

# Governance News

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## Diversity

**In Brief | Elite US-based private firms remain 'incredibly homogenous'? A US study analysing the board composition of 200 of the most heavily funded US based private venture backed companies has identified that women hold just over 7% of board seats, and 60% of these boards include zero women. By contrast, none of the boards of the S&P 500 companies are all-male**

*[Sources: 2019 Study of Gender Diversity In Private Company Boardrooms 11/12/2019; Harvard Business Review 11/12/2019]*

## Shareholder Activism

**No change? BHP has elected to maintain engagement with industry associations, despite pressure from activists to withdraw from certain associations whose climate stance (in their assessment) is at odds with the goals of the Paris Agreement**

**Context:** BHP's Australian AGM was held on 7 November. A shareholder resolution, coordinated by the Australasian Centre for Corporate Responsibility (ACCR) calling for the company to suspend its membership of industry associations whose advocacy is inconsistent with the Paris Agreement received 72.93% votes against, (29.58% support). The result was consistent with the result at the London on 17 October where 22% of London shareholders voted in favour of the resolution (70% of shareholders voted against it). (See: Governance News 23/10/2019; 13/11/2019).

BHP said that it consulted extensively with its shareholders on the resolution in the lead up to both the Sydney and London AGMs and would be 'conducting further consultations in the next few months in relation to shareholders' views on this matter'. BHP added at the time, that shareholder consultations conducted to date would help inform the enhancements to the scope and methodology of BHP's 2019 Industry Association Review.

### Release of BHP's 2019 Industry Association Review

On 12 December, BHP released its 2019 industry association review — a review of the degree of consistency between BHP's energy and climate policy positions and those of the industry associations to which it belongs.

**Material differences identified:** The review identified material differences on climate and energy policies with four associations: 1) the NSW Minerals Council; 2) the US Chamber of Commerce (the Chamber); 3) the Mining Association of Canada (MAC); and 4) the American Petroleum Institute (API). This triggered a further analysis by BHP of any broader benefits received from relevant associations in areas (eg safety, health, workforce, community and economic policy), in order to 'reach an overall assessment on future membership'.

**Outcomes?** Following this analysis, BHP determined that it would remain a member of all four associations, despite the differences in policy position identified. BHP did commit to a number of further steps 'to close the differences identified consistent with BHP's published principles'. These include commitments to:

- review its membership of each of the four associations (by specific dates)
- write to each association asking that a formal climate and energy policy statement be published in 2020, and requesting an annual report from each association as to adherence to the statement on an ongoing basis
- strengthen oversight at group level of representation and engagement by BHP affiliates and entities with industry associations.

**ACCR's response:** In a statement, the ACCR Director of Climate and Environment Dan Gocher said that the report is a 'vindication of BHP shareholders' concerns in the worst way possible. BHP has asked shareholders to hold fire until the end of the year, and then released an impotent review in which the company refuses to bring any of its industry groups to heel. The investors who backed BHP's board now look foolish and weak, in the midst of a catastrophic climate-related bushfire crisis in Australia'. Mr Gocher went on to say that in light of its decision to stay a member of the industry associations, 'BHP should expect increasing pressure and scrutiny.'

**In Brief | The FT reports consumer advocacy group, SumOfUs has coordinated a resolution seeking that Apple publicly commit to respect freedom of expression. The resolution will reportedly be put to Apple shareholders at next year's AGM after Apple lost a bid to have the resolution struck from the agenda. According to The FT, when Apple faced similar proposals in 2016 and 2018 they drew less than 10% support**

[Source: [registration required] The FT 16/12/2019]

## Meetings and Proxy Advisers

### Recent AGM results: Westpac, ANZ, Woolworths, Elders

#### Westpac AGM

The Westpac AGM was held on 12 December. All board supported resolutions were carried.

**Remuneration report:** The resolution to approve the remuneration report was carried with 64.10% of shareholders voting in favour. 35.90% of shareholders voted against it, constituting a second 'strike' and triggering a vote on a spill resolution. The spill resolution was not carried, securing only 8.74% support (91.26% votes against).

In his address to shareholders ahead of the vote, Chair Lindsay Maxsted said that following the 2018 AGM, Westpac had engaged extensively with institutional and retail shareholders and advisory groups to gather feedback on remuneration and take action on the key concerns raised. He then outlined the changes made in response to shareholder concerns, as well as the steps taken following the announcement of the AUSTRAC investigation. These include: the introduction of a clawback mechanism for executive pay (which the Australian comments, mirrors the approach taken at Macquarie Group), reducing board fees for 2019 by 20% and 'applying a zero outcome for management of non-financial risk in Group Executive scorecards; downward remuneration adjustments; reducing some 2019 short term variable reward outcomes to zero; and a downward adjustment to prior year deferred short term variable reward for two former Group Executives'. In addition, Mr Maxsted reiterated that payment of either all/part of 2019 variable awards to the full executive team had been frozen, subject to the independent assessment of accountability for AUSTRAC's claims. He added that where accountability issues are identified 'appropriate consequences will be applied'.

**Director election/re-elections:** All directors standing for election were elected/re-elected. Steven Harker and Margaret Searle were standing for election. 96.47% of shareholders voted in favour of electing Mr Harker (3.53% voted against). Ms Searle received 98.59% of votes in support (1.41% of shareholder voted against).

Resolutions to re-elect Peter Marriott and Nerida Caesar were also carried. Ms Caesar received 74.95% votes in support (25.05% against). 57.97% of shareholders voted in favour of electing Mr Marriott (42.03% voted against).

**Shareholder (ESG) resolutions:** Market Forces coordinated two shareholder resolutions: 1) a special resolution to amend Westpac's constitution to allow advisory resolutions to be tabled at general meetings; and 2) (conditional on the passage of the constitutional amendment) an ordinary resolution requesting Westpac report on strategies and targets to reduce its exposure to fossil fuels including elimination of exposure to thermal coal by no later than 2030. Neither resolution was supported by the board and neither was carried. The constitutional amendment was not supported by the board on the basis that the board considered it is not in the best interests of shareholders and is, in their assessment, unnecessary because the 'board believes that appropriate avenues are already available to shareholders should they wish to express their opinions to the board'. The constitutional amendment received 8.04% support (91.06% votes against).

The Board also advised against the second resolution on the basis that Westpac already discloses 'significant' climate information, including specific targets aligned with the Taskforce on Climate related Financial Disclosures (TCFD recommendations). In addition, the board advised that the lender is due to update its Climate Change position statement in 2020.



Market Forces said that 16.6% of investors supported the resolution, though it was not put to the meeting. Reportedly, a number of questions from shareholders concerned Westpac's climate strategy, in light of recent bushfires and the worsening drought. Market Forces has called on shareholders to continue to push the lender to align its strategy with the goals of the Paris Agreement, including ceasing to lend to the fossil fuel industry.

*[Sources: Westpac ASX Announcements: CEO's address 12/12/2019; Chair's address 12/12/2019; Results of 2019 AGM; Notice of meeting 04/11/2019; Market Forces media release 13/12/2019; [registration required] The AFR 12/12/2019; [registration required] The Australian 13/12/2019]*

## **ANZ AGM**

The ANZ AGM was held on 17 December. All board supported resolutions were carried.

**Remuneration report:** The resolution to approve the remuneration report was carried with 89.94% votes in favour (10.06% of votes against). The resolution granting performance rights to ANZ CEO Shayne Elliott was also carried with 96.94% support (3.06% of votes against).

**Election/re-election of directors:** The two directors standing for re-election were each elected receiving 95.78% and 98.81% support respectively. Paul O'Sullivan was elected with 99.37% of shareholders voting in support.

**ESG (climate) resolutions:** None of the three shareholder resolutions supported by the board, and none were carried. The special resolution seeking to amend the constitution received 5.38% support (94.62% of votes against). Two contingent ordinary climate related resolutions — the first seeking increased climate transition planning disclosure and the second seeking that the lender suspend its memberships of industry associations whose climate stance is inconsistent with the goals of the Paris Agreement (lobbying resolution) — were not put to the meeting. The disclosure resolution received 14.69% proxy support, the lobbying resolution received 16.53% proxy support.

Commenting on the lobbying resolution in his address to the meeting, ANZ Chair David Gonski said that 'it is not the role of any association to represent any single member's view and from time to time we may take positions on certain matters not supported by the relevant industry association'. He went on to say that given the level of interest from stakeholders in the alignment of ANZ's policy position on climate change and those of the associations to which ANZ belongs, ANZ will conduct a review of its industry memberships in 2020 and publish the outcome in the next annual report.

According to The AFR, the Australian Council of Superannuation Investors (ACSI) advised against supporting the climate resolutions at ANZ (and also at the NAB AGM to be held on 18 December).

The AFR quotes Market Forces' executive director Julien Vincent as expressing frustration at the lack of support from superannuation funds. 'These are the same super funds that say they believe in climate science and support the Paris agreements and put their names on investor statements that call on government to get their act together on climate change. Why won't they hold themselves to the same standard?'

In a statement, Market Forces said that a number of questions from shareholders attending the AGM focused on climate issues and more particularly on disclosure by the lender of its climate transition plan, including the target set and accountability mechanisms.

*[Sources: ANZ ASX Announcements: Results of the 2019 AGM; CEO's address; Chair's Address; Market Forces media release 17/12/2019; [registration required] The AFR 16/12/2019]*

## **Woolworths AGM**

The Woolworths AGM was held on 16 December. All resolutions were carried.

**Remuneration report:** The resolution to approve the remuneration report was carried with 94.23% of shareholders voting in favour (5.77% against). Resolutions granting executive incentives were also carried each receiving over 96% support.

**Election/re-election of directors:** The three directors standing for re-election were each elected, receiving between 96.72% and 99.27% support. Jennifer Carr Smith was elected with 99.57% of shareholders voting in favour of her election.



**Demerger resolution:** Over 99% of shareholders also supported the board's resolution for the restructure and eventual demerger of the company's drinks and hotels business.

Media reports have commented that though shareholders voiced concerns about the wage underpayments issue (see: Governance News [06/11/2019 at p19](#)) over the course of the meeting, and though Woolworths said it had identified further issues in other parts of the business, this did not translate into either protest votes against individual directors or votes against the remuneration report. This is attributed to the approach taken by the board and in particular to the announcement of pay consequences for CEO Brad Banducci and Woolworths Chair Gordon Cairns ahead of the meeting. That is, the decision by to forgo his short term bonus for F20 (\$2.6m), and the reduction of Mr Cairns' fee for F20 by 20%.

Reportedly, shareholders also raised a number of questions around supply chain management and the social impact of Woolworths' gambling operations, though again these concerns were not reflected in voting behaviour.

*[Sources: Woolworths ASX Announcements: AGM results 2019; AGM Chairman and CEO's addresses and presentation 16/12/2019; [registration required] The AFR 16/12/2019; The ABC 16/12/2019; The SMH 16/12/2019]*

## Elders AGM

The Elders Ltd AGM was held on 12 December. All resolutions were carried.

**Remuneration report:** The resolution to approve the remuneration report was carried with 63.60% of shareholders voting in support (36.40% voting against, constituting a first 'strike'). Resolutions granting the managing director's long term incentive and ratifying the prior issue of securities were also carried. The resolution to grant the managing director's long term incentive received 75.85% support (24.15% of votes against) and the resolution to ratify the prior issue of securities received 68.32% support (31.68% of votes against).

Writing ahead of the meeting, Glass Lewis commented that the award of Long Term Incentives was 'surprising' given the company's financial performance and questioned the way in which the award was explained, suggesting that there were inconsistencies in the figures used.

**Re-election of director:** Director, Ian Wilton was reelected with 99.58% support (0.42% of votes against).

*[Sources: Elders ASX Announcements: 2019 AGM results 12/12/2019]*

## Regulators

### Top Story | Government's support of ACCC Digital Platforms Inquiry

The Australian government has delivered its response to the Australian Competition and Consumer Commission's Digital Platforms Inquiry.

The Government's response has largely supported the ACCC's recommendations and sets out a detailed roadmap of work for 2020 and into 2021. This includes the creation of a new 'Digital Platforms Branch' within the ACCC which will continue to examine the sector.

MinterEllison has released an article, providing an overview of the government's response and the possible ramifications. The article can be accessed on the MinterEllison website [here](#).

### New Zealand | Attitudes to a cashless society? 85% of people agree with the RBNZ's view that people who are financially excluded could be severely negatively impacted if cash becomes difficult to get or use in New Zealand

The Reserve Bank of New Zealand (RBNZ) has released a [report](#) presenting an analysis of the 2,284 submissions received in response to its issues paper/public consultation on the future use of cash. The consultation forms part of a broader work program looking at cash use.

The purpose of the consultation was to review whether cash has a unique role in New Zealand and identify some of the implications of moving towards a society with less cash.



## Issues associated with the shift away from cash?

Broadly speaking the RBNZ found (findings outlined in more detail below) that there was 'strong public support' for the bank's assessment of the issues raised by the prospect of cash disappearing and in particular, that there was support for the view that the disappearance of cash/increased difficulty in accessing cash could negatively impact certain people who rely on it 'and for whom there is no practicable substitute'.

### Some Key Findings

- **There was a diversity of opinion around the issue of whether it will become harder to get or use cash in New Zealand.**
  - 45% of people were of the view that it will become harder to get and use cash, 37% of respondents disagreed and 17% neither agreed nor disagreed (neutral).
  - Opinion was also varied in terms of the timeframe in which this might occur with 48% of respondents indicating that it would be harder to get/use cash within the next ten years (and 50% of this group indicating this will be the case in the next five years) and 22% indicating that this would happen over a longer timeframe (over 10 years).
  - 19% of respondents stated that it would never happen.
  - 13% of all respondents objected to the idea that cash would become harder to get and use in New Zealand because they felt it was too important and that the ability to access and use cash was a necessity and a right. This was more likely to be mentioned by those who disagreed that cash would become harder to get (26%).
- **A cashless society could negatively impact those who are financially excluded:** The majority of all respondents (85%) agreed with the Bank's view that people who are financially excluded (eg people with low incomes, in rural areas, people without internet access, people over 60 years of age, refugees) could be severely negatively impacted if cash become difficult to get or use in New Zealand. A majority of respondents also agreed that a cashless society could also 'severely negatively' impact people in some Pacific Islands (62%) and people who use cash for cultural customs (63%).
- **Given a hypothetical situation in which cash is hard to get or use, the majority of all respondents agreed with statements that reflected concerns with their privacy, security, and autonomy.** For example, 76% of respondents agreed with the statement that people lose privacy if they are unable to use cash to pay for some things; 73% agreed that reliance on electronic money means increased risk of identity theft/scams; 66% agreed that a cashless society means greater risk of cyber-attack through the banking system; and 68% agreed that people lose the ability to decide their own spending if they can't use cash to pay for some things.
- **Value in having physical cash:** 75% of all respondents agreed that cash enabled people to have 'a personal back-up for a rainy day' and 64% agreed that it was important to have cash because 'it was easier for people to make and stick to a budget'.
- **Who should pay to keep cash in circulation?** 44% of respondents were of the view that the RBNZ should 'only' be responsible for the costs of cash with 'trading banks, credit unions, and other institutions who deal with cash now' as the next most likely group to be identified as 'only' responsible (20% of respondents). 42% of respondents said that customers who use cash should not be responsible for the costs.
- **No answers on what should be done to help stop cash becoming hard to get or to manage the impact of this happening?** The RBNZ writes that 'most were at a loss' in terms of suggesting possible solutions. Some of the suggestions put forward included the following.
  - 14% of respondents suggested that new laws to ensure cash continues to be available as a payment option should be introduced
  - 4% of respondents suggested that community groups, families and individuals could lobby/petition the government to 'fight for the right to stop cash becoming hard to get'

- 'many other' respondents commented that the status quo should be maintained ie the RBNZ should keep producing cash (21%), retailers should keep accepting cash (19%) and individuals should keep spending it (13%)

**Why is the RBNZ concerned about this issue?** The RBNZ is the sole issuer of cash in New Zealand and is required to issue currency that meets the needs of the public. There is no agency responsible for over-seeing the usability of cash by the public or the stability of the cash system in New Zealand. Given this, RBNZ says it is 'taking a leadership position'.

**Conclusions?** Were cash to become less easy to access, the RBNZ considers it would be a 'market failure to the extent that commercial operators did not fully incorporate the wider network benefits of cash. As a result, government action might be required'.

*[Sources: RBNZ media release 16/12/2019; Public consultation on the future of cash use December 2019]*

## Financial Services

### Top Story | Directions in Public M&A 2019

MinterEllison has released a report presenting observations on public M&A trends in FY19 and predictions for the remainder of FY20 based on analysis of ASX market data for the financial year ended 30 June 2019.

The full text of the report is available on the MinterEllison website [here](#).

### Top Story | APRA has formally commenced an investigation into Westpac and imposed a \$500m increase in the bank's capital requirements

#### **Key Takeouts**

- Following the commencement of civil proceedings against Westpac by AUSTRAC, APRA has said it is investigating whether Westpac's conduct (and/or the conduct of its directors/senior managers) may have breached the lender's obligations under the Banking Act (including BEAR obligations) and/or APRA's prudential standards.
- APRA has also imposed an additional capital requirement (\$500m) on the lender 'to reflect the heightened operational risk profile of the bank'.
- APRA Deputy Chair Mr John Lonsdale said that Westpac 'is financially sound' though 'there are potentially substantial gaps in risk governance that need to be closed'.
- APRA has said that the investigation is likely to be extensive and 'lengthy', given the nature of the matters raised by AUSTRAC, the number of alleged breaches and the period of time over which they occurred
- Mr Lonsdale observed that the investigation is an opportunity for the regulator to exercise legal powers that were expanded and strengthened following the CBA Prudential Inquiry, including enhanced investigative powers and the implementation of the BEAR.
- APRA has also said that it will work with AUSTRAC and ASIC as appropriate (given the legal proceedings, and investigation also on foot)
- In a short statement, acknowledging APRA's announcement, Westpac said it is 'committed to cooperating' with the regulator in 'all aspects of its investigation and review'.

Following the announcement by The Australian Transaction Reports and Analysis Centre (AUSTRAC) that it has commenced civil proceedings against Westpac for alleged contraventions of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth) (see: Governance News 27/11/2019), the Australian Prudential Regulation Authority (APRA) has said that it has 'formally commenced' an investigation.

APRA says that the investigation will focus on whether conduct by Westpac, its directors/senior managers, that led to the matters alleged by AUSTRAC, as well as the bank's actions to rectify and remediate the issues





after they were identified, contravened the Banking Act 1959 (including the banking executive accountability regime (BEAR)) or APRA's prudential standards.

### **Details: Scope of APRA's investigation**

APRA says that in 'considering possible contraventions of the Act and the prudential standards' APRA's investigation will examine:

- the adequacy and extent to which governance, control and risk frameworks, were appropriately implemented
- whether accountability and remuneration arrangements were 'adequate, and appropriately implemented to effectively manage non-financial risks'
- whether there was a failure to comply with accountability obligations under the BEAR
- whether there was a failure to comply with the requirements of the prudential standards including Prudential Standard CPS 510: Governance, Prudential Standard CPS 520: Fit and Proper, and Prudential Standard CPS 220: Risk Management
- whether there was a failure to 'promptly notify APRA of any significant breaches and/or a breach of accountability obligations'.

Announcing APRA's investigation, APRA Deputy Chair Mr John Lonsdale said that 'AUSTRAC's statement of claim in relation to Westpac contains serious allegations that question the prudential standing of Australia's second largest bank. While Westpac is financially sound, there are potentially substantial gaps in risk governance that need to be closed. Given the nature of the matters raised by AUSTRAC, the number of alleged breaches and the period of time over which they occurred, this will necessarily be an extensive and potentially lengthy investigation.'

Mr Lonsdale added that the investigation is an opportunity for the regulator to exercise legal powers that were expanded and strengthened following the CBA Prudential Inquiry, including enhanced investigative powers and the implementation of the BEAR.

### **Additional capital requirements and review of Westpac's risk governance**

#### **APRA says it will also:**

1. **Increase Westpac's capital requirements by \$500 million**, 'to reflect the heightened operational risk profile of the bank'. APRA says that this brings the total operational risk capital add-ons that Westpac is required to hold to \$1 billion.
2. **Launch an 'extensive review program focused on Westpac's risk governance'**. APRA says that the review will examine 'risk management, accountability, remuneration and culture' and an 'examination of the steps Westpac has been taking to strengthen risk governance in recent years, including through its self-assessment'.

### **Cooperation with other investigations**

Noting the investigation by the Australian Securities and Investments Commission (ASIC), as well as AUSTRAC's legal proceedings are also on foot, APRA said that it will cooperate with each agency cooperating where appropriate.

*[Source: APRA media release 17/12/2019]*

### **Westpac response**

In a short statement acknowledging APRA's announcement, Westpac said it is 'committed to cooperating' with the regulator in 'all aspects of its investigation and review'.

Westpac Group's Chair, Lindsay Maxsted said, 'Westpac accepts the gravity of the issues presented by AUSTRAC. As previously stated, these shortcomings are unacceptable and we are determined to urgently fix these issues and lift our standards'. Mr Maxsted added that the lender will fully support APRA in its



investigation and review and reiterated that an Accountability and Financial Crime Program Review (conducted by Promontory) is underway.

Commenting on the additional capital requirement, Mr Maxsted said that it will be implemented through an increase in risk-weighted assets, and will apply from 31 December 2019. He added that the 'change is expected to reduce Westpac's Level 2, common equity tier 1 (CET1) capital ratio by approximately 16 basis points, based on the Group's balance sheet as at 30 September 2019'.

[Source: Westpac media release 17/12/2019]

## Top Story | FSRC referral: ASIC has commenced proceedings against TAL Life Ltd

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### Key Takeouts

- The Australian Securities and Investments Commission (ASIC) has commenced civil proceedings against TAL Life Ltd (TAL), for alleged contraventions of the ASIC Act (ss12DB(1) and 12DA(1)), the Corporations Act (s1041H(1)), and the Insurance Contracts Act (s13(2)) in avoiding an income protection claim.
- ASIC is seeking civil penalties in relation to the alleged breaches of s12DB of the ASIC Act and declarations in relation to s12DA of the ASIC Act, s1041H of the Corporations Act and s13 of the Insurance Contracts Act.
- ASIC's investigation arose from a referral from the Financial Services Royal Commission.

On 17 December, the Australian Securities and Investments Commission (ASIC) announced that it has commenced proceedings in the Federal Court against TAL Life Ltd (TAL) in connection with TAL's handling of a claim made under an income protection policy.

ASIC's investigation arose out of a referral made by the Financial Services Royal Commission (FSRC).

[Note: TAL was an insurance case study considered by the FSRC. See: Financial Services Royal Commission Final Report, Volume 2 at p331. TAL's response to the findings proposed by Counsel Assisting in relation to TAL following the Round 6 hearings is available on the FSRC website [here](#).]

### Background

According to ASIC, TAL provided an income protection policy to a woman who was later diagnosed with cervical cancer. She then sought to make a claim under the policy.

TAL issued a claims pack to the woman, requiring that she provide authorities enabling TAL to: a) obtain and access all of her medical records; and b) any information required by TAL from any insurer, employer or accountant or other relevant holder of information.

According to ASIC, TAL then launched an investigation into the woman's medical history and avoided her policy on the basis of purported non-disclosure or misrepresentation.

### ASIC allegations

[Note: The [Concise Statement](#) and [Originating Process](#) which detail ASIC's allegations in detail are available on the ASIC website [here](#).]

### Claims pack representations

Broadly, ASIC alleges that TAL's investigation into the woman's medical history was based on 'false statements' in the claims pack, in that TAL (allegedly) expressly or impliedly represented that it had a right to require the information sought, when this was not the case.

More particularly, ASIC contends that TAL:

- made a false and/or misleading representation in connection with the supply of financial services in contravention of s12DB(1) of the Australian Securities and Investments Commission Act 2001 (ASIC Act);



- engaged in conduct that was misleading/deceptive or likely to mislead/deceive in contravention of s12DA(1) of the ASIC Act;
- engaged in conduct that was misleading/deceptive or likely to mislead/deceive in contravention of s 104H(1) of the Corporations Act 2001 (Corporations Act); and
- failed to act with the utmost good faith in contravention of s13(2) of the Insurance Contracts Act 1984 (ICA) by failing to act with the utmost good faith.

### **The manner in which TAL avoided the policy**

ASIC also alleges that in sending a letter to the consumer in which it avoided her policy (for purported non-disclosure of a depressive condition) TAL: a) avoided the policy without first offering her an opportunity to address concerns; and b) accused her of breaching her duty of disclosure and her duty of utmost good faith under the ICA.

ASIC contends that the manner in which TAL avoided the policy contravened s13(2) of the ICA (the duty of utmost good faith).

### **Relief sought**

ASIC is seeking civil penalties in relation to the alleged breaches of s12DB of the ASIC Act and declarations in relation to s12DA of the ASIC Act, s1041H of the Corporations Act and s13 of the Insurance Contracts Act.

### **Possible penalties?**

ASIC notes that the maximum penalty for a breach of s12DB (false or misleading representations) at the time of the conduct is 10,000 penalty units (\$1.7million).

### **Law reform?**

Following earlier consultation, the government recently released a draft Bill and regulations — [exposure draft] Financial Sector Reform (Hayne Royal Commission Response—Protecting Consumers (2020 Measures)) Bill 2020: claims handling; [exposure draft] Financial Sector Reform (Hayne Royal Commission Response—Protecting Consumers) (Claims Handling and Settling Services) Regulations 2020: claims handling – for consultation.

The proposed legislation would: 1) remove the exclusion of insurance claims handling and settlement services from the definition of a 'financial service' in the Corporations Act 2001; 2) make handling and settlement of an insurance claim, or potential insurance claim, a 'financial service' under the Corporations Act 2001; and 3) tailor application of the existing financial services regime to the new financial service of handling and settling an insurance claim. Consultation will close on 10 January.

The draft legislation proposes to implement Financial Services Royal Commission recommendation 4.8 (removal of the insurance claims handling exemption). (For a summary of the draft legislation see: Governance News 04/12/2019 at p14.)

ASIC comments that it supports the draft Bill 'as improving the conduct engaged in by or on behalf of insurers during the claims handling and settling process'.

*[Sources: ASIC media release 17/12/2019; Concise Statement; Originating Process]*

## **Top Story | ASIC has commenced proceedings against NAB**

### **Key Takeouts**

- ASIC has commenced civil penalty proceedings in the Federal Court against National Australia Bank Limited (NAB) in connection with alleged 'fee for no service' conduct.
- ASIC is seeking declarations of contraventions of the Corporations Act and the ASIC Act, pecuniary penalty orders and ancillary orders, including costs.



On 17 December, (the day before the company's AGM), the Australian Securities and Investments Commission (ASIC) announced that it has commenced proceedings against National Australia Bank (NAB) in the Federal Court in connection with alleged 'fee for no service' conduct.

## Allegations

[Note: The [Concise Statement and Originating Process](#) which set out ASIC's allegations in detail are available on the ASIC website [here](#).]

Broadly, ASIC alleges that during the period 17 December 2013 and 4 February 2019 NAB:

- did not provide ongoing financial planning services to some customers while charging fees to those customers in contravention of s962P of the Corporations Act 2001 (Cth) (Corporations Act)
- did not issue fee disclosure statements to certain clients in contravention of s 962S of the Corporations Act
- issued defective fee disclosure statements which did not accurately describe the fees the customer paid and/or the services the customer actually received in contravention of ss 12DB(1)(a) and (g) and 12DA of the Australian Securities and Investments Act 2001 (Cth) (the ASIC Act) and s 1041H of the Corporations Act
- did not have 'reasonably adequate' systems and controls in place to prevent the issues identified in contravention ss 912A(1)(a), (b), (c), (ca), (e) and (f) of the Corporations Act
- ASIC further alleges that by continuing to charge ongoing service fees to certain customers during the period May 2018 to 4 February 2019 when it stopped charging fees, when NAB knew that it had not delivered the services and had issued defective FDSs/knew that there was a risk that this was the case, NAB engaged in unconscionable conduct in contravention of s 12CB of the ASIC Act 2001 (Cth).

## Relief being sought

ASIC is seeking declarations, pecuniary penalties and compliance orders from the Federal Court to prevent similar contraventions occurring in the future.

The maximum civil penalty for contraventions alleged against NAB are: \$250,000 per contravention for breaches of s962P (charging ongoing fees after the termination of an ongoing fee arrangement) and s962S (failing to provide a timely FDS) and \$1.7 to \$2.1 million maximum penalty (depending on the time period) per contravention for breaches of s12CB (unconscionable conduct) and s12DB (false or misleading representations).

ASIC notes that NAB has said that it has provisioned more than \$2 billion for customer-related remediation across all of its advice licensees.

## NAB's response

The Australian quotes NAB Chief Legal Counsel Sharon Cook as saying that the lender takes ASIC's action 'seriously and will now carefully assess the allegations'.

Ms Cook reportedly went on to say that NAB will 'continue to work co-operatively and constructively with ASIC to deal with this issue. We have already acknowledged failures where customers have paid fees for services they didn't receive and have paid \$37.8m to 27,500 NAB Financial Planning clients. Remediation began in December 2018 and is expected to be completed by June 2020...NAB Financial Planning has made changes to systems and controls and will continue to improve so we can service our clients better.'

## Not unique to the lender



In a statement, ASIC Deputy Chair Daniel Crennan commented that the alleged issues at NAB are not unique to the lender. 'Fees for no service misconduct has been widespread and is subject to ongoing ASIC regulatory responses including investigations and enforcement actions' Mr Crennan said.

He added that the this 'widespread misconduct was examined in some detail by the Financial Services Royal Commission'.

ASIC's latest update on reviews into fees for no service issues at AMP, ANZ, CBA, NAB and Westpac was released on 11 March (for a summary see: Governance News 13/03/2019 at p17).

### Law reform?

To address fees for no service issues specifically, Commissioner Hayne recommended (recommendation 2.1) that the law should be amended to provide that ongoing fee arrangements (whenever made): must be renewed annually by the client; must record in writing each year the services that the client will be entitled to receive and the total of the fees that are to be charged; and may neither permit nor require payment of fees from any account held for or on behalf of the client except on the client's express written authority to the entity that conducts that account given at, or immediately after, the latest renewal of the ongoing fee arrangement.

The government's roadmap for implementing the government's response to the Financial Services Royal Commission's recommendations indicates that it intends to consult on, and introduce legislation to implement the measure by 30 June 2020.

*[Sources: ASIC media release 17/12/2019; Concise Statement; Originating Process; [registration required] The Australian 17/12/2019]*

### NULIS has met the requirements of the additional licence conditions imposed by ASIC

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The Australian Securities and Investments Commission (ASIC) has released an Independent Expert Summary Report prepared by KPMG as the independent expert engaged by NULIS Nominees (Australia) Limited under the additional licence conditions imposed by ASIC on NULIS in 2017.

The report summarises the series of reports KPMG had prepared for NULIS on the adequacy of compliance and risk management practices for its retail and wrap superannuation funds.

**NULIS has met all the requirements of the additional licence conditions imposed:** NULIS has reported to ASIC that it has implemented all recommended changes to policies and procedures. ASIC considers that NULIS has now met the requirements of the additional licence conditions. ASIC adds that it remains engaged with NULIS as it continues to improve its operations and address the recommendations made by the Financial Services Royal Commission.

[Note: On 6 September 2018, ASIC announced that it had commenced proceedings in the Federal Court of Australia against two entities in NAB's wealth management division, NULIS Nominees (Australia) Limited (NULIS) and MLC Nominees Pty Ltd (MLC Nominees). The court proceedings relate to fees charged by both entities to a number of their superannuation members for services, which were (allegedly) not provided (see: Governance News 10/09/2019). Separately, ASIC has also commenced civil penalty proceedings in the Federal Court against National Australia Bank Limited (NAB) in connection with alleged 'fee for no service' conduct. This is covered in a separate post in this issue of Governance News.]

*[Sources: ASIC media release 16/12/2019; KPMG Summary Report: REP 647 Independent expert summary report - NULIS Nominees (Australia) Limited]*

### FSRC recommendation 1.17 update: APRA to delay the consultation on implementing BEAR product responsibility

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**Context:** Financial Services Royal Commission Recommendation (FSRC) 1.17 recommends that following consultation, the Australian Prudential Regulation Authority (APRA) should determine for the purposes of section 37BA(2)(b) of the Banking Act, a responsibility, within each authorised deposit taking institution (ADI) subject to the banking executive accountability regime (BEAR), for all steps in the design, delivery and maintenance of all products offered to customers by the ADI and any necessary remediation of customers in respect of any of those products.



In addition, the FSRC recommended (6.8) that the BEAR should be extended over time to all APRA-regulated financial services institutions.

**Delay announced:** APRA has written to industry announcing that the regulator will delay the consultation on implanting FSRC recommendation 1.17 to allow 'careful consideration' to the alignment of product responsibility with the timing and content of the government's proposed extended accountability regime (FSRC recommendation 6.8). This is intended to both optimise the effectiveness of the changes, and to minimise 'unnecessary cost to institutions'.

APRA says that it will provide a further update on its revised approach to implementing product accountability in the first half of 2020.

*[Sources: APRA media release 13/12/2019; Consultation on proposed approach to product responsibility under the Banking Executive Accountability Regime; APRA letter to industry 13/12/2019]*

## **ASIC has called on the superannuation industry to revisit the way in which life insurance within super is provided to members and focus on delivering better member outcomes**

### **Report Overview | ASIC Report 646 Insurance in superannuation: Industry implementation of the Voluntary Code of Practice**

#### **Key Takeouts**

- ASIC found that some improvements in practices are being introduced as a result of adoption of the Voluntary Code of Practice by a significant number of trustees, but that further work needs to be done to achieve 'the high industry standards consumers expect'.
- ASIC Commissioner Danielle Press said: 'We identified a number of inconsistencies in implementation of the Code, some relating to fundamental aspects such as which members are covered by the Code, the controls around balance erosion, and calculation of timeframes for claims processes. Also, trustees are continuing to leave vulnerable members behind – they need to have better defined policies and processes for those with unique needs'.
- ASIC has called on superannuation trustees to: a) review frameworks, policies and governance of insurance matters in order to support improved outcomes for members; b) strengthen data collection and analysis in order to support product design that meets member needs with minimal account erosion; and c) play an active role, alongside insurers and administrators, in ensuring a good claims experience for members.
- ASIC says that its work in insurance in superannuation will focus (in 2019-20 financial year) on implementing of the PYSP reforms, occupational risk categories in insurance in superannuation and 'value for money in insurance in superannuation' (analysis of how the industry evaluates value between products and between cohorts).
- ASIC also plans to work with industry in its development of more practical guidance on how trustees can better meet the needs of vulnerable consumers.

In the first of a series of planned reports looking at the superannuation industry's progress on improving insurance outcomes for consumers to be released in the 2019–20 financial year, the Australian Securities and Investment Commission (ASIC) has released a report — [Report 646 Insurance in superannuation: Industry's implementation of the voluntary code of practice](#) — outlining its assessment of industry progress on the implementation of the Insurance in Superannuation Voluntary Code of Practice (Code).

The report also outlines key features of insurance in superannuation, potential consumer harms, and ASIC's regulatory focus and expectations in this area.

Announcing the release of the report, ASIC Commissioner Danielle Press said, that ASIC 'recognise that there is significant change occurring in relation to insurance in superannuation. In this dynamic phase, it is important that superannuation trustees remain focused and committed to improving outcomes for members.'

#### **Potential consumer harms and default life insurance**



The report notes that despite 'sound motivations for default life insurance', several reports over the last 24 months have identified potential consumer harms related to insurance in superannuation.

Potential consumer harms include:

- a) poor member-engagement hindering members' understanding of their insurance cover and their ability to make timely and appropriate decisions to suit their circumstances;
- b) members paying premiums for insurance they may not need;
- c) trustees applying default settings (eg smoker status) that may be inappropriate for some members;
- d) members paying premiums for insurance they are ineligible to claim;
- e) members finding it difficult to change their cover or to opt out of insurance; delays and 'onerous and/or opaque' claims handling processes;
- f) variation in decline rates across the industry; and
- g) substantial variation in key terms and definitions across the industry increasing market complexity and limiting the ability to compare products.

### Cost of premiums

Another issue identified is the cost of premiums. According to ASIC, the premiums on the insurance attached to MySuper products (just over \$5 billion in 2017–18) represents a significantly higher cost to funds than the superannuation product itself.

ASIC comments that many consumers are not aware that they are paying for this insurance, and that those who are aware, may find product features, terms and conditions as well as pricing 'too difficult to understand or inappropriate for their circumstances'.

### Why is ASIC monitoring take up of Superannuation Voluntary Code of Practice (Code)?

ASIC says that it is examining take up of the Code to inform its judgement on whether further changes are required to achieve 'necessary industry uplift'. This builds on previous work including from two reports: Report 591 Insurance in superannuation (REP 591) (see: Governance News 10/09/2018 at p19) and Report 633 Holes in the safety net: A review of TPD insurance claims (REP 633) (see: Governance News 23/10/2019).

However, ASIC observes that its 'work and engagement with the Code is not a substitute for proper oversight of the Code by a properly resourced code administrator that would have powers to investigate breaches and to sanction funds if breaches were not remedied'. ASIC says that it considers the absence of such a body is one deficiency of the Code.

ASIC goes on to say that as part of its response to the Financial Services Royal Commission, the government has committed to introduce legislation by 30 June 2020 to make contraventions of 'enforceable code provisions' in ASIC approved codes a breach of the law. ASIC notes that this 'may have potential implications for industry'.

ASIC adds that it is working 'in tandem' with the Australian Prudential Regulation Authority (APRA) to improve consumer outcomes in insurance in superannuation, and notes the recent release by APRA of a consultation paper on proposed revisions to prudential standards (SPS 250) (see: Governance News 27/11/2019 at p15).

### Code implementation — some key points

The Code came into effect in July 2018 however, full compliance is not required until July 2021.

- **Adoption of the Code is not universal:** According to ASIC, 70% of APRA regulated trustees (including more than 90% of trustees authorised to provide MySuper products), have committed to fully implement the Code, 12% have committed to partial adoption, and the remaining 30% have either determined not to adopt the Code or it is 'unknown' whether they will do so. Reasons given by trustees for deciding not to adopt the Code include: a) they consider that their current insurance strategy already aligns with the Code; b) they consider that partial compliance may mislead their members; and c) that the Code is too onerous for their fund and may not be in their members' best interests.



- **'Ample room for improvement':** Though adoption of the Code was found to be 'contributing to a promising uplift and standardisation of processes and services' in some areas — one example given is that the adoption of the Code's target timeframes has resulted in an overall reduction in the length of time taken to process claims and complaints — ASIC found that some 'fundamental aspects' of the Code are being implemented inconsistently eg the controls around balance erosion and the calculation of claim timeframes as well as inconsistent approaches to which members are covered. As such ASIC considers that there is 'ample room for improvement' in terms of delivery of optimal consumer outcomes.

### Improvement areas identified

- **Inconsistent approaches to balance erosion:** The Code requires trustees to set premiums for Automatic Insurance Members at a level that does not exceed 1% of an estimated level of salary for the membership generally, and/or for segments within the membership. However, ASIC found that trustees use different approaches to calculate this estimated salary. For example, some trustees were observed to use members' estimated average lifetime earnings and average lifetime income which allows the trustee to charge premiums that are potentially significantly more than 1% of some members' current salary.

ASIC argues that a standardised approach to the calculation of the 1% premium salary threshold, combined with a requirement for trustees to be more transparent about how the salary cap is calculated, is required in order to deliver more accountability/consistency around this issue.

- **Variation in claim/complaints handling timeframes:** Despite the fact that a number of trustees, insurers and other service providers have elected to adopt the Code's target timeframes and the consumer benefits flowing from this, ASIC identified that some trustees are calculating time 'in unique ways that, in our view, undermine the effectiveness of setting standardised timeframes'.

ASIC cautions that 'the timeframes set out in the Code are just starting points. We expect trustees to do better, and design systems and processes that are focused on delivering good outcomes for their members. Delays in processing claims can negatively affect members' experiences and outcomes'.

- **Better support for vulnerable members:** ASIC found that few trustees have policies for vulnerable members, and that these policies are often not well defined. Further ASIC found that 'a majority' of trustees 'appear reluctant' to engage systematically with vulnerable members, and that many trustees were unable to demonstrate a 'good understanding of their membership and their needs'. More particularly, ASIC observed that trustees: a) 'too often' rely on members to self-identify as 'vulnerable'; b) rely on vulnerable members authorising third parties to act on their behalf; c) have no reference/links on their website to support services; and d) are too reliant on their call centre agents to act as interpreters.

ASIC says that 'protecting vulnerable consumers is a regulatory priority' and that accordingly, ASIC will continue to raise the profile of the issue.

ASIC adds that 'trustees could be more proactive and systematic in how they identify and engage with vulnerable consumers' and further that the Code could 'go further in detailing how trustees should do this, and in embedding a consumer-centric approach to vulnerability'. ASIC suggests that 'industry should develop concrete best-practice guidance to drive positive conduct in this area'.

ASIC adds that it plans to develop 'more practical guidance on how trustees can better meet the needs of vulnerable consumers' and remains engaged with relevant law reform initiatives in this area.

- **Certain protections under the Code are 'easily lost':** Certain protections under the Code apply to 'Automatic Insurance Members' only. This was found to be an issue both because classification as an automatic insurance member could be 'easily lost' in practice by even 'very basic' engagement with insurance (eg by making an election to maintain default insurance) and due to trustees' inconsistent interpretations of term 'Automatic Insurance Members' (despite the fact that it is a defined term).

ASIC observed that some trustees have opted to provide the highest level of protections under the Code to all their members irrespective of their classification. ASIC states that it considers this approach to be 'best practice'.

### ASIC's work in insurance in superannuation in 2019-20 financial year

In the 2019–20 financial year ASIC says it will focus on:





- the implementation of the 'protecting your superannuation package reforms' (Treasury Laws Amendment (Protecting Your Superannuation Package) Act 2019 and Treasury Laws Amendment (Putting Members' Interest First) Act 2019)
- occupational risk categories in insurance in superannuation: models for their use, default category selection, the data and analysis used to inform these choices and the disclosure of these aspects of the product
- value for money in insurance in superannuation: analysis of how the industry evaluates value between products and between cohorts.

ASIC adds that it plans to work with industry in its development of more practical guidance on how trustees can better meet the needs of vulnerable consumers and will also remain engaged with relevant law reform initiatives impacting on insurance in superannuation.

*[Sources: ASIC media release 13/12/2019; ASIC Report 646 Insurance in superannuation: Industry implementation of the Voluntary Code of Practice; IFA 16/12/2019]*

### **Eligible rollover funds to release lost super to ATO by June 30 2021?**

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In a joint statement, Treasurer Josh Frydenberg and Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume announced plans to introduce legislation in early in 2020 to:

1. allow trustees of eligible rollover funds (ERFs) to voluntarily transfer amounts to the Australian Taxation Office (ATO);
2. require trustees to transfer all accounts below \$6,000 by 30 June 2020; and
3. to transfer any remaining accounts still residing in an ERF to the ATO by 30 June 2021.

Mr Frydenberg and Ms Hume said that the changes are 'another step forward in addressing the issue of unnecessary duplicate accounts in the superannuation system, lowering fees and charges, and are consistent with the Productivity Commission's recommendation, in its report Superannuation: Assessing Efficiency and Competitiveness, that ERFs be wound up within three years'.

[Note: Recommendation 5 of the Productivity Commission's *Final Report* recommended that legislation enacted requiring the auto-consolidation of superannuation accounts with balances under \$6000 and 13 months or more of inactivity. Further, the Commission recommended government 'should make explicit that this process should capture accounts held in Eligible Rollover Funds' which should be wound up within three years with APRA oversight'. For a summary of the Productivity Commission's recommendations see: *Governance News 16/01/2019*]

*[Sources: Joint media release Assistant minister for superannuation, financial services and financial technology Jane Hume, and Treasurer Josh Frydenberg 13/12/2019; [registration required] The Australian 12/12/2019]*

### **Superannuation fund merger announced: VicSuper and First State Super to merge**

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VicSuper and First State Super have announced they have signed a merger deed confirming their intention to merge effective 1 July 2020. The merged fund will be one of the largest in Australia, managing more than \$125 billion in retirement savings on behalf of more than 1.1 million members nationally.

**The merger is in the best interests of members:** The statement says that the business case for the merger identified a number of benefits to members of both funds including (among others): scale benefits; access to broader investment opportunities and increased diversification leading to cost savings over time.

**Board composition:** The Board composition will reflect the membership of the merged fund with an equal number of member and employer representatives. The board will comprise 14 directors, four of whom will be appointed from VicSuper's current Directors. The Board will reduce to 10 Directors within two years.

CEO of First State Super, Deanne Stewart will be CEO of the merged fund, while VicSuper's current CEO Michael Dundon will become Deputy CEO. First State Super's Chair Neil Cochrane will become the Independent Chair of the merged fund.

*[Source: First State Super media release 13/12/2019]*



## **APRA has released an updated prudential standard on banking credit risk management**

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Following consultation (see: Governance News 27/03/2019), the Australian Prudential Regulation Authority (APRA) has released an updated prudential standard on credit risk management requirements for authorised deposit-taking institutions (ADIs): Prudential Standard APS 220 Credit Quality (APS 220). The revised APS 220 will come into effect from 1 January 2021.

Separately, the regulator released draft guidance — Draft Prudential Practice Guide APG 220 Credit Risk Management (APG 220) — for consultation. Consultation on the draft guidance closes 12 March 2019.

APRA says that it will consult on revised reporting requirements for credit risk management that would take effect at the same time as the final APS 220 and APG 220 separately.

### **Changes to APS 220**

Generally speaking, APRA has gone ahead with the changes proposed in the consultation which it says were 'broadly supported' in submissions, with some clarifications (outlined briefly below).

[Note: For a summary of the proposed changes to APS 220 see: Governance News 27/03/2019 at p14]

Briefly, the finalised prudential standard:

- broadens its coverage to include credit standards
- incorporates enhanced board oversight of credit risk and the need for ADIs to maintain prudent credit risk practices over the entire credit life-cycle
- provides a more consistent classification of credit exposures, by aligning recent accounting standard changes on loan provisioning requirements, as well as other guidance on credit related matters of the Basel Committee on Banking Supervision
- addresses Financial Services Royal Commission Recommendation 1.12 (Valuations of Land)

### **Issues raised in submissions**

APRA says that issues raised in submissions included the following.

- requests for clarification of the role of the board and senior management in credit risk management
- requests for clarification around the application of the proposed credit standards requirements for certain types of lending
- respondents also raised concerns regarding the proposed valuation of collateral and asset classification requirements
- some submissions suggested the implementation date for the final APS 220 should be deferred given APRA had proposed a 1 July 2020 start date

### **'Key adjustments' made by the regulator in response to issues raised**

The response paper sets out APRA's responses to each of the issues raised in submissions. Key changes highlighted by APRA in response to submissions include the following.

- **credit standards:** The final APS 220 clarifies APRA's expectations around the 'scalable and flexible' approach ADIs should take to assessing a borrower's credit risk. In this regard, APRA says that an ADI must use experienced credit judgement in approach to its credit risk assessment of a borrower. In addition, APRA reworded the final APS 220 so that an ADI would make 'reasonable inquiries' and take 'reasonable steps' to verify a borrower's financial situation.
- **valuation of collateral:** consistent Financial Services Royal Commission recommendation 1.12 (Valuation of Land), the final APS 220 clarifies APRA's expectation that valuation of collateral requirements do not require an ADI to predict when 'external events' are likely to occur, and that 'external events' are wider than drought and flood. In addition, to align with international valuation and accounting standards, the final APS 220 no longer requires APRA approval for fair values to be based on highest and best use.



- **asset classification:** APRA has removed the term 'significantly deteriorated' from the final APS 220 to 'provide for a simpler classification for prudential reporting purposes'. ADIs will be required to classify exposures as 'performing' or 'non-performing' and as 'past-due' and 'restructured'. In addition, APRA amended its proposal for a twelve month period for a restructured exposure to return to performing status and is retaining the current six month requirement.
- **implementation date:** APRA says that in light of the comments in submissions, and the time needed for ADIs to implement regulatory change, APRA has amended the implementation date of the final APS 220 to 1 January 2021 with the expectation that 'entities will review their existing credit risk management frameworks so their credit risk policies, processes and practices fully comply with the new standard from its effective date'.

### The role of the board and senior management

APRA considers it appropriate that the Board review and approve, on at least an annual basis, the ADI's credit risk appetite and credit risk management strategy. However, APRA says it has reconsidered its proposal for the Board to specifically consider 'return levels' and 'target markets' in approving its credit risk management strategy, and has amended the standard so that senior management must address such topics as target markets in developing and implementing credit risk policies consistent with the ADI's credit risk appetite.

### Draft Guidance

APRA has also released a draft Prudential practice Guide APG 220 Credit Risk Management for a three month consultation. The deadline for submissions is 12 March 2020.

APRA says that the draft guidance draws on outcomes from its recent supervisory focus on credit standards and Basel guidance on credit related matters.

The main elements of draft APG 220 include guidance on: a) the credit risk management framework; b) credit origination and assessment and approval; c) credit administration, measurement and monitoring; d) controls over credit risk; e) non-performing exposures; f) restructured exposures; and g) credit risk and accounting for expected credit losses.

*[Sources: APRA media release 12/12/2019; Response to submissions: APS 220 Credit Risk Management; Prudential Standard APS 220 Credit Risk Management; Draft Prudential Practice Guide APG 220 Credit Risk Management]*

### Hints for prospective AFS licence and credit licence applicants?

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The Australian Securities and Investments Commission (ASIC) has released a report — [Report 650 Overview of licensing and professional registration application: July 2018 to June 2019 \(REP 650\)](#) — providing an overview of ASIC's activity and oversight in relation to applications for AFS licences and credit licences and insights into the regulatory and policy issues that impact ASIC's licensing and registration application related activities.

Among other things, the report found, that of all AFS licence and credit licence applications that were approved by ASIC in 2018-2019, 60% were approved in a form different in scope to the licence authorisations sought by the applicant, or in form different to the standard conditions.

ASIC Executive Director Assessment & Intelligence, Warren Day said that ASIC is 'keen to foster a better understanding of the nature of ASIC's decision-making, what we consider when receiving an application and what is likely to increase the time required to consider an application'. As such, the report makes clear the information ASIC wants prospective applicants to be aware of when making an application for a new licence, licence variation or professional registration.

Mr Day said that ASIC 'encourages' prospective applicants to review the report to better inform their applications.

*[Source: ASIC media release 16/12/2019; Report 650 Overview of licensing and professional registration application: July 2018 to June 2019 (REP 650)]*



## In Brief | ASIC has reminded Australian financial services licensees who have not yet updated the Financial Advisers Register that they need to add new details about their financial advisers by 1 January 2020

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[Source: ASIC media release 16/12/2019]

**In Brief | Where is the line between general v personal financial product advice? The AFR reports that Westpac has made an application to appeal the decision in Australian Securities and Investment Commission v Westpac Securities Administration Limited [2019] FCAFC 187. Reportedly, Westpac will allege that 'the court ought to have found that the applicants did not provide personal advice to any relevant customers'**

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[Source: [registration required] The AFR 11/12/2019]

## Accounting and Audit

### **Slightly worse? ASIC audit inspection report released, ASIC has called on audit firms to accept the need to improve, ensure accountability and ensure strong leadership on the issue of audit quality**

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Australian Securities and Investments Commission (ASIC) Report 648 Audit inspection report for 2018–19 (REP 648) has found that auditors did not obtain reasonable assurance that the financial report was free from material misstatement in 26% of the key audit areas reviewed. The 26% figure relates to 207 key audit areas that ASIC reviewed across 58 audit files at 19 Australian audit firms of varying sizes.

**Slightly worse result than previously:** The results compare to 24% of key audit areas in the 18 months to 30 June 2018 and 25% in the 18 months to 31 December 2016.

**Problem areas:** The largest numbers of adverse findings were in two areas:

1. the audit of asset values, particularly impairment of non-financial assets and challenging the reasonableness of any forecasts, key assumptions, and the basis of valuation and the audit of revenue; and
2. the audit of revenue including accounting policy choices, substantive analytical procedures and tests of detail.

**Directors' role:** ASIC emphasises that directors are primarily responsible for the quality of the financial report. As such, ASIC says that directors and audit committees should consider (among other matters): a) non-executive directors recommending audit firm appointments and setting audit fees; b) reviewing the re's devoted to the audit, including the amount of partner time; c) assessing the level of professional scepticism exhibited by the auditor in challenging estimates and accounting policy choices; and d) ensuring independence of the auditor.

**Next steps?** To address the 'continuing overall level of findings', ASIC says that it will adopt a 'more intensive' supervisory and regulatory approach. ASIC's new regulatory initiatives include the following.

- **Implementing ASIC's 'why not litigate' approach** to auditor conduct matters
- **Increased transparency:** The report names and compares the findings in relation to the largest four audit firms
- **Audit firm governance review:** ASIC will conduct a review of conflicts of interest, culture, talent, governance and accountability for audit quality at the largest six audit firms. The review will be completed this financial year. The findings will be published in ASIC's inspection report for the 12 months to 30 June 2020 or in a separate report
- **Review of the analysis of root causes** conducted by audit firms on selected adverse findings from ASIC's financial reporting surveillances where net assets and profits were materially misstated. ASIC says it will consider whether the results of this review indicate a need to improve governance at the company and/or audit firm. ASIC says that this work has already commenced and will be completed by the end of 2020



- **Consultation on revising RG 260:** ASIC plans to consult in H1 2020 on whether [Regulatory Guide 260 Communicating findings from audit files to directors, audit committees or senior managers](#) (RG 260) should be revised to provide that ASIC would routinely report findings from its audit inspection file reviews directly to the directors or audit committee of the entity audited (as opposed to only doing so on an 'exception basis').
- **Release of Report 649:** Separately, but simultaneously ASIC released a report — [Report 649 Audit quality measures, indicators and other information: 2018–19](#) — outlining a 'broad group' of audit quality measures, indicators and other information to supplement the findings in Report 648. ASIC says that the report is intended to promote discussion on the measures/indicators that might be used by auditors/audit committees in monitoring initiatives to improve audit quality and good behaviours by audits/audit committees that support audit quality.

### Areas of focus for firms

Tables 16 and 17 of the report 648 (at p29) outline the areas on which audit firms should focus.

The top three areas are: 1) recognition of the need to improve (the extent to which all partners and staff embrace the need to improve audit quality and the consistency of audit execution); 2) accountability (whether partners/staff understand their roles in conduct quality audits and are held accountable for findings from firm quality reviews/external inspections); and 3) leadership (the extent to which leaders give strong and consistent messages to partners and staff that 'audit quality is non-negotiable').

*[Sources: ASIC media release 12/12/2019; Report 648 Audit inspection report for 2018–19 (REP 648); ASIC media release 12/12/2019; Report 649 Audit quality measures, indicators and other information: 2018–19]*

### Response from industry

Responding to the report, Chartered Accountants Australia and New Zealand (CA ANZ) Reporting & Assurance Leader Amir Ghandar said that the report is a 'timely compass for the audit profession on where we need to focus and improve audit quality'. Mr Ghandar said that industry 'take these results very seriously' and has a 'three-pronged approach' to respond to the findings. CA ANZ will: 1) disseminate specific learnings, tools and guides; 2) facilitate direct engagement between members and ASIC delving into the topics raised; and 3) build targeted training.

Mr Ghandar went on to say that CA ANZ recognises 'the clear need for the audit profession to improve which is one of the reasons why we are proposing a 15-point plan directly targeted at quality, confidence and the relevance of risks auditors are focused on, including strengthening prohibitions on non-audit services, oversight and skills of auditors, and how potential conflicts of interest are addressed. Taken as a whole, the measures underscore a process where ASIC's bar is rising, risk targeting is getting sharper, and this is overall leading to better outputs in the integrity of financial reporting. Notably, actual misstatements identified have steadily decreased down from 11% in 2015 to 2% in the latest report.'

Mr Ghandar welcomed ASIC increased focus on firm governance and culture, consideration of enforcement action and balanced scorecard incorporating a broader set of indicators. He added that CA ANZ 'encourage the regulator to provide more graduated information on how it views the severity of issues identified'.

*[Source: CA ANZ media release 12/12/2019]*

### Former Commonwealth auditor general Ian McPhee will reportedly Chair PwC's new external audit quality advisory board

The AFR reports that former Commonwealth auditor-general Ian McPhee will Chair PwC's new external audit quality advisory board. Mr McPhee will reportedly be joined on the board by former Tabcorp Holdings chief financial officer Damien Johnston and the University of Melbourne's Professor Margaret Abernethy.

Reportedly the advisory board's role is to challenge the firm on its audit and provide advice/guidance on audit quality issues, it will also reportedly have input on the remuneration of audit partners as it relates to audit quality.

*[Source: [registration required] The AFR 16/12/2019]*



## United Kingdom | The FRC has announced its 2020/21 corporate reporting and audit quality review program for 2020/21

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The UK Financial Reporting Council (FRC) has announced its thematic reviews of corporate reporting and audit areas of focus for 2020/21.

- **The FRC's Corporate Reporting Review team will undertake four thematic reviews** (to supplement its routine reviews of corporate reporting) as follows: 1) IFRS 16: review of disclosures in the first year of implementation; 2) cash flows and liquidity disclosures; 3) IFRS 15: a deeper dive; and 4) the effects of the decision to leave the EU on companies' disclosures.
- **The Corporate Reporting Review team will also contribute to a planned FRC-wide project focusing on climate change**, by reviewing the relevant disclosures given in companies' annual reports.
- **Areas of focus for audit monitoring** include auditors' work on: going concern and viability statements; the 'other information' in annual reports; long term contracts; the impairment of non-financial assets; fraud risk and the application of new accounting standards IFRS 15 and 16.
- **In selecting corporate reports and audits for review the FRC will prioritise certain higher risk sectors**, including: financial services; retail (retail property and travel and leisure); construction and materials; and manufacturing.

*[Source: FRC media release 13/12/2019]*

## United Kingdom | Banning (some) non-audit services? The FRC has issued a 'major revision' to its Ethical Standard and revised Auditing Standards

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The Financial Reporting Council issued what it terms a 'major revision' to its Ethical Standard and revised Auditing Standards. The new requirements will generally come into effect from 15 March 2020.

The FRC says that the changes deliver on the FRC's commitment to implement stronger UK ethical requirements and include banning auditors from providing recruitment and remuneration services or playing any part in management decision making. Overall, these changes are intended 'to strengthen auditor independence, prevent conflicts of interest and ensure the UK is seen as a destination to do business, because of stronger investor protection resulting from high quality audit' the FRC states.

The FRC adds that a decision on expanding which entities will follow the requirements has been deferred until after Sir Donald Brydon has issued his report, to ensure a consistent approach.

*[Source: FRC media release 17/12/2019; Accountancy Age 17/12/2019]*

## Risk Management

### Climate Risk

#### The State of New York has lost its case against ExxonMobil

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The State of New York has failed to establish that ExxonMobil misled shareholders over the costs of climate change and more particularly, did not establish that ExxonMobil 'either violated the Martin Act or Executive Law 63(12) in connection with its public disclosures concerning how ExxonMobil accounted for past, present and future climate change risks'.

Justice Ostrager [found](#) that the Office of the Attorney General 'failed to prove, by a preponderance of the evidence, that ExxonMobil made any material misstatements or omissions about its practices and procedures that misled any reasonable investor' given the 'context of the total mix of information available to the public'.

[Note: The full text of the ruling is available [here](#).]

#### Response?

- In a [statement](#), **Exxon Mobil** said that the ruling 'affirms the position ExxonMobil has held throughout the New York Attorney General's baseless investigation. We provided our investors with accurate information



on the risks of climate change. The court agreed that the Attorney General failed to make a case, even with the extremely low threshold of the Martin Act in its favor'. The statement goes on to say that 'Lawsuits that waste millions of dollars of taxpayer money do nothing to advance meaningful actions that reduce the risks of climate change. ExxonMobil will continue to invest in researching breakthrough technologies to reduce emissions while meeting society's growing demand for energy.'

- In a **statement**, **New York Attorney General Letitia James** said that 'despite this decision, we will continue to fight to ensure companies are held responsible for actions that undermine and jeopardize the financial health and safety of Americans across our country, and we will continue to fight to end climate change'.

### **Appeal? Possible, but unlikely?**

CNBC quotes Columbia University Law Professor John Coffee as saying that given the case was dismissed with prejudice, it cannot be tried again on the same facts in New York. Reportedly, Mr Coffee suggested that an appeal could possibly be lodged to the new York State Appellate Court.

Reportedly, Mr Coffee is of the view that a though 'it is conceivable that someone could allege violations of the federal securities laws and sue Exxon' bringing a federal case would be both 'very unlikely' and 'ill fated' given 'federal courts would have to respect this ruling'.

### **Implications for other similar cases (being brought/contemplated in other states)?**

In light of similar litigation already on foot/being contemplated in other states, The FT suggests that the decision could have a negative impact. The FT quotes Thunderbird School of Global Management in Arizona Professor Kannan Ramaswamy as saying that the decision 'signals potential holes in the arguments for the other cases of a similar nature pending in the state court in Massachusetts'.

*[Sources: Exxon Mobil media release 10/12/2019; NY Attorney General media release 10/12/2019; Ruling: People of the State of New York v Exxon Mobil Corporation; [registration required] The FT 11/12/2019; The New York Times 10/12/2019; CNBC 10/12/2019]*

## **In Brief | Europe to be the first climate neutral continent by 2050? The European Commission has released the European Green Deal which resets the Commission's commitment to tackling climate and environmental challenges**

*[Sources: European Commission media release 11/12/2019; The European Green Deal; [registration required] The WSJ 12/12/2019; [registration required] The FT 12/12/2019]*

## **Other Developments**

### **CBA has provided an update on its ongoing review of employee entitlements**

The Commonwealth Bank (CBA) has provided a status update on its ongoing review of employee pay and entitlements for current and former full time, part time and casual employees back to 2010.

#### **Key Points**

- The lender says that the review is now 'substantially complete' and will be finalised this financial year.
- CBA says that to date, it has paid \$13.2m of back-pay plus interest to approximately 41,000 current and former employees. The lender expects the remaining payments to be approximately \$25m (plus interest).
- The lender will commence payments of a further \$14.9m plus interest this week. In addition, CBA says that leave balances have been increased and additional superannuation contributions paid.
- CBA has financially provided for the issue, having raised a provision during the 2017-18 financial year, based on best estimates.
- CBA self-reported the review to the Fair Work Ombudsman (FWO) in February this year and has provided information to the FWO on the progress of the review. As previously disclosed, the FWO is conducting an investigation into the matter and CBA is co-operating with this process.
- CBA says it will provide a final update following the completion of its review.



- The statement adds that CBA has taken steps to ensure that the errors do not recur including the implementation of enhanced governance and controls and a new payroll system.

CEO Matt Comyn commented that 'it is unacceptable that some of our people were not paid the correct entitlements. This should never have happened and I apologise to anyone impacted by these past errors. Our priority is to complete the payments with interest and, where applicable, superannuation.'

Media reports have commented that the issue of worker underpayments appears to be widespread with a number of other entities (eg Woolworths and the ABC among others) implicated. Previously, Fair Work Ombudsman Sandra Parker has said she will raise the issue with boards around the country (see: Governance News 06/11/2019 at p19-20).

*[Sources: CBA media release 13/12/2019; SBS 14/12/2019; [registration required] The Australian 13/12/2019;*

### **Related News: Underpayment issue at NAB?**

The Australian reports that National Australia Bank (NAB) has identified an underpayment issue, reportedly impacting approximately 730 employees and involving \$850,000. Reportedly the Finance Sector Union has been informed and the Fair Work Ombudsman will also be notified.

The Australian quotes NAB chief people officer Susan Ferrier as saying 'We have let down our colleagues and it's not good enough'.

*[Source: [registration required] The Australian 17/12/2019]*

**In Brief | In his keynote address to the Australasian Business Ethics Network Conference, ASIC Commissioner John Price spoke about the importance of culture as a framework for ethical decision making and ASIC's work in promoting strong culture, including the work of the corporate governance taskforce. Mr Price explained that at the heart of the 'work of the corporate governance taskforce is a desire to build understanding and improve current corporate governance practices that can support changes towards a more ethical culture in business decision-making and so enhance trust in our financial system'**

*[Sources: Keynote address at the Australasian Business Ethics Network (ABEN) Conference by ASIC Commissioner John Price 09/12/2019; [registration required] The Australian 13/12/2019]*