark 'provided the opportunity for the banks to synchronise their significant increases to interest-only rates during the price monitoring period, at a significant cost to those borrowers'.

The regulator also found there were no changes to interest rates or other charges, to recover the cost of the government's major bank levy. 'After reviewing internal bank documents, confidential financial data and publicly available financial information for each Inquiry Bank, we found no evidence that the Inquiry Banks changed residential mortgage prices specifically to recover the cost of the Major Bank Levy, whether in part or in full, during the price monitoring period' the report states.

In a statement commenting on the report, Treasurer Josh Frydenberg said (among other things) that the ACCC's findings add 'further weight to the important actions' the government's planned Open Banking reforms which he said would 'improve competition and transparency in the residential mortgage market' and 'revolutionise the ability of consumers to shop around for a better deal'.

Mr Frydenberg also said that the government has asked the Council of Financial Regulators to accelerate the development of options to implement the development of an online calculator which will report on actual interest rates paid and discounts received by different types of borrowers (as was recommended by the Productivity Commission's report into competition in the financial system).

[Sources: ACCC media release 11/12/2018; Residential mortgage price inquiry: final report; Treasurer Josh Frydenberg media release 11/12/2018; [registration required] The SMH 10/12/2018; [registration required] The Australian 10/12/2018]

Implementation of new professional standards for financial advisers update: ASIC has clarified RG 146 requirements for advisers, FASEA has confirmed accreditation requirements for professional designation programs.

- **ASIC has clarified Regulatory *Guide 146 Licensing: Training of financial product advisers* (RG 146) requirements for financial advisers:** ASIC has issued a statement confirming that existing RG 146 requirements (which sets out the minimum training standards for financial advisers) will not apply to new entrants to the industry seeking to become a relevant provider from 1 January 2019. New advisers will need to meet the new professional standards requirements. However, RG 146 will continue to apply to financial advisers who are authorised by their Australian Financial Services Licensee as an 'existing provider' until the new requirements apply to them. RG 146 will also continue to apply to advisers who are not 'relevant providers' (those who only provide general advice, those who provide advice about Tier 2 or less complex financial products and those who only give advice in relation to a time-sharing scheme). ASIC states that it will review and update the guidance for advisers who are not relevant providers.

[Sources: ASIC media release 14/12/2018; Independent Financial Adviser 14/12/2018]

- **FASEA has confirmed the accreditation process** and has called on financial services industry associations with relevant professional designation programs to submit their curriculum content for approval as soon as is practicable.

[Sources: FASEA media release 12/12/2018; Independent Financial Adviser 12/12/2018]

In Brief | Following APRA's recent announcement of enforcement action against IOOF entities and certain executives, IOOF's CEO and Chair have reportedly stepped down (temporarily) from their respective roles. IOOF non-executive director, Allan Griffiths has reportedly been appointed as acting Chair.

[Sources: [registration required] The AFR 10/12/2018; [registration required] The Australian 10/12/2018]

Accounting and Audit

United Kingdom | New calls to break up the big four: A report commissioned by the UK Shadow Chancellor, has reportedly recommended a number of measures to reform the UK audit sector including breaking up the big four

A report into the UK audit sector commissioned by Shadow Chancellor John McDonnell has reportedly recommended measures to reform Britain's accounting sector, including (among other things) placing a 50% market share cap on the 'big four' accounting firms (EY,PwC, KPMG and Deloitte) creating an independent body to audit the accounts of banks and other institutions, and breaking up accounting firms to separate auditing from other activities.

The report has been released ahead of the Competition and Markets Authority review (expected to be released this month see: Governance News 15/10/2018) into the audit sector, which media reports speculate may also recommend: a restriction on the number of large listed companies that the big four are able to audit; and the introduction of joint audits which would see a smaller rival firm working alongside one of the dominant four on the accounts of large companies.

[Sources: City AM 14/12/2018; [registration required] The FT 14/12/2018]

United Kingdom | The Financial Reporting Council has issued revised auditing standard and is consulting on guidance for quality bank audits

The UK Financial Reporting Council (FRC) has issued a revised *International Standard on Auditing (UK) 540 (Revised) Accounting Estimates and Related Disclosures*, based on *ISA 540 (Revised) Auditing Accounting Estimates and Related Disclosures* of the International Auditing and Assurance Standards Board (IAASB).

The new standard covers the audit of expected credit losses in banks and reflects the increased importance and complexity of estimates in financial statements.

The FRC's Acting Executive Director of Audit and Actuarial Regulation Mike Suffield, commented that new standard 'provides a comprehensive, principles-based approach to delivering audits of estimates and related disclosures to a level that meets the needs of users and protects the public interest.'

Timeline: This ISA (UK) is effective for audits of financial statements for periods beginning on or after 15 December 2019, though the FRC notes that early adoption is permitted.

Consultation on proposed revisions to Practice Note 19 (the audit of banks and building societies): The FRC is also consulting on updates to its Practice Note on The Audit of Banks and Building Societies, to reflect revisions to the UK auditing standards (ISAs (UK)), in particular: ISA (UK) 540 (Revised December 2018); changes in legislation and regulation; and the establishment of the Prudential Regulatory Authority (PRA) and Financial Conduct Authority (FCA) in place of the Financial Services Authority (FSA).

Consultation closes on 8 March 2019.

[Sources: FRC media release 12/12/2018; International Standard on Auditing (UK) 540 (Revised); Feedback Statement and Impact Assessment Auditing Accounting: ISA (UK) 540 (Revised December 2018) Auditing Accounting Estimates and Related Disclosures; Proposal to revise Practice Note 19 The Audit of Banks and Building Societies in the United Kingdom; Exposure Draft: Practice Note 19 (Revised) - The Audit of Banks and Building Societies in the United]

In Brief | Update on the progress of the Kingman Review: The minutes from the November meeting of the independent review into the Financial Reporting Council (Kingman Review) were released on 12 December.

[Source: Financial Reporting Council Review: Advisory Group — meeting minutes, 14/11/2018]

Risk Management

Cybersecurity and Privacy

Top Story | ACCC's Digital Platforms Inquiry calls for far-reaching reforms

On 10 December 2018, the Australian Competition and Consumer Commission (the ACCC) released its preliminary report on the Digital Platforms Inquiry (Report), outlining a range of significant findings and far-reaching recommendations that impact business, the media, and consumer privacy rights.

The ACCC is seeking feedback on its preliminary recommendations as well as the additional concerns it has identified for further analysis and assessment. Submissions are due by 15 February 2019. The final report is due by 3 June 2019.

Key Takeouts identified by MinterEllison Partners Miranda Noble and Paul Schoff, and Special Counsel Veronica Scott are:

1. The ACCC has found that Google and Facebook have substantial market power in a number of markets, which affects how news is distributed online and how companies collect, use and disclose personal information.
2. The regulator recommends sweeping reforms to address this, including changes to cornerstones of Australian's consumer and privacy laws and a government review of our media regulatory framework.
3. A major recommendation is that unfair contract terms should be illegal and subject to financial penalties, rather than merely void.

The full article, entitled: *ACCC's Digital Platforms Inquiry calls for far-reaching reforms* is available on the MinterEllison website here.

[Source: ACCC's Digital Platforms Inquiry calls for far-reaching reforms 14/12/2018]

A global coalition of technology firms has issued a statement calling on the Australian government to address 'flaws' in the recently enacted Assistance and Access Act when it reconvenes next year

The Reform Government Surveillance Coalition (a group of global technology firms including Apple, Google, Facebook, Microsoft, LinkedIn and Twitter) have released a statement criticising the recently enacted Australian encryption-access legislation: *Telecommunications and Other Legislation Amendment (Assistance and Access) Act 2018*.

The group states that it 'has consistently opposed any government action that would undermine the cybersecurity, human rights, or the right to privacy of our users – unfortunately, the Assistance and Access Bill that was just passed through the Australian Parliament will do just that. The new Australian law is deeply flawed, overly broad, and lacking in adequate independent oversight over the new authorities. RGS urges the Australian Parliament to promptly address these flaws when it reconvenes'.

Government open to considering further amendments? Attorney General Christian Porter issued a statement, following the passage of the Bill on 6 December, stating that the Morrison government had agreed to consider Labor's proposed amendments in the New Year if any 'genuinely reflect the recommendations of the Parliamentary Joint Committee of Intelligence and Security'. The Bill was referred to the Parliamentary Joint Committee of Intelligence and Security (the Committee having already delivered its first report and recommendations on 5/12/2018) on the 6 December for report by 3 April 2018.

[Sources: Reform Governance Surveillance statement 07/12/2018; [registration required] The AFR 12/12/2018; Attorney General Christian Porter 06/12/2018; Telecommunications and Other Legislation Amendment (Assistance and Access) Bill 2018]

In Brief | AustralianSuper has released a statement advising that the accounts of about 11,000 AustralianSuper members have been the target of a security breach that occurred earlier in the year. Reportedly the fund 'does not believe there has been any misuse of the accounts' and 'All affected members have been contacted and the fund has reported this account activity to the Privacy Commissioner at the Office of the Australian Information Commissioner (OAIC)'.

[Sources: Australian Super media release 11/12/2018; Financial Standard 14/12/2018]

Conduct Risk

Room to improve? 35% of employees in Australian, NZ and UK workplaces say that they have been aware of misconduct during the past 12 months at work but only 65% say they would report it according to the latest IBE survey of employee attitudes to ethics in the workplace.

The Institute of Business Ethics (IBE) has released its latest survey of employee attitudes to ethics in the workplace.

Some key themes from the Australian, New Zealand and UK participants

A total of 2,268 employees in Australia, NZ and the UK were surveyed. IBE writes that the following common themes were distinguishable from the findings.

- **Organisations are perceived to be honest by most employees:** The majority of employees across all three countries (84% in NZ and 81% in Australia and the UK) said that their organisation acts with honesty.
- **Organisations with an ethics program in place are perceived to be more ethical by employees:** 85% of employees in organisations with a comprehensive ethics program said that their organisation acts responsibility in all its business dealings as compared with 54% in organisations with no ethics program.
- **13% of managers indicated that it is acceptable to artificially increase profits** in the books as long as no money is stolen and 34% of managers believe petty fiddling is inevitable in a modern organisation.
- **Line managers set a better example in organisations with ethics programs in place:** 83% of employees in organisations with an ethics program said that their line manager sets a good example of ethical business behaviour in comparison with 38% in organisations without ethics programs in place.
- **12% of participants reported feeling pressured to compromise their ethical standards** with time pressure the most common form of pressure mentioned.
- **35% if employees have been aware of misconduct during the past 12 months at work.** People treated inappropriately/unethically was the most frequently cited type (44%) of misconduct mentioned, followed by bullying/harassment (40%) and safety violations (34%).
- **Most employees would speak up:** 65% of employees across all three countries said that they would speak up about misconduct if they became aware of it. Employees in the UK were most likely to have reported misconduct (67%) followed by those in NZ (65%) and Australia (63%).
- **Employees are more likely to speak up about misconduct in organisations with an ethics program in place:** 79% of employees in organisations with a comprehensive ethics program who have been aware of misconduct spoke up as opposed to 32% of those in a similar position in an organisation with no ethics program.
- **22% of participants reported that they are incentivised to live up to ethical standards.** The most common incentive is including ethics in annual appraisals or performance reviews.

[Sources: Institute of Business Ethics: Ethics at work: 2018 survey of employees: Australia, New Zealand and United Kingdom; IBE Summary; Ethics at Work 2018 Survey of Employees Australia; FCPA blog 04/12/2018]

An ACTU survey has found nearly 64% of women and 34% of men have experienced sexual harassment at work

The Australian Council of Trade Unions (ACTU) has released the results of a survey of Australian workers which identified that a majority of women, and a third of men, have experienced harassment at work.

Some Key Points

- **More than half of all respondents (54.8%) had experienced sexual harassment** at their most recent workplace or at a previous workplace.
- **A majority (64%) of respondents had witnessed sexual harassment** at their most recent workplace or at a previous workplace. Of people who have witnessed harassment at work, nearly a quarter (23.6%) said the harassment they witness is frequent, 34.7% said it was either infrequent or rare and 41.7% described it as occasional.
- **Respondents had been harassed by a range of people**, including co-workers, customers or clients as well as supervisors, managers or senior co-workers. Most people – both male and female – who reported harassment were harassed by men. Respondents most commonly reported harassment from co-workers (36.9%) and supervisor/managers (20.9%) followed by more senior co-workers (16.9%), clients or customers (9.2%) and boss/employers (5.8%).
- **Respondents who had experienced sexual harassment had been subjected to a range of inappropriate behaviours**, including crude or offensive remarks, unwanted sexual attention, inappropriate sexual contact and sexual coercion.
- **Most employees who have experienced harassment do not make a formal complaint:** 27% of those who experienced sexual harassment made a formal complaint. The top three reasons for not making a formal complaint were: fear of retribution/negative consequences (55%), lack of faith in the complaints process (50%) and lack of confidence that the complaints process would be confidential (46.5%). Other reasons included not thinking the harassment was serious enough (28%) and being unaware of how the complaints process worked (8.7%) (among others).
- **70.4% of those who complained were unsatisfied or mostly unsatisfied with the complaints process:** Of those who pursued a formal complaint (27% of those who experienced harassment) 43% said that their complaint was ignored or not taken seriously; 25.8% said that they were treated less favourably because they had complained; and 12% said their employment was terminated, or they had left their job. Nearly half — 44.7% — of the group who'd experienced harassment said their harasser had suffered no consequences and 24.4% were not told of any complaint outcome. The most common consequence was a formal warning. 14.8% of those who lodged a formal complaint said that they felt satisfied or very satisfied with the process. 14.8% said that they were neither satisfied nor unsatisfied.
- **Better protection for complainants the number one way to improve the process:** 60.1% of respondents said that the complaint process could be improved by better protecting complainants from victimisation. Other measures to improve the process included: provision of more information and support for those experiencing sexual harassment (53.8%); better remedies for the complainant (47%); making the complaints process quicker (34.4%) and a stronger role for unions in the process (32.5%); other measures (33.6%).

About the survey:

- The report is based on responses from 9,600 people from a range of industries.
- The survey was conducted between 18 September and 30 November 2018.
- The majority (68%) of respondents were women, the remaining 31.5% were men.

[Source: ACTU survey: Sexual Harassment in Australian Workplaces: Survey Results]

Discrimination is still an issue in Irish workplaces according to a new study

The Matrix Workplace Equality Survey was conducted online in October 2018 among 1,019 people (60% female, 40% male) working across a broad range of industries and sectors in Ireland.

Among the survey findings were the following:

- 50% of women and 35% of men have experienced discrimination (in some form) in the workplace
- 21% of women and 12% of men reported experiencing sexual harassment in the workplace

- 44% of women (and 14% of men) reported having to tolerate sexist jokes and comments
- 69% of women (compared to just 29% of men) suggested that the glass ceiling is still in place.

[Source: The Matrix Workplace Equality Survey 2018]

Whistleblowing

The Royal Bank of Scotland has reportedly launched an investigation following whistleblower allegations of cultural issues at the lender

Reportedly, The Royal bank of Scotland (RBS) has launched an investigation following whistleblower allegations that harassment of staff eg alleged persistent intimidation, threats of job loss, pressure to act unethically and humiliation is 'rife' at the lender.

RBS is quoted as stating that it has not yet reached any conclusions but that the appropriate action will be taken if any of the allegations are substantiated. The lender also reportedly said that staff engagement scores across the bank are at the highest level since records began over a decade ago, with more than 90% of staff knowing how to raise concerns about employee wrongdoing or misconduct and agreeing that people are treated with respect regardless of their job.

[Source: itv news 10/12/2018]

Climate Risk

In Brief | The largest ever group of institutional investors (415 institutional investors with $32 trillion under management including some of the world's largest pension funds, asset managers and insurance companies) have signed the Global Investor Statement, calling on governments around the world to urgently increase their efforts to meet the Paris climate change agreement goals (including by committing to phasing out coal power). The agreement was signed during the COP24 conference(the 24th Conference of the Parties to the United Nations Framework Convention on Climate Change in Poland).

[Sources: UNEP media release 10/12/2018; The Investor Agenda media release 10/12/2018; 2018 Global Investor Statement to Governments on Climate Change; The Guardian 10/12/2018; Reuters 10/12/2018]

In Brief | The latest Climate Change Performance Index evaluating, comparing and ranking the climate protection performance of 56 countries and the EU (together responsible for more than 90% of global GHG emissions) in combatting climate change has ranked Australia 56th, putting it in the very low category with China, Canada, the US, the Republic of Korea and Saudi Arabia. Overall, the CCPI found that to implement the Paris Agreement, countries must raise their ambitions and enact concrete measures to make their individual contributions to the global goal.

[Sources: CCPI Index 2019; CCPI media release 10/12/2018]

Supply Chain Risk

Ansell has reportedly committed to various measures to mitigate supply chain risk following media reports of concerns relating to migrant workers employed by Malaysian glove suppliers

The ABC reports that in response to concerns raised relating to the conditions of migrant workers in a Malaysian factory that supplies gloves to Ansell, Ansell has said that it has:

- Introduced a mandatory standards framework for foreign worker recruitment and retention within the Ansell group which 'comprises of: a prohibition of confiscation of passports, provision of secure lockers for workers, safe travel to and from work, a ban on workers paying recruitment fees, a general requirement that salaries and benefits meet or exceed local and country laws; and improved hostel facilities, in addition to expanding safety and other training and onboarding for all workers'.
- Committed to undertaking other changes to 'further mitigate the risk of slavery and human trafficking in Ansell's business and within its supply chain', including by working with the Supplier Ethical Data

Exchange (Sedex) to begin third-party audits of its top-tier global suppliers (rather than relying on its suppliers doing their own self-assessment audits).

According to the ABC, Ansell has also confirmed that from next year, it will be reporting under the recently enacted *Modern Slavery Act 2018 (Cth)* and that by 2020 it will provide a public statement on what it uncovered in its supply chains.

[Source: The ABC 12/12/2018]

In Brief | The Federal Modern Slavery Act 2018 (Cth) received royal assent

[Sources: Modern Slavery Bill 2018 (Cth); Modern Slavery Act 2018 (Cth)]

Restructuring and Insolvency

Rule changes and additional funding announced to combat illegal phoenix activity

Assistant Treasurer Stuart Robert has announced changes to the Insolvency Practice Rules, which he said are designed to protect the interests of honest creditors, including trade creditors and employees. The new Rules will restrict the voting rights of certain creditors related to the phoenix company to ensure the interests of honest creditors are not affected by those complicit in illegal phoenix activity. More particularly, the Assistant Treasurer said that the changes would ensure that illegal 'phoenix operators and those who collude with them are unable to stack votes to the detriment of honest creditors'.

In addition, Mr Robert announced that the government will provide an additional $8.7 million over 4 years from 2018-19 to increase funding for the Assetless Administration Fund. The additional funding will increase the Australian Securities and Investments Commission's (ASIC's) ability to fund liquidators, who play a vital role in investigating and reporting illegal phoenix activity, including supporting the new liquidator avenues to recover assets lost through illegal asset stripping activity.

[Sources: Assistant Treasurer Stuart Robert 11/12/2018; Insolvency Practice Rules (Corporations) Amendment (Restricting Related Creditor Voting Rights) Rules 2018]

Corporate Misconduct and Liability

Prime Trust | The HCA has unanimously allowed (in part) ASIC's appeal against the Full Federal Court decision in the Prime Trust matter

The High Court has handed down its judgment in the appeals brought by the Australian Securities and Investments Commission (ASIC) against four former directors of Australian Property Custodian Holdings Pty Ltd (APCHL) (the responsible entity of the Prime Retirement and Aged Care Property Trust), Mr Bill Lewski, Dr Michael Wooldridge, Mr Mark Butler and Mr Kim Jaques.

High Court unanimously allowed, in part, four appeals from a decision of the Full Federal Court reinstating declarations made by the primary judge Murphy J in the Federal Court that Mr Lewski, Dr Wooldridge, Mr Butler and Mr Jaques each contravened the *Corporations Act 2001 (Cth)* (Corporations Act).

In a statement welcoming the decision, ASIC Commissioner John Price said that the result provides 'clear guidance' and clarification of principles. 'Directors who are officers of responsible entities have an obligation to scheme members to discharge their duties with care and diligence, not improperly use their position, comply with the law and act in the interests of investors. The matter also highlights the need for people in business to recognise they are custodians of other people's money' he said. He added that it demonstrates ASIC's willingness to 'take hard cases and litigate them through to superior Courts when needed. ASIC has the people, the powers and the desire to hold those engaged in misconduct to account' he said.

Facts

- APCHL was the responsible entity of the Prime retirement and Aged Care Property Trust (Prime Trust), a managed investment scheme which owned various retirement villages.

- On 19 July 2016, four directors (Mr Lewski, Dr Wooldridge, Mr Butler and Mr Jacques) met and resolved to amend Prime Trust's constitution to introduce, without any corresponding value to members, substantial new fees payable from assets of the scheme to APCHL (an entity owned by interests associated with Mr Lewski). The new fees included a 'listing fee' ($33m) payable upon listing of the scheme's units on the Australian Securities Exchange (ASX). The directors did not seek approval from unit holders of the Prime Trust in relation to the constitutional changes, or in respect of the payment of the listing fee.
- Subsequently, the APCHL board (including a fifth director Mr Clarke) met and resolved to lodge the amended constitution with ASIC. It was lodged the next day and would have become effective at that time (if valid).
- The $33m listing fee was later paid to companies associated with Mr Lewski.
- APCHL collapsed in 2010 when administrators were appointed owing investors approximately $550m.

Background

- ASIC commenced proceedings in 2012 in the Federal Court. As more than six years had elapsed since the 19 July 2006 meeting, ASIC was time-barred from bringing proceedings alleging breaches of the Corporations Act in relation to the decision to amend the constitution. ASIC instead alleged that APCHL (as the responsible entity) and the directors contravened the Corporations Act by resolving to lodge the amended constitution with ASIC, and by later acts effecting the payment of the fees.
- The primary judge found that APCHL and the directors had contravened numerous provisions of the Corporations Act (including the duties of care and skill, duties of loyalty, duties not to make improper use of a position and duties of compliance). Declarations of contravention were made, as were orders imposing pecuniary penalties on all five directors and periods of disqualification for four directors.
- The directors (but not APCHL) appealed to the Full Federal Court, which overturned the decision of the primary judge. The Full Court held that although the amendment resolution was invalid, the amendments had 'interim validity' once lodged with ASIC (until set aside) and that on this basis, the directors were entitled to act in accordance with the amended constitution that they honestly believed existed. Since the board had resolved on 19 July 2006 to amend the scheme constitution, then, 'absent dishonesty, there could be no contraventions arising from actions intended to give the amendments legal effect or actions to implement payments based upon the amendments. Effectively, any negligence, disloyalty, improper use of a position, or failure of compliance was spent'.
- ASIC then applied to the High Court for special leave to appeal, which was granted.

HCA decision

ASIC relied upon three grounds of appeal in the case of each of the four directors. ASIC argued that the Full Federal Court:

1. Erred in concluding that Pt 5C.3 of the *Corporations Act*, which includes s 601GC(1)(b), contains a concept of 'interim validity'.
2. Erred in finding that APCHL and the directors were not liable for the breaches of duty under ss 601FC and 601FD because they had an honest belief that the Constitution had been amended.
3. Erred in concluding that the onus lay upon ASIC to prove that the Listing Fee Payments were not authorised by the Constitution consistently with s 208(3).

ASIC was successful on the first two grounds of appeal. The High Court found that:

- **There is no concept of interim validity in the Corporations Act (Act)** which allows an unlawful amendment to a scheme constitution to take effect, upon its lodgement with ASIC, until it is set aside

by an order of the Court. The HCA found that the concept of interim validity relied upon by the Full Court is not supported by the text or protective purpose of s601GC.

- **The directors' 'honest belief' in the validity of the amendments to the constitution was not sufficient to absolve them of breaches of their duties under the Corporations Act.** The Court found that directors have a duty of loyalty to the members and must act in the members' interests and not make improper use of their position. 'The Loyalty Duty requiring a director to give priority to the members' interests in circumstances of conflict of interest…is not satisfied by an honest or reasonable belief. A contravention occurs when a director prioritises her or his own interests over those of the members, no matter how honest or reasonable the director was in doing so' the court found.
- **Members have a right to have a scheme administered according its constitution.** The Court found that the primary Judge was correct in finding that the relevant conduct by the directors had adversely affected members' rights and that the directors were required to consider this before resolving to lodge the amended scheme constitution. 'The primary judge correctly concluded that none of the Directors could reasonably have believed that it was in the best interests of the members to bring the Amendments into effect by the Lodgement Resolution or to make the accelerated Listing Fee Payments by the Payment Resolutions. His Honour also correctly concluded that the Directors should have voted against the Lodgement Resolution in order to prioritise the members' interests in having APCHL comply with the Constitution over the conflicting interest of APCHL in receiving the fees' the Court found.

The Court dismissed ASIC's ground of appeal relating to the operation of s208(3), finding that 'the Full Court was correct to conclude that in order for ASIC to prove that the Directors were involved in the contravention of s 208 by APCHL, ASIC needed to prove that the Directors knew that the Constitution did not authorise the Listing Fee. It did not do so'.

The matter will be remitted to the Federal Court to reassess the penalties and disqualification periods for each of the four directors, together with ASIC's cross appeals about the adequacy of the original penalties.

[Sources: ASIC media release 14/12/2018; High Court Summary; Australian Securities & Investments Commission v Lewski [2018] HCA 63; ASIC Key Matters: ASIC Prime Trust; [registration required] The Australian 14/12/2018; [registration required] The Age 14/12/2018; The SMH 13/12/2018]

ASIC has announced that the former CFO of Leighton Holdings has been found guilty of falsifying the company's accounts

The Australian Securities and Investments Commission (ASIC) has announced that the former CFO of Leighton Holdings Ltd (LHL) has been found guilty of criminal charges brought by ASIC, namely of engaging in conduct which resulted in the falsification of the firm's accounts in the District Court of NSW. More specifically ASIC states that he was found guilty of two counts of contravening section s1307(1) of the *Corporations Act 2001 (Cth)*.

The former managing director of LHL was found not guilty of one count of aiding and abetting the commission of an offence by the former CFO.

The former CFO will appear on bail before the District Court on 31 January 2019. The penalty for breaching s1307 is a fine of $11,000 or imprisonment for two years (or both). He may face up to 4 years or $22,000 fine (as he was found guilty of two counts of breaching the provision).

ASIC Commission John Price is quoted in the AFR as stating that the result represents a 'significant win' for ASIC and added that it is now 'very focused' on taking enforcement action. 'If you are in business and you get involved in corporate criminal activity, then you need to know that ASIC has the people, ASIC has the powers and ASIC has the very clear will to hold you to account' he reportedly said.

[Sources: ASIC media releases 11/12/2018; 31/01/2017; The New Daily 11/12/2018; The AFR 11/12/2018; 12/12/2018; The ABC 11/12/2018]

Other News

The government is consulting on the proposed structure and function of a Federal ICAC (Commonwealth Integrity Commission)

On 13 December 2018, the Australian Government announced that it will establish a Commonwealth Integrity Commission (CIC) to strengthen integrity arrangements across the federal public sector and issued a consultation paper outlining the proposed functions and structure of the CIC for consultation.

It's proposed that:

- The CIC will be established as an independent statutory agency, led by a commissioner and two deputy commissioners.
- The CIC will be comprised of two divisions:
  - a law enforcement integrity division (which will have the same functions and powers as the current Australian Commission for Law Enforcement Integrity, but with a broader jurisdiction) and;
  - a public sector integrity division (which will investigate alleged criminal corruption involving government departments and their staff, parliamentarians and their staff, the staff of federal judicial officers, and in appropriate circumstances, recipients of Commonwealth funds).

In a statement, Attorney General Christian Porter said that the proposed approach is designed to 'avoid the serious failings of state based integrity bodies' which have proven to be "kangaroo courts"' on some occasions. He added that the 'CIC will have the power to conduct public hearings only through its law enforcement division, the public sector integrity division will not have the power to make public findings of corruption. Instead, it will be tasked with investigating and referring potential criminal conduct to the Commonwealth Director of Public Prosecutions'. He said that this approach would ensure that it is 'the courts that make findings of criminally corrupt conduct'.

The deadline for submissions on the proposed structure and scope of the CIC is 1 February 2019.

The Australian reports that Labor leader, Bill Shorten, has criticised the government's plan on the basis that it 'is too limited in scope, too limited in power, and it has no transparency'. Mr Shorten also reportedly questioned the proposal to exempt current governments from any scrutiny by the new federal CIC, and the proposal to limit the scope of the CIC by preventing it from investigating of retrospective cases.

[Sources: Attorney General Christian Porter media release 13/12/2018; Consultation page; Consultation paper – A Commonwealth Integrity Commission – proposed reforms; The New Daily 13/12/2018; The AFR 13/12/2018; [registration required] The Australian 13/12/2018]