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In Brief | Further superannuation reform? The Australian labor party has announced that if elected it intends to enact further superannuation reform to address the gender superannuation gap. This includes a plan to add $400 million to the super balances of women in receipt of Commonwealth Paid Parental Leave entitlements (which will also ally to those receiving Dad and Partner Pay payments) and phasing out the $450 minimum monthly income threshold for eligibility for the superannuation guarantee. Industry Super Australia has reportedly welcomed the announcement as a positive start to closing the gap. 23

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Boards and Directors

In Brief | What should the limits of NED accountability be? The Australian reports that Chair of I-MED and CEDA Paul McClintock has expressed concern about the shifting expectations of non-executive directors in the wake of the Financial Services Royal Commission, cautioning that expectations need to remain 'realistic' or 'risk unravelling the board and management separation model'.

[Source: [registration required] The Australian 18/09/2018]

Remuneration

NAB has announced a new BEAR-compliant executive remuneration framework

National Australia Bank (NAB) has announced a 'new and simplified executive remuneration framework' for the NAB Group Chief Executive Officer and Executive Leadership Team (ELT). NAB writes that the new framework is compliant with the Banking Executive Accountability Regime (BEAR) and will apply to the current 2018 financial year and to future years.

Summary of changes

According to NAB's statement, changes to the remuneration framework include the following.

- **The replacement of short-term and long-term incentives with a single variable reward based on performance.**
- **Alignment to long-term performance through deferral in shares**: 40% of the variable reward will be paid in cash following the end of the financial year and the remaining 60% will be awarded in shares that will be deferred for at least four years (deferred shares). NAB states that for executives other than the CEO, this exceeds the level of deferral required by the Banking Executive Accountability Regime (BEAR).
- **Variable reward can be forfeited, further deferred or clawed back**: The whole variable reward (both cash and deferred shares) will be subject to clawback in certain circumstances. 'Upon resignation, dismissal for cause, failure to meet threshold conduct requirements, or if the Board determines that it should exercise its discretion, the executive will forfeit any entitlement to variable reward' NAB states. In addition, the board has the power to extend the deferral period beyond four years if it considers that circumstances warrant.

New reward structure by role

Under the new framework, the CEO's actual variable reward will be between zero and 300% of fixed remuneration, depending on business and individual performance. The CEO's 'at target' total reward is $7.94 million ($1.05 million or 11% less than in 2017).

For NAB's Chief Risk Officer and Chief Legal & Commercial Counsel, the actual variable reward will be between zero and 180% of fixed remuneration, depending on business and individual performance. The variable reward target will be 120% of fixed remuneration.

For other executives, the actual reward will be between zero and 255% of fixed remuneration, depending on business and individual performance, with the variable reward target being 170% of fixed remuneration.

Decrease in executive remuneration overall: NAB states that under the new framework, the aggregate 2018 ELT total reward at target levels (including CEO) has reduced by approximately 15% compared to 2017, including allowance for the value of dividends under the new framework. The CEO's 'at target' total reward is $7.94 million ($1.05 million or 11% less than in 2017).

Commenting on the new framework NAB Chair Dr Ken Henry said: 'The NAB Board is determined to drive customer focus at every level of the organisation. This lens needs to be considered alongside financial metrics when assessing executive performance if we are to deliver long-term, sustainable performance for shareholders. The new framework provides the right tools to assure performance. NAB is a complex business and the Board recognises it is important to attract, retain and reward skilled executives, while

remaining mindful of the quantum of executive remuneration. Where NAB falls short of customer, shareholder and community expectations, the new framework provides the Board with the ability to hold leaders accountable.'

Further detail on the new framework will be provided in NAB's Remuneration Report (to be available 16 November 2018).

Shareholder support?

NAB's announcement states that the new framework was developed based on detailed and ongoing engagement with investors, proxy advisors, regulators and executives, and taking into consideration NAB customer and community sentiment.

The AFR comments that when a single variable award structure was introduced by QBE Insurance last year, QBE received a first strike, though notes that NAB's new framework has 'received positive endorsement by shareholders and some proxy advisers'.

[Sources: NAB ASX Announcement 19/09/2018; [registration required] The FT 19/09/2018; The SMH 20/09/2018; [registration required] The AFR 19/09/2018]

Disclosure and Reporting

Climate Disclosure

Top Story | Worse than in 2011? ASIC Report 593 reminds directors (among other things) of their legal obligation to report on climate risk.

Overview: ASIC Report 593 Climate risk disclosure by Australia's listed companies

On 20 September, the Australian Securities and Investments Commission (ASIC) released: *Report 593 Climate risk disclosure by Australia's listed companies* setting out ASIC's high-level findings and recommendations for listed companies, following an ASIC review of disclosure practices in the market. Overall, ASIC found that outside of companies in the ASX 200, there was very limited climate risk disclosure by listed companies and that in some cases, the disclosure was non-specific and therefore of limited value to investors. The report also includes four high level recommendations relating to the consideration and disclosure of climate risk.

Key Findings

- **Larger companies were more likely to disclose climate risk across all forms of disclosure reviewed, including in annual reports, than smaller companies.**
  - Among the ASX 1-100: 40% of companies disclose climate risk as a material risk in the Operating and Financial Review (OFR) and 80% included it in their annual report.
  - For ASX 101-200 companies this dropped to 5% of companies including climate risk as a material risk in the OFR and 35% including it in their annual report.
  - For ASX 201-300 companies, 5% included climate as a material risk in the OFR and 30% included it in their annual report.
- **Companies appear less likely now, than in 2011, to include climate change content:** The report found that the percentage of annual reports containing 'climate change content' for the period 2011 to 2017 has actually decreased from 22% in 2011 to 14% in 2017. ASIC suggests that the 'higher rates of inclusion of "climate change content" in annual reports in the earlier part of this decade may be because of transition climate risk at that time in the form of legislative change under the Clean Energy Act 2011 (Cth)'.
- **Non-specific disclosure**: In relation to prospectuses ASIC found limited examples of companies explicitly citing and disclosing climate risk (either physical or transition) as a relevant risk factor. Of the 25 prospectuses reviewed:

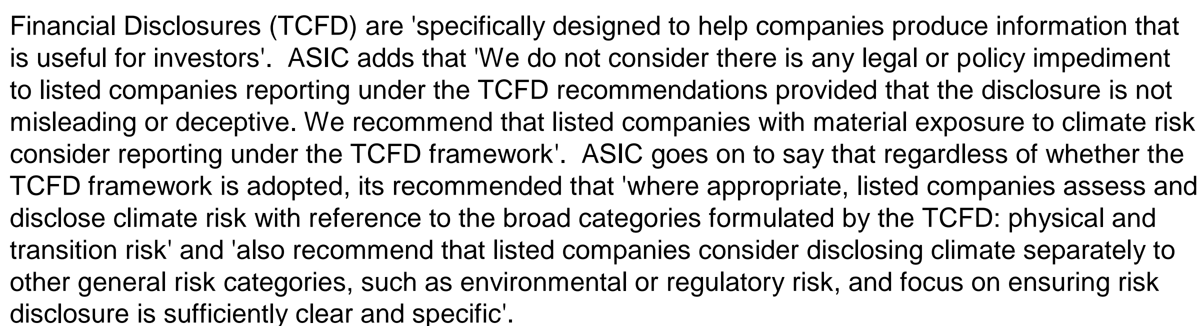
- In 'the majority of prospectuses reviewed' though both environmental and regulatory risks were generally cited as risks to the business model of the relevant company, 'there was insufficient detail disclosed to enable an investor to determine if climate risk formed part of those broader risk categories, and, if so, how and to what extent'.
- None of the prospectuses reviewed expressly identified any physical climate risks.
- One prospectus cited transition climate risk as a key risk, highlighting public concern around the issue of climate change and the possible impact of regulatory responses as a risk to the relevant company's business model. The relevant disclosure also explained how different regulatory responses may affect the company's operating and financial performance.

- **'Fragmented climate risk disclosure practices':** ASIC observed that lack of standard/consistent climate risk disclosure practices across the sample of disclosures reviewed, 'make comparisons difficult'. Fragmented climate risk disclosure practices make comparisons difficult.
- **A number listed companies intend to adopt the recommendations (either in full or in part) of the Task Force on Climate-related Financial Disclosures (TCFD).**

Commenting on the report findings, ASIC commissioner John Price said: 'Climate change is a foreseeable risk facing many listed companies in the Australian market in a range of different industries. Directors and officers of listed companies need to understand and continually reassess existing and emerging risks (including climate risk) that may affect the company's business – for better or for worse…We intend to monitor market practice as it continues to evolve and develop in this area.'

Key Recommendations

1. **Consider climate (and consider the TCFD final report):** 'Directors and senior managers of listed companies need to understand and continually reassess existing and emerging risks that may be applicable to the company's business, including climate risk. This should extend to both short-term and long-term risks' ASIC writes. In relation to the adoption of the TCFD recommendations, ASIC states that 'Regardless of whether a company follows the disclosure recommendations of the TCFD, we recommend that directors and senior managers consider the TCFD's final report which serves as a useful reference for climate risk and its assessment, governance and management'.
2. **Develop and maintain strong and effective corporate governance**: 'Strong and effective corporate governance helps in identifying, assessing and managing material risks. Strong corporate governance facilitates better information flow within a company and facilitates active and informed engagement and oversight by the board in identifying and managing risk. Transparency is one of the fundamental tenets of strong corporate governance. When climate risk is material, consideration should be given to disclosing the company's governance and risk management practices around climate risk' ASIC states.
3. **'Comply with the law'**
    - Directors of listed companies should carefully consider the requirements relating to OFR disclosure under s299A(1)(c) *Corporations Act 2001 (Cth)* ASIC writes. 'We consider that the law requires an OFR to include a discussion of climate risk when it could affect the entity's achievement of its financial performance or disclosed outcomes' the report states. In addition, referencing Regulatory Guide 247: Effective disclosure in an operating and financial review (Para 64) ASIC writes that 'directors should also consider the requirement to include any relevant analytical comments and specify how risk factors that are within the control of management will be managed'.
    - Preparers of disclosure documents should consider, ASIC writes, the relevant issuing company's exposure to climate risk as part of any due diligence process and, 'when that risk is material, the prospectus should disclose it in a clear, concise and effective way' (s710 Corporations Act 2001 (Cth) and Regulatory Guide 228: Prospectuses: effective disclosure for retail investors)
4. **Disclose useful information to investors — 'consider' adopting the TCFD framework:** ASIC states that the voluntary disclosure recommendations issued by the Task Force on Climate-related



Financial Disclosures (TCFD) are 'specifically designed to help companies produce information that is useful for investors'. ASIC adds that 'We do not consider there is any legal or policy impediment to listed companies reporting under the TCFD recommendations provided that the disclosure is not misleading or deceptive. We recommend that listed companies with material exposure to climate risk consider reporting under the TCFD framework'. ASIC goes on to say that regardless of whether the TCFD framework is adopted, its recommended that 'where appropriate, listed companies assess and disclose climate risk with reference to the broad categories formulated by the TCFD: physical and transition risk' and 'also recommend that listed companies consider disclosing climate separately to other general risk categories, such as environmental or regulatory risk, and focus on ensuring risk disclosure is sufficiently clear and specific'.

Investor Group of Climate Change (IGCC) has welcomed the release of the report

IGCC issued a statement welcoming the release of ASIC's report. IGCC CEO Emma Herd said: 'Financial regulators are clearly telling corporate Australia that they must report on climate change risk with the same level of rigour as any other financial risk. This report finds that currently they are not…Australian companies must lift their game when it comes to reporting on climate change risks, or they risk losing access to capital…This report shows that Australian companies have the policy and accounting frameworks they need to report on climate change risks in a meaningful way. With ASIC, APRA and the market calling for better reporting on climate change, it's time for Australia companies to step up.'

Context

- **Climate disclosure is a strategic priority for ASIC**: This review of climate disclosure was flagged in ASIC's latest report on Corporate Finance Regulation (ASIC Report 589) which identified climate as an area of focus (among others) for the regulator over the next six months, despite current regulatory uncertainty.

- **Review of regulatory guidance planned:** Report 589 also flagged that a review of relevant regulatory guidance is planned for release by the end of the year (see: Governance News 03/09/2018). In terms of the scope of the review of ASIC guidance, ASIC's strategic plan identifies the review of existing guidance in Regulatory Guide 170 Prospective Financial Information and Regulatory Guide 247 Effective disclosure in an operational and financial review. In addition, the strategic plan identifies as 'engagement with Treasury' on 'ASIC actions to address the government's response to the recommendations of the senate economics references committee report: Carbon Risk: A burning issue' as areas of focus.

[Note: MinterEllison has prepared a guide on climate risk disclosure to assist boards and their committees: The climate risk reporting journey: a corporate governance primer. See: ASIC's new focus on climate change risk disclosure - what does it mean for corporate boards?]

[Sources: ASIC media release 20/09/2018; ASIC Report 593 Climate risk disclosure by Australia's listed companies; IGCC media release 20/09/2018]

In Brief | The Hong Kong Securities and Futures Commission (SFC) has announced a new strategic framework to contribute to the development of green finance in Hong Kong. Among other things, the strategy states that 'Our top priority in green finance is to enhance listed companies' reporting of environmental information emphasising climate-related disclosure, taking into account the Mainland's policy direction to target mandatory environmental disclosure by 2020, and aiming to align with the TCFD recommendations'. The strategy states that amendments to the Listing Rules and other possible means to achieve this will be considered.

[Sources: SFC media release 21/09/2018; Strategic Framework for Green Finance]

Diversity Disclosure

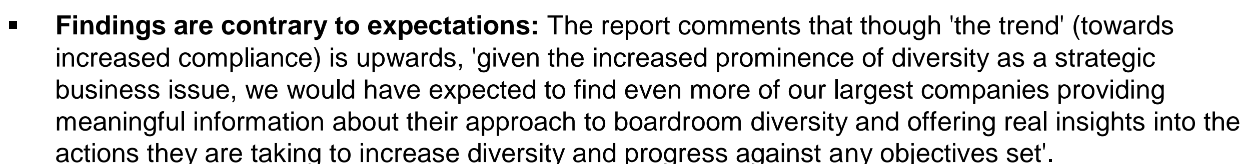
Room to improve: The UK FRC has called on the FTSE 350 to improve the quality of diversity reporting.

The UK Financial Reporting Council (FRC) has released the results of analysis, conducted by the University of Exeter Business School, into the current extent and manner of reporting by FTSE 350 companies on diversity at board and senior management levels in their annual reports.

The report found that there is a range of approaches to reporting, with a minority of companies providing 'best in class' detailed information in annual reports.

Key Points

- **Reporting as a 'driver of change'**: The report attributes progress towards improved diversity in part to diversity reporting, 'Transparency has been an important driver of this change' the report states.
- **FRC expectation that diversity is viewed, and reported on, as a strategic issue:** 'In order to maintain a competitive edge and success over the long-term, UK companies need to consider how diversity and inclusion is relevant to the specific circumstances of their business, the markets in which they operate, the workforce on which they rely and the customers and communities which they serve. These considerations should be built into companies' strategic plans for meeting their corporate aims' the FRC states.
- **Progress since the introduction of the diversity reporting requirement:** Overall, the quality of reporting on diversity was found to have improved since it was first included in the Corporate Governance Code in 2012. For example, in 2012 56 FTSE 100 companies reported that they had a board diversity policy, all of which focussed solely on gender diversity. In 2018. 98% of FTSE 100 and 88% of FTSE 250 companies have a board diversity policy and 33% of these refer to ethnicity as well as gender.
- **Quality of reporting against Provision B.2.4 of the Corporate Governance Code 2016 is mixed**: Provision B.2.4 of the UK Corporate Governance Code calls for 'A separate section of the annual report should describe the work of the nomination committee, including the process it has used in relation to board appointments. This section should include a description of the board's policy on diversity, including gender, any measurable objectives that it has set for implementing the policy, and progress on achieving the objectives'. The report found that:
  - 15% of the FTSE 100 discussed all four elements referenced in the Provision, while a further 20% discussed three of the four elements.
  - 6% of FTSE 250 companies discussed all four elements, while an additional 8% discussed three of the four. Over 60% discussed only two of the four elements.
- **Range of approaches to reporting:** Analysis of the annual reports of FTSE 350 companies revealed a range of approaches to diversity reporting with an estimated 20-30% of the FTSE 100 and 10% of the FTSE 250 demonstrating a 'best in class approach' . However, at the other end of the spectrum was a 'minimalistic, "tick box' approach". The majority of FTSE companies, the FRC writes, comply 'with the letter of the Code, but reporting tends to include boiler-plate commentary and suggests a lack of deeper understanding and commitment'.
- **Those companies categorised as 'best in class' in terms of the quality of their reporting**:
  - Demonstrate a 'maturity of approach to gender diversity' and have begun to consider how best to increase ethnic diversity. A number are increasingly discussing diversity as a much broader concept that encompasses a range of sources of difference, including social and educational background, disability and other 'protected characteristics'.
  - Are more likely view diversity as an issue of strategic importance and to link it to company strategy.
  - Set measurable objectives and are more knowledgeable about which initiatives are successful within their own organisations.



- **Findings are contrary to expectations:** The report comments that though 'the trend' (towards increased compliance) is upwards, 'given the increased prominence of diversity as a strategic business issue, we would have expected to find even more of our largest companies providing meaningful information about their approach to boardroom diversity and offering real insights into the actions they are taking to increase diversity and progress against any objectives set'.

Expectation that the quality of reporting will improve

The FRC states that its expectation is that the combination of reporting requirements under DTR 7.2.8A (the first annual reports prepared against this requirement were issued from March/April 2018 and fell outside the sample used for this report) and the 2018 Corporate Governance Code (which applies for accounting periods beginning 1 January 2019 onwards) will improve reporting quality going forward. 'The aim of the 2018 [Corporate Governance] Code in relation to diversity is for companies to deepen their understanding of how diversity can impact their business and encourage them to take a more strategic, multi-faceted approach to diversity and inclusion. We expect the combination of the new reporting requirements in DTR 7.2.8A and in the 2018 Code, to bring about a significant shift in the quality of diversity reporting and provide greater insight into how companies approach diversity in practice' the FRC writes.

About the survey: The sample of reports analysed included 54 reports from 2016 and 296 from 2017. The first annual reports prepared against the new diversity policy reporting requirement in DTR 7.2.8A were issued from March/April 2018 and therefore fell outside the sample used for this report.

[Source: UK Financial Reporting Council media release 17/09/2018; Board Diversity Reporting September 2018]

Other Developments

United States | Former CEO and company pay the price for non-disclosure of reputational risk: SeaWorld, its former CEO have agreed to pay more than $5m to resolve SEC fraud charges that they misled investors regarding the impact of the documentary Blackfish on Seaworld's reputation and business.

The Securities and Exchange Commission (SEC) has announced that SeaWorld Entertainment Inc and its former CEO have agreed to pay more than $5 million to settle SEC allegations that they misled investors about the impact of the documentary 'Blackfish' on the company's reputation and business.

The documentary was critical of SeaWorld's treatment of its orcas and received wide media attention as it became more widely distributed in 2013, SEC writes. SEC alleges that:

- From approximately December 2013 through to August 2014, SeaWorld Inc and former CEO James Atchison 'made untrue and misleading statements or omissions in SEC filings, earnings releases and calls, and other statements to the press regarding Blackfish's impact on the company's reputation and business'.
- According to the SEC's complaint, on 13 August 2014 when SeaWorld acknowledged that its declining attendance was partially due to negative publicity related to the documentary for the first time, it triggered a fall in SeaWorld's stock price, which SEC alleges caused a 'significant loss to shareholders.'
- The SEC's complaint, filed in federal court in New York, charges SeaWorld and former its former CEO with both:
  - violating antifraud provisions of the federal securities laws; and
  - with reporting violations.

Settlement: SEC writes that SeaWorld and its former CEO have agreed to settle the SEC's charges without admitting or denying the allegations, with SeaWorld paying a $4 million penalty and Mr Atchison paying over $1 million in penalty and disgorgement. SeaWorld's former vice president of communications, also agreed to settle a fraud charge and to pay disgorgement and prejudgment interest of approximately $100,000. SEC states that he was 'not assessed a penalty, reflecting his substantial assistance in the SEC's investigation'.

The settlements are subject to court approval.

Consequences of non-disclosure: Co-Director of the SEC Enforcement Division Steven Peikin is quoted as commenting: 'This case underscores the need for a company to provide investors with timely and accurate information that has an adverse impact on its business. SeaWorld described its reputation as one of its 'most important assets,' but it failed to evaluate and disclose the adverse impact Blackfish had on its business in a timely manner.'

SeaWorld response: The FT reports Seaworld has said that 'The Company is pleased to have resolved this matter and to continue to focus on delivering superior guest experiences, world-class animal care and rescuing animals in need'.

[Sources: SEC media release 18/09/2018; [registration required] The FT 19/09/2018]

In Brief | The US Department of Justice has reportedly submitted a 'voluntary request' concerning Tesla CEO Elon Musk's recent announcement of plans to take the company private. Noting that SEC has also launched a separate civil investigation into Mr Musk's statements, The FT comments that the DOJ's request is the most 'significant escalation' of the government's scrutiny of Mr Musk's statement and suggests that it is a further setback for Tesla in the wake of a number of senior executive departures.

[Note: Mr Musk's plan to take the company private was made via Twitter last month, reportedly triggering an upswing in Tesla's share price. Media reports at the time reported that the US Securities and Exchange Commission had contacted Tesla to inquire about the accuracy of Mr Musk's tweet and why the announcement was not made in a regulatory filing. See: Governance News 13/08/2018, 27/08/2018]

[Source: [registration required] The FT 19/09/2018]

Regulators

Australian Securities and Investments Commission (ASIC)

Design and distribution obligations in relation to financial products: *The Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018* introduced.

Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 was introduced in the House of Representatives on 20 September. The Bill appears to be similar to the exposure draft released for consultation on 20 July 2018.

[Note: The Bill has been introduced following initial consultation on exposure draft legislation relating to the design and distribution of financial products and ASIC product intervention powers (See: Governance News 15/01/2018), and a second consultation on a revised draft (see: Governance News 23/07/2018)]

The Bill has been referred to the Senate Economics Legislation Committee for inquiry and report by 9 November 2018.

Key Points

- **Introduce design and distribution obligations**
  - Schedule 1 to the Bill proposes to amend the *Corporations Act 2001* (Cth) (Corporations Act) to introduce design and distribution obligations in relation to financial products. The Bill sets out: the new obligations; the products in relation to which the obligations apply; ASIC's powers to enforce the obligations; and the consequences of failing to comply with the obligations.
  - According to the explanatory memorandum, the new obligations will 'improve consumer outcomes by ensuring that financial services providers appropriately promote the provision of suitable financial products to consumers have a customer-centric approach to making initial offerings of those products'.

- The new obligations will 'generally apply' to products about which the offeror must make disclosure under the Corporations Act 'products that require a disclosure document, such as a product disclosure statement or prospectus'.
- There are some exceptions to this. These include 'exceptions for products and distribution methods, where there are existing similar regimes or other competing policy priorities' eg MySuper products, margin lending facilities, securities issued under an employee share scheme and fully paid ordinary shares. In addition, the new regime does not apply to financial products offered by an exempt body or an exempt public authority.
- Date of effect: Two years after the Bill receives the Royal Assent.

- **Product intervention power**: Schedule 2 will amend the Corporations Act and the Credit Act to introduce a product intervention power for the Australian Securities and Investments Commission (ASIC) to prevent or respond to significant consumer detriment. It sets out: the new power and when it can be exercised; the range of products which can be subject to the power; ASIC's obligations when exercising the power; and the consequences for failing to comply with an ASIC order. Schedule two will commence the day after the Bill receives the Royal Assent.
- **Penalties:** A contravention of every obligation in the new regime is both a civil penalty provision and an offence. 'This allows the regulator or prosecutor (as the case may be) to take a proportional approach to the enforcement of the new regime' the explanatory memorandum states.

[Sources: Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018; Explanatory Memorandum]

Competition added to ASIC mandate, removal of requirement to engage staff under PSA: Treasurer Josh Frydenberg has welcomed the passage of *Treasury Laws Amendment (Enhancing ASIC's Capabilities) Bill 2018*

Treasurer Josh Frydenberg has issued a statement welcoming the passage of *Treasury Laws Amendment (Enhancing ASIC's Capabilities) Bill 2018*.

The Bill will amend the *Australian Securities and Investments Commission (ASIC) Act* 2001(Cth) to:

- Require ASIC to consider the effects that the performance of its functions and the exercise of its powers will have on competition in the financial systems. The explanatory memorandum notes that this implements recommendation 30 made by the Financial System Inquiry to add competition to ASIC's mandate which was accepted by the government in October 2015.
- Allows ASIC to employ staff outside of the *Public Service Act 1999 (Cth)* (PSA) effective 1 July 2019.

Treasurer Josh Frydenberg has welcomed the passage of the legislation.

- Commenting on the removal of the requirement to engage staff under the PSA, Mr Frydenberg said it would allow ASIC 'to compete more effectively for suitable staff. It will also allow ASIC to tailor management and staffing arrangements to suit its needs, ensuring it is fit for purpose to deliver effectively on its mandate'. He added that the change would align ASIC with the Australian Prudential Regulation Authority (APRA) and the Reserve Bank of Australia (RBA).
- Commenting on the addition of competition to ASIC's mandate (the requirement that ASIC consider the effects that the performance of its functions and the exercise of its powers will have on competition in the financial system) Mr Frydenberg said that competition is 'critical in improving the performance of the financial system. It ensures that both consumers and investors get value for money in the in financial products and services they use. This Bill enacts key recommendations from the Financial System Inquiry and the ASIC Capability Review. It is further evidence of this Government's commitment to strengthening ASIC, to ensure the financial system delivers fair and optimal outcomes for all Australians'.

[Sources: Treasury Laws Amendment (Enhancing ASIC's Capabilities) Bill 2018; Explanatory Memorandum; Treasurer Josh Frydenberg media release 18/09/2018]

In Brief | Deadline to join AFCA was 21 September: ASIC issued a final 'warning' to financial firms (Australian financial services licensees, Australian credit licensees, authorised credit representatives and superannuation trustees) to join AFCA before the deadline, cautioning that 'Financial firms who do not do this will be in breach of the law'. ASIC writes that although it is finalising an instrument to enable firms to notify ASIC about their AFCA membership details over an extended period 'This does not extend the period for joining AFCA'.

[Source: ASIC media release 20/09/2018]

In Brief | Treasurer Josh Frydenberg has announced that Peter Kell has resigned as a Deputy Chair of ASIC after seven years of service, effective 6 December 2018. 'The Coalition Government thanks Mr Kell for his contribution to ASIC and wishes him well in his future endeavours' the Treasurer said.

[Source: Treasurer Josh Frydenberg media release 18/09/2018]

Australian Prudential Regulation Authority (APRA)

In Brief | Treasurer Josh Frydenberg has announced the appointment of Mr John Lonsdale as a full-time member and second Deputy Chair to the Australian Prudential Regulation Authority (APRA) for a period of 5 years. 'A second Deputy Chair will add experience to APRA's Board, with Mr Lonsdale's appointment ensuring a strong blend of supervisory experience, industry knowledge and policy expertise within its Executive Group' he said in a statement.

[Source: APRA media release 18/09/2018]

Corporate Social Responsibility and Sustainability

In Brief | Has the expectation of an ethical/responsible approach to investing moved from a niche market to the mainstream? RIAA's Responsible Investment New Zealand Consumer Survey 2018 has found 71% of the NZ public expect their funds to be invested ethically and 62% said that they are also ready to shift their funds if company practices are inconsistent with their values.

[Sources: RIAA media release 18/09/2018; Factsheet: Responsible Investment New Zealand Consumer Survey 2018; Report: Responsible Investment New Zealand Consumer Survey 2018]

Financial Services

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

Royal Commission hearings Round 6 Insurance hearings: overview of week 2 life insurance and general insurance case studies

Royal Commission Round 6: week 2, 17 September 2018 – 21 September 2018

Carrying on from week 1, the second week of Round 6 hearings into Insurance again focussed on the topic of Life Insurance before moving on to consider the topics of general insurance and the regulatory regime.

A high level overview of some of the issues to arise in the CommInsure, TAL and REST and AMP case studies (life insurance) and the issues identified for investigation by Senior Counsel Assisting Rowena Orr QC in relation to general insurance is below.

[Note: The remaining Round 6 case studies/possible open findings will be included in a separate post, in the next issue of Governance News.]

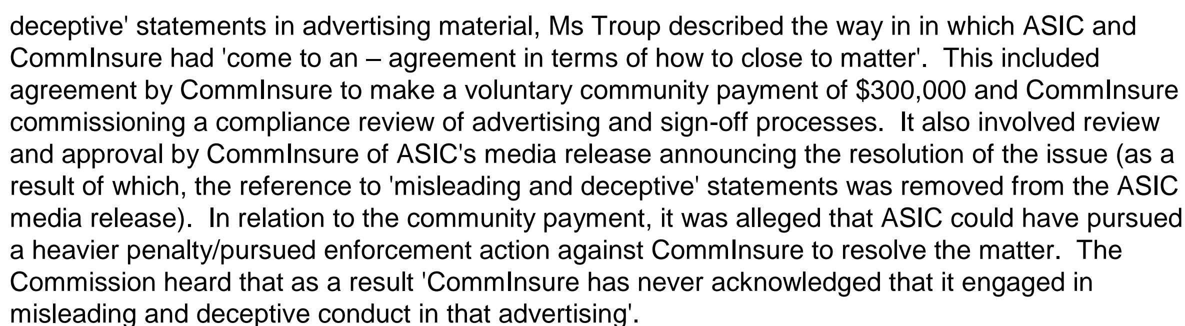
CommInsure Case study

In her opening statement to the Commission, Counsel Assisting Rowena Orr QC said that the focus of this case study would be on issues connected with policy design and the claims handling process. The primary focus was on two claims involving the definitions of 'heart attack' and 'radical surgery' (for breast cancer) in

trauma policies issued by CommInsure, which were relied on by to reject or to partially reject, customers' claims for full payment under their policies for these conditions.

Questions were asked in relation to the following issues (among others): the time taken to update definitions and the review/update process; the clarity of communication to customers regarding cover in advertising material; the approach by CommInsure to dealing with the claims in these two instances and with the subsequent complaints to Financial Ombudsman Service (FOS); and the way in which CommInsure approached engaging with the FOS and also with the regulator (the Australian Securities and Investments Commission (ASIC)). An overview of some of these issues in the context of the first claim (heart attack) is below.

- **Delay in updating policy definitions:** The first claim investigated by the Commission involved the denial of the full trauma payment to one customer (the insured) on the basis that his heart attack did not meet CommInsure's policy definition of 'heart attack' contrary to medical opinion supplied by the Insured, and contrary to CommInsure's knowledge that the definition did not meet the accepted medical definition of heart attack for two years prior to his claim. The Commission heard that the heart attack definition had not been updated by CommInsure for 11 years, and that and the decision to update it (following media reports raising concerns about the definition) as well as decisions concerning when the backdated revised definition should apply, were prompted in part by commercial considerations. The Commission also heard that ASIC had raised concerns. Commenting on the use of outdated definitions by CommInsure, Senior Counsel Assisting Rowena Orr QC said that 'ASIC considers, and we agree, that reliance on outdated definitions is clearly out of step with community expectations. The community expects that medical definitions in life insurance policies will appropriately reflect the community's understanding of what constitutes a particular medical definition…As we've heard in relation to CommInsure, the evidence suggests that those expectations have not always been met'.
- **Issues with outdated definitions not unique to CommInsure:** Ms Orr said that 'this issue [outdated definitions] is not unique to CommInsure'. Based on submissions from the ten entities (Auto & General, CommInsure, Greenstone, MLC, OnePath, Suncorp, Westpac and Zurich, as well as Freedom and ClearView) supplied to the Commission, Ms Orr said that 'eight of the 10 accepted that there had been deficiencies in their processes'. Ms Orr added that a 'central theme was the lack of procedures to ensure regular and formal reviews'.
- **Approach to engaging with FOS:** The claim eventually became the subject of an Financial Ombudsman Service (FOS) complaint, and the Commission heard in detail how this process played out, with a number of questions focussing on CommInsure's conduct in engaging with FOS. The Commission heard that CommInsure challenged the jurisdiction of the FOS to hear the complaint and elected not supply certain information in response to CommInsure's requests. FOS raised a number of concerns with CommInsure concerning this, including that it had 'caused significant delay in the handling of the investigation, it hampered the timely resolution of the matter for the applicant, had the potential to prejudice the outcome of the dispute' and may amount to 'serious misconduct as defined in paragraph 11.3 of the FOS terms of reference' which CommInsure resisted. Unsatisfied with CommInsure's response, the issues were referred by the FOS to ASIC for further investigation and resolution as part of ASIC's broader investigation into issues concerning life insurance claims handling at CommInsure.
- **CommInsure's advertising and promotion of heart attack cover:** A number of questions also concerned CommInsure's advertising and promotion of heart attack cover. Counsel Assisting noted that ASIC has raised concerns that certain 'advertisements were misleading and deceptive, and that by those advertisements, CMLA [CommInsure] was also breaching its obligation to act in the utmost good faith in section 13 of the Insurance Contracts Act' as no indication was given that only some heart attacks were covered in the advertisements. Asked whether she accepted that certain advertisements were 'misleading' to consumers about the coverage of trauma policies for heart attacks, Ms Troup agreed that this was the case.
- **Engagement with ASIC/ASIC's approach to enforcement:** A number of questions in relation to the heart attack claim also concerned the approach taken by CommInsure to engagement with ASIC and more particularly, CommInsure's continued defence of its position. ASIC's approach to enforcement was also questioned. In relation to engaging with ASIC on the issue of 'misleading and



deceptive' statements in advertising material, Ms Troup described the way in in which ASIC and CommInsure had 'come to an – agreement in terms of how to close to matter'. This included agreement by CommInsure to make a voluntary community payment of $300,000 and CommInsure commissioning a compliance review of advertising and sign-off processes. It also involved review and approval by CommInsure of ASIC's media release announcing the resolution of the issue (as a result of which, the reference to 'misleading and deceptive' statements was removed from the ASIC media release). In relation to the community payment, it was alleged that ASIC could have pursued a heavier penalty/pursued enforcement action against CommInsure to resolve the matter. The Commission heard that as a result 'CommInsure has never acknowledged that it engaged in misleading and deceptive conduct in that advertising'.

- **ASIC's approach to engagement:** Counsel Assisting referenced part of an email from ASIC to CommInsure which said: 'Could you [CommInsure] please consider and let us know whether this is sufficient for CommInsure to resolve the matter, including by way of payment of the community benefit payment in the absence of infringement notices'. Commissioner Hayne then asked Ms Troup understood by 'Let us know whether this is sufficient for CommInsure to resolve?' to which she responded 'I think it was the two organisations resolving the matter that was satisfactory for both companies'. Commissioner Hayne said: 'The regulator asking the regulated whether the proposal was sufficient in the eyes of the party alleged to have broken the law. Is that right?' Ms Troup said: 'I guess in terms of we could have taken an approach of continuing to defend our position, and so this was the alternative'.

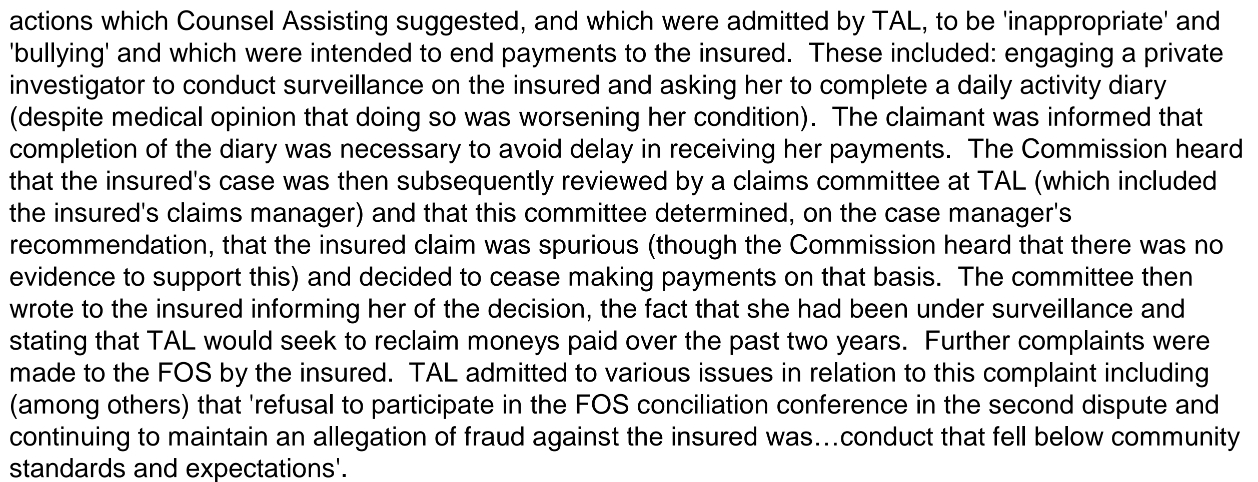
TAL case study

In her opening statement to the Commission Counsel Assisting Rowena Orr QC highlighted that a key question for consideration in this round of hearings would be 'what changes to the existing regulatory framework are necessary to improve the experiences of people with mental illness in dealing with life insurance companies'. She also noted that the treatment of mental health and of pre-existing medical considerations was raised as a concern in a number of public submissions and by beyondblue and the Public Interest Advocacy Centre (PIAC). See: Governance News 17/09/2018]

A central area of focus in this case study, was the treatment by TAL of a customer who made a claim for income protection on the basis of 'general anxiety disorder'. A high level outline of some of the issues in relation to this is below.

Income protection claim for 'general anxiety disorder'

- **Denial of claim based on undisclosed condition:** The claim considered the case of a nurse (the insured) who made a claim under her TAL income protection policy for 'generalised anxiety disorder' caused by workplace stress. The Commission heard that the insured's claim was supported by her doctor who found that her condition was a 'new onset illness' as distinct exacerbation of an existing condition. Upon receipt of the claim, the Commission heard that a TAL case manager undertook a 'general review', as the claim was categorised as 'high risk'. As a consequence of this, the insured was informed by letter that her case had been referred to the TAL legal team for investigation and potential remedies on the basis that she had a history of work-related stress. TAL's conclusion was based on her two visits to the employee assistance program (which the Commission heard were unrelated to employment-based stress). The Commission heard that the insured challenged this decision, and that eventually the claim became the subject of an FOS complaint. The FOS found in favour of the insured on the basis that her isolated instances of stress did not need to be disclosed to TAL when she took out the policy and were unrelated to her later anxiety disorder. TAL rejected the FOS' initial recommendations and the FOS then made a determination in the insured's favour requiring that TAL complete the assessment of her claim, and that any outstanding premiums should be deducted from any payment made should the assessment by successful. Contrary to this, TAL required the nurse to pay $2215 in outstanding premiums for reinstatement of her policy before reassessing her claim. FOS then wrote to TAL saying that the proposed approach appeared to be in breach of its direction. The Commission heard that the claim took over three years (from the initial claim being lodged) to be accepted.
- **Attempts to end the payments (use of surveillance):** Following acceptance of the claim, and the commencement of monthly payments, the Commission heard that a TAL case manager took various



actions which Counsel Assisting suggested, and which were admitted by TAL, to be 'inappropriate' and 'bullying' and which were intended to end payments to the insured. These included: engaging a private investigator to conduct surveillance on the insured and asking her to complete a daily activity diary (despite medical opinion that doing so was worsening her condition). The claimant was informed that completion of the diary was necessary to avoid delay in receiving her payments. The Commission heard that the insured's case was then subsequently reviewed by a claims committee at TAL (which included the insured's claims manager) and that this committee determined, on the case manager's recommendation, that the insured claim was spurious (though the Commission heard that there was no evidence to support this) and decided to cease making payments on that basis. The committee then wrote to the insured informing her of the decision, the fact that she had been under surveillance and stating that TAL would seek to reclaim moneys paid over the past two years. Further complaints were made to the FOS by the insured. TAL admitted to various issues in relation to this complaint including (among others) that 'refusal to participate in the FOS conciliation conference in the second dispute and continuing to maintain an allegation of fraud against the insured was…conduct that fell below community standards and expectations'.

In addition, Counsel Assisting asked a number of questions in relation to the incentives paid to case managers for ending claims including detailed questions about the key performance indicators (KPIs) used to assess case manager performance and the percentage of KPIs linked to ending payments/closing claims to which the witness was unable to give detailed responses. Questions were also asked about the adequacy of oversight of the claims manager involved in the claim. Counsel Assisting also alleged that the claim was indicative of broader cultural issues at TAL 'that the misconduct…admitted in connection with this claim is attributable to a culture within TAL that endorses and encourages attempts to limit TALs liability to pay out under claims'. This was rejected by TAL on the basis that 'this is one individual claim. And it does not happen to all our claims'.

Broader issue: use of surveillance in mental health claims

Counsel Assisting provided a summary of the information received by the Commission in relation to the use of surveillance by ten entities from 1 July 2013 to 30 June 2018. Among other things, MS Orr said made the following observations.

- **Surveillance more likely to be used in mental health claims:** Throughout the relevant period of the last five years, insurers more regularly engaged in surveillance activities in connection with mental health claims than in connection with physical health claims. Of the 10 entities from which the Commission sought statements, surveillance activities occurred in mental health claims more than twice as frequently as in physical claims.
- **Impact of the Insurance Code of Practice**: MS Orr said that according to the data, since 1 July 2016, the number of claims in which surveillance has been used has decreased significantly. She said that it was likely that this is due to the 'influence' of the Life Insurance Code of Practice, which obliges insures to use other methods of verifying information before arranging surveillance and places a number of limitations on the use of surveillance.

Provision of life insurance through superannuation: REST and AMP case studies

In her opening statement, Ms Orr Said that the REST and AMP case studies would consider issues connected with the provision of group life insurance policies through superannuation including: the design of the products and the role of superannuation trustees in the claims handling process.

REST case study

This case study largely concerned the case of a REST member who suffered a total and permanent disability (TPD) (she became a paraplegic) and made a claim under TPD cover held through the fund (with AIA). The claim was made five days after her insurance cover ended (due to exclusions in her cover, in this case because she had been out of work for 71 days and because her balance was below a minimum stated threshold) and the insurer notified the member that the claim was declined. The Commission heard that because REST was unaware that she had ceased her employment, the member had continued to pay insurance premiums with the result that at the time she was injured, she was paying premiums for a policy on which the insurer found, she was ineligible to claim. Instead, she was found to be entitled to a partial refund

of her premiums. The claim eventually proceeded to the Supreme Court of NSW before it was eventually settled with the member.

Role of the trustee in the claims handling process: One of the lines of questioning pursued by Counsel Assisting concerned the role of REST as trustee, in the process of handling complaints. Counsel Assisting asked AMP witness Lachlan Ross, 'what I'm trying to understand is what REST conceives its role as being. Are you an intermediary between the two [the insurer and the insured/member], are you there to fight for the member, or are you there to defend the insurance policy on behalf of the insurer?'. Mr Lachlan responded: 'REST's view is that insurance is very valuable to its membership. And ultimately, it's REST that has made the decision to provide this benefit to its members. And it works very hard to make sure that any benefits that a member is entitled to are paid to the member', he went on to say that 'It [REST] works with the insurer and in RESTs case we have an administrator, an external administrator to design the claims process and monitor claims, make sure that any benefits members are entitled to are paid'. More specifically, in relation to the claim described above, Counsel Assisting questioned whether 'at any point REST failed to act in the best interests of this member?' to which Mr Ross replied that 'With hindsight, I wish we had done more… I wish we could have got the benefit to the member sooner because REST is only interested in providing benefits to members who are entitled to them'. Counsel Assisting also questioned whether the 'mistakes' made in relation to the handling of the claim were 'preventable due to record keeping' which Mr Ross agreed was the case.

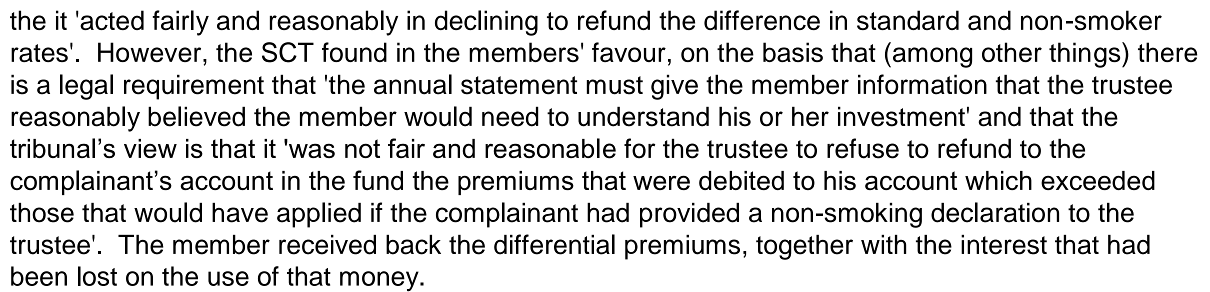
Value of cover/REST systems: On a separate issue, Counsel Assisting questioned the value of income protection cover, offered through REST, for unemployed members given that 'under the REST group life policy, an income protection benefit is payable, and when it is payable, it's calculated by reference to the member's pre-disability income' ie if the pre-disability income is nil, 'necessarily the income protection benefit is nil'. The Commission also heard that REST does not have a process in place to detect whether members are employed beyond being notified by the employer, with the result that unemployed members (whose employers had not informed REST) would continue to be charged income protection insurance. Asked whether in these circumstances 'that the income protection insurance becomes a junk insurance product' Mr Ross said that he did not believe that it is.

Universal definitions: Counsel Assisting questioned whether Mr Ross saw any value in there being universal definitions for group life policies for key terms and exclusions, to which Mr Ross responded 'I think theoretically, yes, would be my answer to that. But how that would work in practice, I don't know. But I think there is merit to that in theory, yes'.

AMP case study

Among the issues considered in this case study were: a complaint in relation to charging a non-smoker a higher premium and continued payment by deceased members of insurance premiums.

- **Non-Smoker complaint:** One issue investigated in this case study, concerned a complaint received by AMP from a member who had been charged at a higher premium (alleged smoker rate) for his insurance for the period 2005-2013 because he did not provide AMP with a non-smoking declaration at the time he transferred from coverage via his employer to a new policy. The complaint was made on the basis that he was a non-smoker, and had not received enough notice of the option to make the declaration/pay the lower premium. He requested a reimbursement of the additional premiums, which the Commission heard amounted to approximately $72,000. The Commission heard that in the absence of evidence to the contrary, AMP members were (allegedly) assumed to be smokers and charged at the higher rate, despite ASIC's view in Report 529: Member experience of Superannuation that: 'Trustees should not presume that members smoke in determining their insurance premiums. There are low levels of smoking in the community, with only 14.5% of adults being daily smokers. In these circumstances, it is statistically appropriate to assume a person is not a smoker, in the absence of other information about that member or that group of members'. The Commission heard that an AMP internal assessment of the complaint and request for reimbursement, suggested that it was 'unethical' not to include smoker status in annual statements to members, rather than on one occasion by letter (upon entry). Asked whether he agreed that it was unethical, AMP witness John Sainsbury did not agree, but conceded that it would have been better if the annual statements did disclose the smoker status (the Commission later heard that in 2013 this change was made). When AMP declined to reimburse the member, a complaint was lodged with the Superannuation Complaints Tribunal (SCT), and AMP maintained its position that


the it 'acted fairly and reasonably in declining to refund the difference in standard and non-smoker rates'. However, the SCT found in the members' favour, on the basis that (among other things) there is a legal requirement that 'the annual statement must give the member information that the trustee reasonably believed the member would need to understand his or her investment' and that the tribunal's view is that it 'was not fair and reasonable for the trustee to refuse to refund to the complainant's account in the fund the premiums that were debited to his account which exceeded those that would have applied if the complainant had provided a non-smoking declaration to the trustee'. The member received back the differential premiums, together with the interest that had been lost on the use of that money.

- **Role of the trustee:** Among the issues raised with Mr Sainsbury by Counsel Assisting were a number of questions about how the AMP structure enables the trustee to act in the best interests of members, including in relation to the example above, given that the administrator was also representing the insurer. Counsel Assisting asked: 'is part of the problem here that AMP views these questions from the perspective of the insurer and not the perspective of the members who are paying for the insurance' and went on to ask 'I have asked you a question twice now expressly about the perspective of a trustee who is presumably advocating on behalf of the members and both occasions you have answered by reference to a consideration relevant only to the insurer'.
- **Timing of breach reporting/systems:** A second issues considered concerned the fact that AMP systems do not cease charging members upon notification of their death, but have been 'coded' to continue charging premiums, and then refund them, once the claim is finalised. The Commission heard that AMP had become aware of the issue in 2016, but has not yet reported the issue to either ASIC or APRA. The Commission also heard that AMP reported to ASIC this year, some instances in which premiums charged to deceased members had not been refunded, or where the amount of the refund was not correct. Counsel Assisting questioned whether continuing to charge premiums for group life insurance where the member had passed away was conduct falling below community standards and expectations, and whether the conduct was attributable at least in part to AMP's control systems – to which Mr Sainsbury agreed. Mr Sainsbury disagreed that AMP 'has not acted efficiently, honestly and fairly by continuing to charge premiums in those circumstances expectations' which Mr Sainsbury denied was the case on the basis of the fact that it was not AMP's 'stated practice'.

General Insurance

Further opening remarks introducing the topic of General Insurance

As flagged in her initial opening statement, Counsel Assisting Rowena Orr QC said that the case studies considered would examine issues relating to the way general insurance products are sold, how general insurance products are designed, and how claims are handled under general insurance policies (including cases deferred from round 4 of hearings concerning the experiences of people who have made claims under home insurance policies following natural disasters). More particularly, Ms Orr said that the hearings would focus on general insurance products that are sold to consumers, in particular, home insurance, travel insurance and add-on insurance. Finally, themes concerning the regulation of both life insurance and general insurance would be considered.

Ms Orr went on to provide an overview of the general insurance industry based in part on data that certain general insurance companies have provided to the Commission, summarised what consumers and consumer advocates have told the Commission about their experiences with general insurance and explained what ASIC, the Financial Ombudsman Service (FOS), and the General Insurance Code Governance Committee have told the Commission about their compliance roles in relation to general insurance.

Submissions received in preparation for this round of hearings.

In preparation for this round of hearings, Ms Orr said that the Commission sought witness statements from AAI, IAG, QBE, Allianz, and Youi, and from the three major banks that have general insurance businesses, CBA, ANZ and Westpac. The entities were asked to tell the Commission about how they design general insurance products; how they sell and promote general insurance products; how they handle claims under

general insurance policies; and how they remunerate the personnel involved in selling general insurance products and handling general insurance claims.

Sale of insurance/remuneration of personnel involved

Reverse Competition in sale of add-on insurance: Ms Orr noted that general has always been excluded from the conflicted remuneration provisions of part 7 of the Corporations Act which 'means that there is no limit on the amount that general insurance companies can pay in commissions in relation to the sale of general insurance products'. Ms Orr went on to say that this exclusion has led to what ASIC has termed 'reverse competition' in relation to the sale of add-on insurance products through intermediaries (eg through car dealers). Ms Orr explained that this refers to a situation where insurers compete on the price paid to car dealers in commissions to buy access to distribution channels, as opposed to competing on price or value of products offered to consumers. Ms Orr went on to say that in the financial years from 2013-2015 ASIC found that insurers paid more than $600m in upfront commissions to car yard intermediaries for the sale of add-on insurance products. In the same period, the insurers collected $1.6 billion in premiums from those products, and paid out only $144 million in claims.

In addition to this, Ms Orr also said that submissions provided information about other forms of monetary benefit given to AFSL licensees or AFSL representatives eg standard commissions calculated as a percentage of insurance premiums written, as well as profit share payments, additional commissions, and volume-based incentives and outlined the amounts paid by insurers.

Reasons for denying claims

The most common reasons why insurers denied claims were identified in submissions as including:

- **motor vehicle insurance claims**: a specific exclusion in the wording of the policy which prevented the claim being covered (eg where the claimed damage was found to result from lack of maintenance rather than being caused by an accident), non-disclosure by the claimant at the time of purchasing the policy, or because the customer did not meet a condition of the policy which related to the specific circumstances of the claim.
- **home and contents insurance claims**: claims were commonly denied because there was no coverage for the particular claimed event or item under the policy, or because a specific exclusion or exception in the wording of the policy prevented the claim from being covered (eg where the damage was found to be caused by wear and tear rather than by the claimed event.
- **travel insurance claims:** claims were commonly denied because there was no coverage for the claimed event or item under the policy, because a specific exclusion or exception in the policy prevented the claim being covered, or because the customer was unable to prove loss or ownership of the claimed item.

Decline rates

Ms Orr said that claims made under travel insurance policies are declined the most frequently (of all kinds of claims) with more than one in every 10 claims declined. Motor vehicle claims and home and contents claims were declined in full at a rate of .27% and 5.77% respectively.

Closure rates

Many of the problems associated with the handling of general insurance claims can arise after a decision about the claim has been made. Claims are closed most quickly in relation to travel insurance claims, averaging approximately 41.18 days after receipt of the claim. Claims made under motor vehicle and home and contents policies take significantly longer to resolve and are closed at approximately 64 and 65 days respectively.

Areas of concern raised in public submissions

Of the 8977 public submissions received by the Commission to 14 September, 620 were identified as relating to general insurance. Of these, the three most common types of general insurance policies referred to were: home and contents insurance; car insurance; and travel insurance.

- **Home and contents insurance – delays/refusals to pay out on policies:** The most common issues raised in the public submissions concerned claims handling processes. Many submissions referred to delays in handling insurance claims and refusals to pay out on insurance policies. The negative impact of ongoing delays in processing claims and undertaking repair work, use by insurers of third parties to undertake repairs, the selective use by insurers of assessors or reports from professionals, insurers' requiring that particular service providers be engaged to undertake repairs (and the associated delays/issues with repair quality) were areas of concern. In addition, Ms Orr said that a number of the public submissions related to the handling of insurance claims following natural disasters. Many of which raised similar claim handling concerns. Some also referred to pressure from insurers for policyholders to accept cash settlement payments which did not reflect the true cost of the damage or were substantially below the claim amount and which left organisation of repairs within the settlement amount to the consumer.
- **Travel Insurance — treatment of pre-existing conditions/denial of claims on the basis of pre-existing conditions**: The most common concerns in relation to travel insurance related to the treatment of pre-existing conditions, including charging high premiums to cover such conditions or a denial of claims on this basis.

Issues raised by consumer organisations

Concerns raised included the following.

- **Concerns in relation to the disclosure of policy terms:** CHOICE noted that long and complex terms and conditions in the product disclosure statements for insurance policies often result in consumers facing loopholes or exceptions that mean they don't receive the support that they expected from their insurance policy when they make a claim. CHOICE identified use of non-standard definitions as one contributor to a lack of understanding on the part of consumers about what they are covered for. The Financial Rights Legal Centre (FRLC) told the Commission that it commonly hears consumers complaining that they have been caught by the fine print of their insurance policies. It considers that disclosure documents are overly complex, long and ineffective in empowering consumers to make informed choices at the point of sale, and that rather than promoting consumer understanding, disclosures allow insurers to manage their liability and reduce claims' outcomes.
- **Concerns in relation to sales practices for general insurance:** The Financial Rights Legal Centre (FRLC) and the Consumer Action Law Centre (CALC) both told the Commission that general insurance sold under a no advice or general advice model results in the widespread selling of insurance that is unsuitable for the people buying it. CALC considers that this leads to poor outcomes for consumers who are provided with insufficient or inadequate information to inform their decision or to engage with the complexities of the products. The Financial Rights Legal Centre also told the Commission that this model leads to significant under-insurance as consumers are not fully informed about the limitations of their cover.
- **Claims handling:** Consumer Action said that many consumers are discouraged from making claims in the first place because of a fear that the claim would lead to an increased premium. It also said that the two stage internal dispute resolution processes adopted by general insurers can deter people from pursuing legitimate complaints as the complaint process is seen as laborious.
- **Sale of add-on insurance.** CALC told the Commission that these products are often expensive compared to insurance bought directly from an insurer, and that they are often low value. FRLC also raised concerns in relation to the selling practices for these products including keeping consumers captive until after a sales pitch is completed, using the cooling off period as a selling point, deliberately masking the cost of insurance in loan payments, and serious deficiencies in scripts used for sale of consumer credit insurance products.
- **The experience of clients in relation to national disasters:** The submission from the FRLC raised issues relating to the price of premiums for flood coverage. It expressed concern that events similar to the floods in 2011 are likely to occur again with significant numbers of properties uninsured for flood as a result of customers being unable to afford appropriate cover, being refused cover, or opting out of cover without appreciating the full extent of their risk.

ASIC enforcement actions in relation to general insurance.

ASIC told the Commission that it has taken action on 32 occasions since 1 January 2008 that it described as enforcement action against general insurers. Ms Orr then gave an overview of these actions. The actions included: issuing three sets of infringement notices in respect of misleading advertising of insurance products; the imposition of additional conditions on the licence of two insurers, the acceptance by ASIC of an enforceable undertaking from one entity in relation to the misconduct of sales people who had made misleading statements to consumers and sold unsuitable insurance policies; and 26 requests by ASIC for entities to take remedial action.

Financial Ombudsman Service (FOS)

FOS reported an increase in the number of general insurance disputes it received in the 2016 to ’17 year, up by 2612 disputes on the previous year, or approximately 38%. FOS accepted 8756 general insurance disputes in 2016 to ’17, accounting for approximately 35 per cent of all disputes accepted by FOS. FOS reported that the increase in general insurance disputes has been due to a continuation of industry specific issues, including higher claim numbers, organisational changes, and the impact of Tropical Cyclone Debbie.

FOS told the Commission that the periods with the highest number of accepted disputes have been linked to the occurrence of natural disasters, particularly during 2010 and 2011.

The main issue in these disputes was confusion over the extent of cover due to the various definitions of flood and storm.

Allianz case study

This case study was largely concerned with 'incorrect and misleading statements made by Allianz in relation to its travel insurance products and the compliance processes within Allianz' Ms Orr said.

The Commission heard that as part of a website redesign in 2015, the content on a website through which customers could purchase various forms of insurance, was also changed, but was not reviewed and approved by Allianz before it went live. A number of issues were then identified by Allianz a week after the website became accessible to the public. These included issues relating to disclosure of conditions not being sufficiently prominent/misleading and the absence of Corporations Act disclosures. During the period between December 2015 and May 2018, the Commission heard that Allianz undertook 'a series of reviews that either identified additional misleading content or confirmed the results of the previous reviews' and that during the period, the 'incorrect, misleading and deceptive content was accessible the public' on the website. Allianz did not consider taking 'the offending parts' of the website down during this period and did not make a report to ASIC during this period.

In addition, the Commission heard that Allianz had received advice, prior to the website redesign concerning issues in relation to advertising material. For example, prior to the website redesign, advice from MinterEllison had raised issues in relation to the use of the word 'unlimited' in advertising material, but the content was uploaded despite this.

The Commission heard that a breach report was made to ASIC in June of this year and that 'all the incorrect, misleading and deceptive statements' have now been removed from the website.

- **Delay in rectifying the breaches/reporting to ASIC:** A number of questions were asked by Counsel Assisting concerning the delay in addressing the issues identified on the website. Counsel Assisting alleged that insufficient priority was given to rectifying the issue — to 'protect the bottom line' — despite the fact that Allianz was 'contravening financial services laws' in not doing so. In addition, questions were asked concerning the decision not to alert ASIC to a potential breach as required by s912D *Corporations Act 2001 (Cth)* when the issues were identified (which Allianz witness Michael Winter agreed had been the wrong decision). A number of questions were also raised in relation to the accuracy of the breach report, Counsel Assisting alleging that it did not make full disclosure (because it omitted to identify all previous similar breaches).
- **Remediation:** The Commission heard that customers impacted have not yet been identified, but that ASIC data indicates that 'in excess of two million travel insurance policies' were sold during the period when the potentially incorrect or misleading content was on the website. The Commission

also heard that customers have not yet been remediated, but that Allianz is 'very close' to meeting with ASIC on remediation plan.

- **Oversight/Accountability:** Asked whether those involved in the 'failures to rectify the incorrect, misleading and deceptive content' had faced internal disciplinary consequences as a result of these issues, Mr Winter said that they had not.
- **Compliance processes more broadly within Allianz:** Chief Risk Officer Lori Callahan was also asked a series of questions concerning 'what is happening with this breach with regard to rectification of the issue itself, remediation of customers and then the strengthening of the controls to prevent it from happening again'. Counsel Assisting alleged Allianz has focused on technical or legal compliance' and that insufficient priority and resourcing had been given to the compliance function over a number of years. The Commission heard that Allianz is in the process of reviewing 'open matters' going back to 2012, and that 'a framework or a foundation' has been put in place to address historical compliance issues/strengthen compliance function and that Allianz is 'at the start of that process'. The Commissioner asked: 'Am I to take the burden of the evidence you have just given as an acknowledgement that Allianz does not now have adequate risk management systems?' to which MS Callahan agreed. A series of questions were also asked about two reports into the compliance function at Allianz including an independent report, completed by Deloitte (intended to be submitted to APRA). The Commission heard, that the report was critical of Allianz processes/systems, and that Ms Callahan requested that it be withdrawn. It was alleged that the reason for Ms Callahan's request was that the report contained statements that were inconsistent with statements to ASIC. Ms Callahan maintained that this was not her motivation. In addition, a number of questions were asked concerning the adequacy of breach reporting systems and the adequacy of risk and compliance functions.
- **Add-on insurance via car dealerships:** Another issue explored was 'add on' car insurance sold through car dealerships. Ms Callahan admitted that Allianz's conduct in this area is below community standards, as insurance was sold to many customers who would be unable to claim, or were sold excessive or otherwise unnecessary cover and that Allianz expects to remediate a number of customers. Ms Callahan admitted that was an indication of flaws in monitoring some of the distributors and underwriters that sell its insurance products. Ms Callahan also said that the company is already investing in improved surveillance and monitoring of its third party distributors.

IAG case study (Swann case study)

This case study concerned issues in relation to the sale of add-on insurance products sold through car and motorcycle dealerships and the remediation paid to customers, by Swann after ASIC raised concerns.

[Note: The action in question appears to be the action referenced in ASIC's 19 December media release.']

The Commission heard that IAG has since withdrawn from the market.

Among other issues, questions focused on: sales practices (training/oversight of those selling the products); the payment of incentives to car/motorcycle dealerships and their employees to sell the insurance products (the Commission alleged that this led to outcomes that were not always in the best interests of the customers); product design (the Commission heard that ASIC raised concerns); the approach IAG took to addressing concerns raised by ASIC and the approach taken by IAG to monitoring and oversight.

- **Value of add-on insurance products:** IAG witness Benjamin Bessell was asked to comment on whether add-on insurance products are 'of sufficient value to a sufficient number of consumers to warrant them being in the market?' Mr Bessell responded that 'if things like commissions are capped, product disclosure statements are more easily understood, some of the benefit periods are perhaps extended or even removed from a policy. I think there are a combination of factors there that would – would ensure there is greater value for a – for a consumer'.
- **General advice:** Asked to comment on the issue of giving general advice is problematic in ensuring consumers receive products suitable to their needs, Mr Bessell said 'I think it's an ongoing discussion within the industry, and will be an ongoing discussion for some time. I think the – the general advice and personal advice model has its place. Is it perfect? No, I don't think it is.'

[Sources: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry Round 6: 12 September 2018 – Draft Transcript for Day 52; 13 September 2018 – Draft Transcript for Day 53; 14 September 2018 – Draft Transcript for Day 54; 17 September 2018 – Draft Transcript for Day 55; 18 September 2018 – Draft Transcript for Day 56; 19 September 2018 – Draft Transcript for Day 57]

Other Developments

ASIC has announced that it has commenced civil penalty proceedings against Dover Financial and its sole director, Mr Terry McMaster in connect with Dover's Client Protection Policy.

The Australian Securities and Investments Commission (ASIC) has announced that it has commenced civil penalty proceedings against Dover Financial Advisers Pty Ltd (Dover) and its sole director, Mr Terry McMaster in connection with Dover's 'Client Protection Policy' (Protection Policy).

ASIC states that the proceeding is a continuation of its enforcement action in relation to Dover's Protection Policy which 'to date has resulted in the cancellation of Dover's AFS licence and Mr McMaster's permanent exit from the financial services industry'.

ASIC allegations

ASIC alleges that the Protection Policy was misleading and deceptive because it 'contained false and misleading representations as to the rights and protections available to clients'; 'created a significant imbalance in Dover's and its authorised representatives' rights and obligations compared to those of clients'; and 'sought to protect the interests of Dover and its authorised representatives by avoiding liability to clients for poor financial advice'.

ASIC also alleges that Mr McMaster was 'knowingly concerned' the alleged conduct, as sole director and the only responsible manager for the period in which the policy was in use, and as the Key Person on Dover's Australian Financial Services Licence.

Relief sought by ASIC

ASIC is seeking declarations that Dover and Mr McMaster contravened the financial services law; and pecuniary penalties against both Dover and Mr McMaster for those contraventions.

Relief against Dover

- Pursuant to s21 of the Federal Court of Australia Act 1976 (Cth) (Federal Court Act) or s 1101B(1)(a) of the Corporations Act 2001 (Cth) (Corporations Act), ASIC seeks declarations that Dover has contravened s 1041H of the Corporations Act, s 12DA(1) of the ASIC Act and s 12DB(1)(i) of the ASIC Act.
- Pursuant to s 12GBA(1)(a) of the ASIC Act, ASIC seeks orders that Dover pay pecuniary penalties in respect of its contraventions of s 12DB(1)(i) of the ASIC Act.

Relief against Mr Terrence McMaster

- Pursuant to s 21 of the Federal Court Act, ASIC seeks declarations that McMaster was knowingly concerned in Dover's contraventions of s 1041H of the Corporations Act, s 12DA(1) of the ASIC Act and s 12DB(1)(i) of the ASIC Act.
- Pursuant to s 12GBA(1)(e) of the ASIC Act, ASIC seeks orders that McMaster pay pecuniary penalties in respect of being knowingly concerned in Dover's contraventions of s 12DB(1)(i) of the ASIC Act.

[Sources: ASIC media release 17/09/2018; Concise statement; [registration required] The AFR 17/09/2018]

[Note: The closing statement Round 2 of the Financial Services Royal Commission hearings suggested that it would be open to the Commissioner to find (among other things) 'that Dover might have engaged in misconduct in the following ways. First, by engaging in misleading and deceptive conduct contrary to section 1041H of the Corporations Act or section 12DA of the ASIC Act in connection with the Dover Client Protection Policy. Second, contrary to section 912A(1)(c) of the Corporations Act, Dover failed to comply with financial services laws, namely, section 1041H of the Corporations Act and section 12DA of the ASIC

Act by its incorporation of the client protection policy into all contracts of the authorised representatives and their clients.]

[Source: Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry: 24 April 2018 – Final Transcript for Day 17]

Reported response by Mr McMaster

Unequal treatment? The ABC reports that Mr McMaster has questioned whether ASIC has been even-handed in its enforcement approach, suggesting that ASIC appears to have taken a lighter approach with the larger lenders, than has been applied in the case of Dover.

Regulator refused to engage? Independent Financial Adviser reports that Mr McMaster maintains that Dover requested that ASIC undertake an audit in 2016 and 'formally asked for an interim report and undertook to act on all findings in November 2016 but were told "no" by ASIC. We repeatedly asked for meetings throughout 2017 but again, we were repeatedly told "no" by ASIC.' According to Mr McMaster, Dover engaged five different law firms with experience in AFSL compliance to review its operations and none expressed concerns about the customer policy. 'Dover voluntarily provided two expert legal/compliance reports to ASIC in 2017, each of which indicated there was no problem with the CPP. ASIC did not respond. But we now know ASIC internally dismissed both the reports as incompetent. ASIC didn't tell Dover this. It would have been nice to know' he is quoted as saying.

[Sources: The ABC 18/09/2018; Independent Financial Adviser 18/09/2018]

In Brief | The AFR reports that ASIC has written to FinTech Australia cautioning that ASIC 'will consider regulatory action where appropriate' if fintech lenders fail remove unfair contract terms from their loan contracts as Prospa has done. Reportedly the clauses removed by Prospa were flagged as problematic in ASIC Report 565: Unfair contract terms and small business loans released in March.

[Source: [registration required] The AFR 19/09/2018]

In Brief | ASIC has extended to 30 September 2018, licensing relief for foreign financial services providers to allow them to provide financial services to Australian wholesale clients without needing to hold an Australian Financial Services Licence.

[Source: ASIC media release 21/09/2018]

In Brief | Further superannuation reform? The Australian labor party has announced that if elected it intends to enact further superannuation reform to address the gender superannuation gap. This includes a plan to add $400 million to the super balances of women in receipt of Commonwealth Paid Parental Leave entitlements (which will also ally to those receiving Dad and Partner Pay payments) and phasing out the $450 minimum monthly income threshold for eligibility for the superannuation guarantee. Industry Super Australia has reportedly welcomed the announcement as a positive start to closing the gap.

[Sources: Leader of the Australian Labor Party Bill Shorten media release 19/09/2018; Financial Standard 19/09/2018]

Risk Management

Supply Chain Risk

In Brief | The Federal Modern Slavery Bill passed the House of Representatives on 18 September and is now before the Senate.

[Source: Modern Slavery Bill 2018 (Cth)]

Whistleblowing

United States | The National Whistleblower Center has formally requested that SEC extend the public comment period for proposed changes to the rules governing the SEC Whistleblower Program over

concerns some of the proposals announced by the Commission (including the proposal to 'cap' payments') reflect the 'radically anti-whistleblower' policy positions of the US Chamber of Commerce.

The National Whistleblower Center (NWC), has issued a media release formally requesting the Securities Exchange Commission (SEC) to extend the public comment period for proposed changes to the rules governing the SEC Whistleblower Program, including (among others) proposals to enable the SEC to limit large whistleblower rewards and increase 'small' awards (see Governance News 09/07/2018.)

NWC writes that the request is based on SEC's failure to produce 15,877 emails and other documents it identified in response to a Freedom of Information Act (FOIA) request filed by the NWC. The NWC FOIA request sought documents related to 'lobbying efforts' by Wall Street firms and the Chamber of Commerce that (NWC alleges) gave rise to the SEC's proposed rules.

NWC explains that it is of the view that some of SEC's proposals, including the proposal to 'cap' whistleblower awards, reflect the 'radically anti-whistleblower position' (allegedly) held by the US Chamber of Commerce. NWC's statement expresses concern that 'the SEC is the first executive agency to endorse "caps" in a proposed rule, and based on the public comments of the Commissioners, appears poised to be the first agency to ever adopt this discredited and highly destructive Chamber of Commerce proposal'. NWC argues that 'there is a compelling need for full and complete transparency as to why the Commission proposed this rule, and what lobbying efforts were behind the proposals. The public needs this information to fully understand the intent behind the Commission's proposals, and to be in a position to fully and properly respond to the proposed rules'.

The deadline for public comments was 18 September 2018.

[Source: Whistleblower protection blog 17/09/2018]

Australian position: Bill still before the Senate (no incentive scheme included)

- **Progress on the Whistleblower Bill:** In Australia, *Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2017* was introduced by the Government in the Senate on 7 December 2017 following consultation (Governance News 08/12/2018). The Bill proposes to create a single whistleblower protection regime in the *Corporations Act 2001 (Cth)* covering the corporate, financial and credit sectors and to create a new whistleblower protection regime in the taxation law, to protect those who expose tax misconduct. The Bill was intended to apply to disclosures made on or after 1 July 2018 with companies having until 1 January 2019 to implement a compliant policy. As at 19 September 2018 the Bill is yet to pass either house, though the senate committee has recommended that it be passed. The Senate Committee also recommended (among other things) the introduction of a rewards scheme for whistleblowers and the establishment of an independent whistleblower protection authority (see: Whistleblower bill update — what you need to know and do next 24/04/2018).
- **Proposed revisions to ASX Corporate Governance Principles and Recommendations:** The ASX Corporate Governance Council recently consulted on proposals to update and issue a fourth edition of its Corporate Governance Principles and Recommendations (consultation closed on 27 July). Among the proposed changes is the inclusion of a new recommendation (3.3) that would require entities to have and disclose a whistleblower policy that encourages employees to come forward with concerns that the entity is not acting lawfully, ethically or in a socially responsible manner and providing suitable protections if they do; and ensuring that the board is informed of any material concerns raised under that policy that call into question the culture of the organisation (see: Governance News 04/05/2018).

Reputational Risk

In Brief | The WSJ reports that Wells Fargo has publicly acknowledged the possible negative commercial impact that reputational damage over media reports of recent governance scandals may be having on its commercial lending for the first time. Reportedly Wells' CFO gave a press conference in which he said that he expected to see business loans fall from second quarter levels, due to a 'host of factors' including reputational issues. 'Shifting blame to those who helped bring its lapses to light is unlikely to reassure potential clients or investors that Wells Fargo is taking its issues as seriously

as it should. The bank's competitors are pulling ahead while it remains stuck in the mud' The WSJ comments.

[Source: [registration required] The WSJ 15/09/2018]

Other News

Royal Commission into Aged Care Quality and Safety: Public feedback requested to develop detailed terms of reference closes 25 September.

Prime Minister Scott Morrison announced the Government's decision to ask the Governor General to establish a Royal Commission into the aged care quality and safety on 16 September.

The Royal Commission will primarily look at the quality of care provided in residential and home aged care to senior Australians. It will also include young Australians with disabilities living in residential aged care settings.

Consultation

The government is seeking feedback to develop the detailed Terms of Reference. Comments are open to members of the community, including residents and their families and aged care providers and aged care workers.

It is anticipated it will cover the quality of care provided to older Australians and the extent of substandard care; the challenges of providing care to Australians with disabilities living in residential aged care (including provision of care to younger people with disabilities); the challenge of addressing the care needs of the growing number of dementia patients as they age; and the future 'challenges and opportunities' for delivering aged care services in the context of 'changing demographics, including in remote, rural and regional Australia' as well as other matters that the Commission considers necessary.

Timeline: Consultation closes on 25 September.

The Governance Institute has welcomed the announcement of the Royal Commission into Aged Care. Acting CEO Meegan George has suggested that 'Similar to the learnings from the banking royal commission, aged care providers need to put the customer first and ensure they find the right balance between societal purpose and sustainability'.

[Sources: Department of Ageing and Aged Care media release 21/09/2018; Consultation to develop the detailed Terms of Reference for the Royal Commission into Aged Care Quality and Safety 17/09/2018; Governance Institute media release 18/09/2018]

In Brief | FEG scheme reforms Bill introduced: A Bill intended to address corporate misuse of the Fair Entitlements Guarantee Scheme (FEG) was introduced into the House of Representatives on 20 September.

[Source: Corporations Amendment (Strengthening Protections for Employee Entitlements) Bill 2018]