Governance News

8 May 2019

Mark Standen
Partner

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

Siobhan Doherty
Partner

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

Kate Hilder
Consultant

T +61 2 9921 8785 |

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

Contents

Diversity 4

Top Story | ACSI calls for compulsory cultural reviews and (board) gender targets for listed entities 4

United States | Low director turnover is the key barrier to progress on board diversity on US boards according to a new study from Corporate Board 5

Remuneration 7

United Kingdom | Investors are unwilling to address excessive pay? A report from the High Pay Centre has found 'say on pay' reforms have been ineffective in addressing excessive executive pay 7

Institutional Shareholders and Stewardship 8

Top Story | ACSI calls for reform of Australia's investment stewardship framework 8

BlackRock, Vanguard and Fidelity under pressure to exercise their voting rights to apply pressure on companies to act to address climate risk........ 11

In Brief | Active as opposed to 'activist'? Are superannuation funds (and in particular industry funds) becoming more willing to exercise their power to influence decisions on specific social issues (eg labour reform), or is it just a question of 'active ownership'? The Australian quotes ACSI CEO Louise Davidson as dismissing claims that industry funds are increasingly 'activist'. 'It is about exercising our ownership rights and responsibilities. Active ownership is different to activism. You would be hard pressed to see us as campaigners on specific issues' she is quoted as saying 11

Other Shareholder News 11

United Kingdom | Most companies unlikely to appoint a worker a director? An LAPFF survey has found that most UK issuers will not opt to appoint employees to boards (to meet new Governance Code requirements), preferring instead to appoint a NED to represent worker interests 11

Meetings and Proxy Advisers 12

Recent AGM results: AMP, Woodside, Santos, Boeing 12

In Brief | #MeToo resolutions? Google is reportedly facing a number of shareholder resolutions calling on the company to implement various governance changes to address the 'diversity crisis'. One proposals reportedly calls on the company to disclose how it deals with sexual abuse claims 13

Directors' and Officers' Duties and Liabilities 13

What does 'challenging' management effectively look like in practice? The AICD has published insights from three experienced directors describing how they approach the challenge of balancing maintaining positive relations with management against testing executive views 13

Canada | Bill C-97 proposes (among other things) to amend s122 (duty of care of directors and officers) to include a new subsection 'Best interests of the corporation' 15

In Brief | Artificial intelligence as an antidote to board groupthink? A recent post on Harvard Law School Forum argues that AI has the potential to be more effective than existing strategies to counter group think on boards and thereby aid and improve (if not replace) board decision making 15

Disclosure and Reporting 15

In Brief | The AASB and AUASB have released the latest version of Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2. Originally published in December 2018, the paper contains several updates and guides directors, preparers and auditors when preparing and auditing financial statements. Even though the guidance is not mandatory, the AASB and AUSB states that it represents the IASB's best practice interpretation of materiality 15

In Brief | What does effective climate related disclosure look like? The Climate Disclosure Standards Board (CDSB) and the Sustainability Accounting Standards Board (SASB) have jointly released guidance to assist firms to more effectively implement the Task Force on Climate-related Financial Disclosure (TCFD) recommendations. The guidance includes examples of what effective disclosure looks like 15

Financial Services 16

Top Story | (Maybe) CAMAC 2.0? Labor plans (if elected) to establish a new Treasury based taskforce to 'fill the gap' left by the abolition of the Corporations and Markets Advisory Committee 16

ASIC not industry should write and administer mandatory codes of conduct? Choice and the Superannuation Consumers' Centre's joint submission to Treasury argues that the existing model of self-regulation needs to be rethought to better protect consumers against harm 17

Time to act to address unpaid superannuation: Unpaid Super Guarantee entitlements total $5.94bn according to an Industry Super Australia commissioned report 18

The AFR suggests that the joint venture between Catholic Super and Equip Super could provide a pattern for other smaller funds, seeking economies of scale, to follow 19

One regulatory regime for financial advisers? The FSC has issued a statement calling for the regulation of tax financial advisers to be streamlined under FASEA 19

APRA has called on the life insurance industry to urgently address concerns about the sustainability of individual disability income insurance (DII) 20

In Brief | The Australian reports that Federal Labor leader Bill Shorten has said that Labor (if elected to government) would consider creating a government owned bank out of Australia Post possibly modelled on the NZ government controlled Kiwi Bank which is a subsidiary of New Zealand Post 20

In Brief | APRA has released a letter to non-authorised deposit-taking institution (ADI) lenders seeking feedback on proposed amendments to the Economic and Financial Statistics data collection. The proposed changes would capture lending volumes from the non-ADI sector in a manner that allows direct comparisons to the ADI sector allowing APRA and the Council of Financial Regulators to assess the impact of non-ADI lending activity on financial stability and whether measures are required to address a potential escalation in risk. Submissions on the proposed changes are due by 1 June 2019 20

Accounting and Audit 20

In Brief | The International Auditing and Assurance Standards Board (IAASB) has published a discussion paper exploring possible options to address the challenges of applying the International Standards on Auditing (ISAs) to less complex entities and views on possible actions to address these challenges.   Consultation

closes on 12 September 2019. Feedback on this document is requested to the AUASB by 31 August 2019 from all interested stakeholders 20

In Brief | The AFR reports that the big four consulting firms: Deloitte, EY KPMG and PwC have faced/are facing a number of court actions over their auditing and advisory work 21

Risk Management 21

Cybersecurity and Privacy 21

Top Story | New board requirements and responsibilities: information security 21

Companies leading in cybersecurity share certain traits according to a Deloitte report 21

Climate Risk 22

United Kingdom | UK parliament has declared a state of Environment and Climate Emergency, CCC report recommends a new net-zero emissions target for the UK 22

Out of step with businesses on climate? A number of Australian businesses are reportedly reviewing their association memberships in response to Business Council of Australia 23

In Brief | Human action is causing mass global extinction: A landmark study, the Global Assessment of the Intergovernmental Science-Policy Platform for Biodiversity and Ecosystem Services (IPBES Assessment) presents evidence that biodiversity is necessary to human survival, that human action threatens more species with global extinction now than ever before, that existing goals are inadequate and makes the case for immediate, transformative change 23

Other Developments 24

United States | The CFTC has said that whistleblowers who report internally first, may be eligible for an 'enhanced' payment 24

Diversity

Top Story | ACSI calls for compulsory cultural reviews and (board) gender targets for listed entities

Overview: ACSI policy paper, Towards Improved Corporate Culture and Diversity

The Australian Council of Superannuation Investors (ACSI) has released a policy paper outlining two proposals to ensure company boards are focused on culture and diversity both of which are identified by ACSI as drivers of long-term shareholder value.

Key Takeouts

1. **Board gender quotas and regular cultural reviews**: ACSI proposes that: 1) all listed entities should be required to undertake regular cultural reviews and disclose the action taken; and 2) all listed entities should be required to set a time frame within which they will achieve board gender balance (40:40:20) and that if this is not achieved by 2025, regulatory intervention should occur
2. **ACSI (and ACSI members consider) long term sustainable investment to be 'underpinned' by strong culture and diversity:** 'Our members consider that long-term, sustainable investment is underpinned by sound management of environmental, social and governance (ESG) risks and opportunities. They recognise that good culture is not supplementary to effective management, but integral to it. They understand the link between corporate culture and organisational diversity. In particular, gender diversity can assist in developing corporate culture, with diverse directors more likely to identify a broader set of risks and opportunities, and a diverse board demonstrating the company's commitment to diversity and inclusion more broadly'.
3. **The announcement is part of ACSI's broader policy response to the Financial Services Royal Commission** which includes measures to strengthen corporate accountability and investment stewardship. An overview of ACSI's broader policy response is included in a separate post in this issue of governance news.

Context for the proposals

- **Culture can 'drive or discourage misconduct':** ACSI argues that as was identified by the recently completed Financial Services Royal Commission, and as is recognised more generally, poor culture is a key contributor to major behavioural and governance failings, which harm consumers, investors and markets
- **Investors view poor culture as a material risk to the value of their investments:** 'Poor corporate culture can have a profound impact on a company's reputation, social licence to operate and value. Loss of social licence to operate puts companies at risk of reputation damage, intervention by regulators, and loss of customer and community support. Accordingly, investors recognise that poor corporate culture is a material risk to the value of their investment'.
- **Long term sustainable investment is 'underpinned' by strong culture and diversity:** 'Our members consider that long-term, sustainable investment is underpinned by sound management of environmental, social and governance (ESG) risks and opportunities. They recognise that good culture is not supplementary to effective management, but integral to it. They understand the link between corporate culture and organisational diversity. In particular, gender diversity can assist in developing corporate culture, with diverse directors more likely to identify a broader set of risks and opportunities, and a diverse board demonstrating the company's commitment to diversity and inclusion more broadly'.

Policy Proposals

Proposal 1: Regular cultural reviews

All listed entities should be required to undertake regular cultural reviews and disclose the action taken

ACSI argues that despite 'the observations and focus on corporate culture, the pace of improvement in Australia has been slow' and that improvement is needed across the market. ACSI considers that 'the observations on culture from around the world, the CBA report and the Royal Commission' should apply to all listed entities and that all listed entities should be required to undertake regular culture reviews.

[Note: The CBA report referred to is the Australian Prudential Regulation Authority's (APRA's) prudential inquiry report into the CBA which was released last year (see: Governance News 04/05/2018). Among other things, the Financial Services Royal Commission's Final Report included a recommendation (recommendation 5.6) that every financial services entity should 'as often as reasonably possible' take steps to assess the culture and governance practices within their organisation, identify and address any issues identified and then evaluate the changes made. See: Governance News 11/02/2019]

Proposal 2: Gender balance on boards (of listed companies)

All listed entities should be required to set a time frame within which they will achieve board gender balance (40:40:20). If companies are unwilling to set a reasonable time frame or those targets do not improve diversity by 2025, regulatory intervention should occur.

ACSI explains that gender balance in this context means 40% men, 40% women and 20% 'unallocated' to allow flexibility. Commenting on this measure ACSI CEO Louise Davidson said that it is the next 'logical step' in supporting improved board diversity. ACSI considers that diverse boards 'make for better governed companies and maintain more effective oversight' of environmental, social and governance (ESG) risks and opportunities which ACSI considers to be 'intrinsically linked to the creation of long-term shareholder value'.

Broader context: ACSI's policy response to the Financial Services Royal Commission

The proposals form part of ACSI's broader policy response to the Financial Services Royal Commission. which includes, in addition to the reforms outlined in this post, measures to strengthen corporate accountability and also measures to strengthen investment stewardship and integrate ESG considerations into institutional investment decision making. A summary of ACSI's overall policy response is covered in a separate post in this issue of Governance News.

[Sources: ACSI media release 06/05/2019; Towards Improved Corporate Culture and Diversity 06/05/2019]

Response to the proposed 40:40:20 gender target?

- The AFR quotes Westpac and Transurban Chair Lindsay Maxsted as saying that though supportive of the 30% female board representation target, the push for new gender targets is 'premature'. Mr Maxsted reportedly said, 'The reason that I consider any further push to be premature is that, in general, the pool from which we should be recruiting is the senior executive, including CEO roles, and that is where most attention should be focused'.
- Noting that gender representation on ASX 200 boards has stalled, Australian Institute of Company Directors (AICD) CEO Angus Armour, reportedly agreed that achieving the 30% gender target should remain the focus. 'Our initial target of 30 per cent remains in place…The ASX100 met this target last year but once you move into the 100-200 it falls dramatically away. We think the 30% target should be the baseline and that remains the priority' he said.
- Graeme Samuel reportedly said that diversity of skills, thought, knowledge and experience rather than gender per se, is desirable. 'The targets are interesting but they are not the be-all and end-all for improving the quality of directors…We have to look at the talent pool available, which is much wider…It is not to diminish the importance of gender diversity but there is also diversity of culture and skills' he is quoted as stating.

[Source: [registration required] The AFR 07/05/2019]

United States | Low director turnover is the key barrier to progress on board diversity on US boards according to a new study from Corporate Board

Overview: *Corporate Board Practices in the Russell 3000 and S&P 500: 2019 Edition*

Corporate Board, has released its latest report into governance trends and developments in US public companies. According to the report, despite changes in governance practices and more particularly, the

demand for board refreshment and increased board diversity, the composition of many boards has remained largely unchanged due primarily to the extremely low rate of director turnover.

Some Key Points

Board composition

Gender diversity

- There has been modest progress over the past two years in response to increasing demands for (gender) diversity: In the S&P 500, female directors represent 22.5% of the total (up from 19.3% in 2016). In the Russell 3000, the proportion is 16.4% (up from 14.1% in 2016)
- While progress on gender diversity of corporate directors is being reported, 20% of firms in the Russell 3000 still have zero female directors. Even though women are elected as corporate directors in larger numbers than has been the case previously, almost all board chair positions remain held by men (only 4.1% of Russell 3000 companies have a female board chair, and 4.3% in the S&P500)
- Energy companies are the least diverse: Energy companies rank as the least diverse in terms of board committee leadership, with only 7.8% of their committees led by female director

Younger generations remain unrepresented

- The median age of board directors is 64 for the S&P 500 and 63 for the Russell 3000
- No director in either index is younger than 30 and outliers are far more likely to be older than younger: only 0.3% of directors in the Russell 3000 are younger than 36, while 2% are older than 80
- Only 10% of Russell 3000 directors and 6.3% of S&P 500 directors are aged 50 or younger, and in both indexes about one-fifth of board members are more than 70 years of age
- Across industries, utilities companies report the highest median director age (65 years), while communication services companies report the lowest (60 years)
- IT and communication services are the sectors with the highest concentration of new-economy businesses, and their companies' boards of directors appear to be younger: 51.8% of corporate directors serving on the boards of communication services companies and 47.2% of those on the boards of IT companies are 60 or younger

Zero change over the past two years? According to the report, the numbers show no change from those registered two years ago and nor do the numbers on the adoption of retirement policies based on age (only about 25% of Russell 3000 companies choose to use such policies to foster director turnover).

Board assessment

- **Board assessment is now widespread** among all but the smaller companies with 80% of Russell 3000 companies assessing their board's performance annually (up from 77% in 2016) and most companies also assess their committees' performance annually (77% of companies in the Russell 3000 and 93% in the S&P 500).
- **Individual director assessment less widespread (even in larger firms):** Though many board members consider the performance of at least one fellow director to be suboptimal, an institutionalised/systematic annual process for the assessment of individual directors continues to remain far less prevalent, even among larger organisations. In the Russell 3000, only 14.2% of companies report having instituted such an annual process (only a slight increase on 13.2% in 2016). In the S&P 500, less than 30% of companies report doing so. Only an additional 3.3% of Russell 3000 companies disclose having an individual director assessment process (but provide no information on its frequency); virtually all other firms in the index remain silent on the practice.
- **Use of outside professional facilitators to conduct board performance assessments is rarely disclosed**: Only 3.4% of Russell 3000 companies and 7.7% of S&P 500 companies disclose that they use independent assessors. 19.7% of Russell 3000 and 23.7% of S&P 500 companies state explicitly in their SEC filings that they do not involve any third party in the assessment process. 76.9% of Russell 3000 companies and 68.6% of S&P 500 companies are silent on the use of third-party assessors

Barriers to change?

The very low rate of director turnover remains the primary barrier to board refreshment/diversification.

- **The primary reason for the lack of progress on diversification of director skills/backgrounds/gender on US boards is identified as lack of board turnover.** 'Average director tenure continues to be quite extensive, board seats rarely become vacant and, when a spot is available, it is often taken by a seasoned director rather than a newcomer with no prior board experience'.
- **Directors are slow to step down:** Average director tenure exceeds 10 years and approximately 25% of Russell 3000 directors retire after 15+ years of service. The longest average board member tenures are seen in the financials (13.2 years), consumer staples (11.1 years), and real estate (11 years) industries.
- **Other barriers to change** identified in the report include:
  - Prior board experience remains a key consideration in appointing new directors: Despite the demand for more inclusiveness and a diverse array of skills, companies continue to value prior board experience in their director selection. Only 25% of companies elect a director who has never served on a public company board before though larger companies are more likely than smaller companies to do so. Companies with annual revenue of $20 billion or higher are twice as likely to elect two first-time directors as those with an annual turnover of under $1 billion (7.3% versus 3.2%).
  - Among smaller companies, staggered board structures are also a barrier to change: Almost 60% of firms with revenue under $1 billion continue to retain a classified board and hold annual elections only for one class of their directors, not all. And while just 9.5% of financial institutions with asset value of $100 billion or higher have director classes, the percentage rises to 44.1% for those with asset value under $10 billion.
  - Plurality voting remains a barrier to change: This voting standard allows incumbents in uncontested elections to be re-elected to the board even if a majority of the shares were voted against them. In the Russell 3000, 51.5% of directors retain plurality voting. Only 15.5% of the Russell 3000 companies have adopted some type of proxy access bylaws. Such bylaws allow qualified shareholders to include their own director nominees on the proxy ballot, alongside candidates proposed by management. In all other companies, shareholders that want to bring forward a different slate of nominees need to incur the expense of circulating their own proxy materials.

About the report: The report documents corporate governance trends and developments at 2,854 companies registered with the US Securities and Exchange Commission (SEC) that filed their proxy statement in the January 1 to November 1, 2018 period and, as of January 2018, were included in the Russell 3000 Index, as well as select findings from 494 companies listed in the S&P 500.

[Sources: [registration required] The WSJ 24/04/2019; Bizjournals 29/04/2019; The Conference Board media release 24/04/2019; [registration required] Executive Summary; [registration required] Full Report: Corporate Board Practices in the Russell 3000 and S&P 500: 2019 Edition]

Remuneration

United Kingdom | Investors are unwilling to address excessive pay? A report from the High Pay Centre has found 'say on pay' reforms have been ineffective in addressing excessive executive pay

The UK High Pay Centre has released a report: *The myth of shareholder stewardship: How Effectively Do Shareholders oversee FTSE 100 CEO Pay?* which examines the voting patterns of shareholders in FTSE 100 companies in AGMs between 2014 and 2018 ie over the first full five years of the 'say on pay' regime. The aim of the study was to assess the effectiveness of 'say on pay' in reducing executive pay levels.

Specifically, the report examines: a) the number of remuneration votes at shareholder AGMs that were defeated; b) the number of remuneration votes that received significant levels of dissent (ie over 20%); and c) average levels of dissent on remuneration votes.

[Note: Among the proposals put forward by The Australian Council of Superannuation Investors (ACSI) as part of its response to the Financial Services Royal Commission are proposals to enhance corporate accountability including the introduction of a binding shareholder vote on remuneration policy every 3 years to supplement the existing two strikes rule. See: Governance News 01/05/2019]

Some Key findings

- The report concludes that 'say on pay' has been ineffective in addressing excessive pay. Median executive pay for FTSE 100 CEOS is currently £3.9 million, 137 times the pay of the median full time worker across the UK as a whole.
- 100% of pay policies put to AGMs were approved by shareholders
- Combining votes on both remuneration reports and remuneration policy, the average level of dissent over the period was 8.8%, meaning that the average remuneration-related resolution passed with 91% shareholder approval
- 11.1% of over 700 remuneration-related resolutions attracted significant (ie over 20%) dissent.

The case for reform?

- The High Pay Centre argues that there are a number of reasons why investors are failing to hold companies to account using existing mechanisms including: a) that shareholders are disengaged, b) that they are risk averse (they view voting against executive pay demands as potentially risking the loss of a CEO); and c) that investment managers tend to benefit from a culture of very high pay.
- Polling shows that there is public dissatisfaction with existing measures and support for measures to address very high pay and economic inequality, including caps on top pay and worker representation on company boards.
- The High Pay Centre has called for corporate governance and stewardship structures to be 'opened' to stakeholders 'beyond shareholders', for example, through worker representation on company boards and remuneration committees. The report notes that the UK has taken some steps in this direction through reforms to the recently revised Corporate Governance Code but argues that the government needs to go further in order to rebuild public trust in business, address inequality, and 'deliver an economic model that rewards everyone fairly and proportionately for their work'.

[Note: The UK Local Authority Pension Fund Forum (LAPFF) has recently issued a statement outlining the results of a survey into how companies plan to meet a new requirement under the UK Corporate Governance Code to give employees a voice on boards. According to the LAPFF very few companies intend to appoint a worker director, to meet new Corporate Governance Code requirements. This is covered in a separate post in this issue of Governance News.]

Responding to the study, the Guardian quotes shadow business secretary Rebecca Long-Bailey as stating that 'Today's findings sadly tell us what we already know…policies have failed to tackle excessive executive pay in some businesses which is contributing to rampant inequality.'

[Sources: High Pay Centre media release 02/05/2019; The myth of shareholder stewardship: How Effectively Do Shareholders oversee FTSE 100 CEO Pay?; The Guardian 06/05/2019]

Institutional Shareholders and Stewardship

Top Story | ACSI calls for reform of Australia's investment stewardship framework

Overview: ACSI policy paper, Towards Stronger Investment Stewardship

As part of its broader response to the Financial Services Royal Commission, The Australian Council of Superannuation Investors (ACSI) has released a policy paper outlining two proposals to strengthen investment stewardship in line with global best practice and in line with growing ESG expectations.

Key Takeouts

1. **Call for action to strengthen investment stewardship:** The Australian Council of Superannuation Investors (ACSI) has called on the incoming government, regulators and investors to commit to strengthen investment stewardship and to mandate the integration of environmental, social and governance (ESG) considerations into investment decision making.
2. **ACSI is calling for two changes**: 1) explicit regulatory recognition (by APRA) of the importance of ESG issues in the formulation of investment strategies; and 2) a review of the regulatory framework for stewardship (including consideration of: the appropriate minimum standards and reporting, the regulatory framework and a stewardship code for institutional investors).
3. **Broader policy response to the Financial Services Royal Commission:** The two proposals are part of ACSI's broader policy response to the financial services royal commission which is summarised briefly at the end of this post.

The Australian Council of Superannuation Investors (ACSI) has released a third policy paper outlining two proposals to strengthen investment stewardship in line with global best practice and in line with growing ESG expectations. The proposals aim, ACSI says, 'to acknowledge the importance of environmental, social and governance (ESG) considerations to investment risk and returns and to strengthen investment stewardship by making it more consistent'. The proposals are part of ACSI's broader policy response to the Financial Services Royal Commission.

Proposals

Proposal 1: Integration of ESG considerations into APRA standards and guidance

Revision of APRA standards and guidance to explicitly recognise the importance of environmental, social and governance (ESG) issues in the formulation of investment strategies and a requirement for superannuation trustee boards to have access to capacity and competence on ESG issues.

ACSI's view is that ESG considerations have a material financial impact on investment value over the long term, and that this is insufficiently reflected in current APRA guidance or standards. Updating APRA's standards and guidance to integrate ESG considerations is appropriate, ACSI considers, because it would support stronger stewardship (the protection and enhancement of the long-term value of investments). It would also be an opportunity, ACSI suggests, to address confusion between ESG considerations and ethical investing (two different approaches) in current APRA guidance (SPG 530 Investment Governance).

The proposal is in line, ACSI writes, with the views expressed by Commissioner Hayne in the Financial Services Royal Commission's Final report.

In addition, ACSI argues that strengthening APRA's guidance and standards as proposed, would align with global investment practice (eg the UK Financial Reporting Council's (FRC's) proposed changes to the UK's Stewardship Code to require signatories to integrate stewardship into their investment approach and demonstrate how they take material ESG issues into account when fulfilling their stewardship responsibilities) and bring Australia up to date with other developed markets. Finally, ACSI notes that it is an area that APRA has said it will consider enhancing, and ACSI calls on the regulator to consult on revisions as soon as possible.

[Note: APRA recently released the results of its review of 2013 reforms of the superannuation prudential framework and flagged areas for potential further enhancement. Among them were enhancements to SPS 530 Investment Governance including (among other things) reviewing and updating the guidance on consideration of environmental, social and governance (ESG) factors in formulating investment strategy. See: Governance News 01/05/2019]

Proposal 2: Review the regulatory framework for stewardship.

The review should consider appropriate minimum standards and reporting, the appropriate regulatory framework, and a stewardship code that applies to all institutional investors.

In Australia, ACSI developed the Australian Asset Owner Stewardship Code (Code) which investors may adopt on a voluntary basis (see: Governance News 18/05/2018). Separately, the Financial Services Council (FSC) also has a number of relevant standards that apply to FSC members (not the market more broadly). ACSI argues that the 'benefits of a stewardship code that applies to a more comprehensive array of stakeholders are tangible' eg ACSI considers that where asset managers are signatories to the UK Stewardship Code, they both better equipped to judge the compatibility of their manager's stewardship commitments with their own and better able to meet asset owners' expectations.

It is ACSI's view that a stewardship code that is applicable to all institutional investors should be introduced, within an appropriate regulatory framework. This could be undertaken, ACSI suggests, in coordination with relevant stakeholders such as APRA and the Financial Services Council (FSC), and as part of a broader consultation on the regulatory aspects of stewardship.

[Note: The recently completed 'root and branch' independent review of the Financial Reporting Council (FRC) led by Sir John Kingman (the Kingman Review) found, among other things, that 'The Stewardship Code, whilst a major and well-intentioned intervention, is not effective in practice' and that a 'fundamental shift in approach' is needed to ensure that the revised Code more clearly 'differentiates excellence in stewardship' with a focus on 'outcomes and effectiveness, not on policy statements'. The Review states that 'If this cannot be achieved, and the Code remains simply a driver of boilerplate reporting, serious consideration should be given to its abolition'. See: Governance News 16/01/2019]

Not onerous?

The AFR quotes ACSI CEO Louise Davidson as stating that ACSI's proposed reforms are not onerous 'It's really about increasing transparency about stewardship activities, such as how you monitor assets and service providers, engaging with companies and proxy voting' and not about revealing investment secrets. 'We're really focused on the principles they [investors] use in their decision-making, and greater transparency about the issues that are important to them — for instance board composition, or remuneration' Ms Davidson added.

Context: ACSI's broader response to the Financial Services Royal Commission

The proposals put forward follow the release of two earlier policy papers: the first proposing four reforms to address corporate accountability (see: Governance News 01/05/2019) and the second aimed at strengthening corporate culture and diversity (covered in a separate post of this issue of Governance News.)

Together, ACSI states, the proposals respond to issues identified by Financial Services Royal Commission. ACSI CEO Louise Davidson said, 'The momentum for change is strong following the Royal Commission. Australia's policy makers and regulators have a significant opportunity to improve regulatory settings in ways that are good for consumers and investors, good for sustainable business practices, and in line with growing demand for investment stewardship ESG integration.'

Snapshot: ACSI's proposed reforms in response to the Financial Services Royal Commission

Corporate Accountability: ACSI proposes four measures to enhance corporate accountability: a) requiring a binding shareholder vote on remuneration policy every 3 years; b) requiring disclosure of CEO pay ratios to shareholders; c) introducing annual director elections; and d) permitting non-binding (advisory) shareholder resolutions.

Culture and Diversity: ACSI proposes two measures to strengthen corporate culture and diversity: 1) all listed entities should be required to undertake regular cultural reviews and disclose the action taken; and 2) all listed entities should be required to set a time frame within which they will achieve board gender balance (40:40:20) and that if this is not achieved by 2025, regulatory intervention should occur .

Effective Stewardship: ACSI proposes two measures to strengthen effective stewardship: 1) Revise APRA's investment guidance to explicitly recognise the importance of ESG issues in the formulation of investment strategies; and 2) Review the regulatory framework for stewardship. The review should consider appropriate

minimum standards and reporting, the appropriate regulatory framework, and a stewardship code that applies to all institutional investors.

[Sources: ACSI media release 08/05/2019; ACSI policy paper: Towards Stronger Investment Stewardship; [registration required] The AFR 07/05/2019; Money Management 08/05/2019]

BlackRock, Vanguard and Fidelity under pressure to exercise their voting rights to apply pressure on companies to act to address climate risk

Reportedly, a coalition of groups led by Majority Action has delivered over 129,000 petition signatures to BlackRock, Vanguard and Fidelity calling on them use their voting powers to help drive change on climate issues. Reportedly, the petition calls on asset managers to support climate related shareholder resolutions and to vote against the reelection of directors (where the directors in question are not supporting the long-term interests of investors) at a number of upcoming AGMs over the next nine weeks including: Amazon, ExxonMobil, Ford and General Motors.

Majority Action executive director Eli Kasargod-Staub is quoted as stating that, 'it is obvious that private dialogue is not yielding results nearly as fast or as ambitious as what is needed to match the urgency of this crisis. Shareholders are clear that the time for engagement without meaningful progress and action must come to an end.'

[Source: Investment Week 01/05/2019]

In Brief | Active as opposed to 'activist'? Are superannuation funds (and in particular industry funds) becoming more willing to exercise their power to influence decisions on specific social issues (eg labour reform), or is it just a question of 'active ownership'? The Australian quotes ACSI CEO Louise Davidson as dismissing claims that industry funds are increasingly 'activist'. 'It is about exercising our ownership rights and responsibilities. Active ownership is different to activism. You would be hard pressed to see us as campaigners on specific issues' she is quoted as saying

[Source: [registration required] The Australian 07/015/2019]

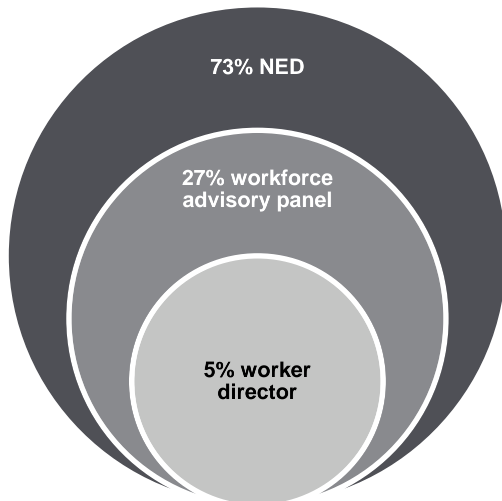
Other Shareholder News

United Kingdom | Most companies unlikely to appoint a worker a director? An LAPFF survey has found that most UK issuers will not opt to appoint employees to boards (to meet new Governance Code requirements), preferring instead to appoint a NED to represent worker interests

The UK Local Authority Pension Fund Forum (LAPFF) has issued a statement outlining the results of a survey into how companies plan to meet a new requirement under the UK Corporate Governance Code to give employees a voice on boards.

[Note: The revised UK Corporate Governance Code 2018 was released, following consultation in July 2018 (see: Governance News 15/12/2017; 23/07/2018). It applies to accounting periods beginning on or after 1 January 2019. Provision 5 of the Code outlines three possible options for companies to adopt to give the 'workforce' a voice: 'For engagement with the workforce one or a combination of the following methods should be used: a director appointed from the workforce; a formal workforce advisory panel; a designated non-executive director. If the board has not chosen one or more of these methods, it should explain what alternative arrangements are in place and why it considers that they are effective'. See: UK Corporate Governance Code 2018.]

Some Key Points



According to the LAPFF of the 66% of companies that have reached a decision about how they will meet the new requirement, the majority (73%) are planning to appoint a non-executive director; 27% plan to establish a workforce advisory panel; and small proportion — 5% (2 companies) — plan to appoint a director from the workforce

Eleven per cent of companies are yet to decide on what action they will take and 18% of respondents have decided to explain rather than comply.

Why not appoint a worker director? According to the LAPFF, the most common reason given for rejecting a worker director or a workforce advisory panel was the size of the workforce. Some companies said their workforces were too small while larger companies questioned how one person could represent a global workforce. Other objections included conflicts of interest, creating a distraction and delayed decision making.

'Disappointing' result: In a statement, LAPFF's acting chair, Cllr Paul Doughty said that the survey results are disappointing. 'Prime Minister 'Theresa May's plans for worker representation on boards were radical but companies are overwhelmingly taking the safe option of giving responsibility to a non-executive director. Companies have fallen well short of the prime minister's original pledge to give workers direct representation and shake up corporate governance. Companies' response shows a disappointing lack of innovation and imagination'. Noting that there are already a number of large UK public companies with worker directors, and that the practice is common in Europe, Mr Doughty said it was surprising that so many companies 'couldn't find a way to represent workers more directly than by giving responsibility to a non-executive director'.

About the survey: LAPFF wrote to FTSE All-Share companies between 15 February and 13 March 2019. The anonymised survey received 57 responses of which 39% were from FTSE 100 companies, 40% were from the FTSE 250 and 21% were small-cap companies. The responses represented 20% of the FTSE 100 and about 10% of the FTSE 350.

[Source: Local Authority Pension Fund Forum 01/05/2019]

Meetings and Proxy Advisers

Recent AGM results: AMP, Woodside, Santos, Boeing

AMP AGM: All resolutions were carried at the AMP AGM held on 2 May including the adoption of the remuneration report (which received 89.41% votes in favour, avoiding a second 'strike') and the reelection of Chair David Murray (87.31% votes in favour). Prior to the meeting, The Australian Shareholders' Association said it would not support the remuneration report because it considered that though AMP had reduced executive bonuses and committed to revise the remuneration structure, the new structure was yet to be finalised and lacked sufficient detail. The ASA also raised concerns about what it termed the 'excessive sign-on benefit' for the new CEO and the failure to seek shareholder approval of the sale of the life business. However the ASA indicated it would support Mr Murray's reelection on the basis of the value he brings to the board and to shareholders. According to The AFR, Australian Super, the Australian Council of Superannuation Investors (ACSI), CGI Glass Lewis, Institutional Shareholder Services (ISS) and Ownership Matters also said they would support Mr Murray's reelection. Climate Action group, Market Forces had urged shareholders to vote against Mr Murray's reelection due to his stance on climate risk. Separately, AMP also announced the appointment of John Patrick Moorhead as CFO (effective 1 June 2019) and the appointment of Marissa Bendyk as General Counsel Corporate and Governance and Group Company Secretary (effective 06/05/2019).

[Sources: AMP ASX Announcement: Results of AGM 02/05/2019; Appointment of new CFO 02/05/2019; Appointment of new General Counsel 06/05/2019; ASA media release 24/04/2019; Independent Financial Adviser 26/04/2019; [registration required] The SMH 22/04/2019; [registration required] The AFR 17/04/2019; 27/04/2019; 02/05/2019; Market Forces media release 02/05/2019]

Shareholder proposal to split the CEO/Chair role at Boeing defeated: A shareholder proposal calling for the combined Chair/CEO role at Boeing to be split, and for an independent Chair appointed, in the wake of the firm's response to two recent fatal 737 Max crashes, was reportedly rejected by shareholders at the recent AGM. Reportedly the proposal which if passed would have given directors the option to allow the incumbent CEO and Chair to retain his dual role, then split the roles once his eventual successor became CEO, was not supported by the Boeing board. Reportedly the board said that it reviews its governance structure annually and that it considered the proposed approach to be inappropriate: 'The Board should be able to select its leadership structure based on what will best serve shareholders' interests under the circumstances, not pursuant to an inflexible policy established in advance'. According to The WSJ, the proposal was rejected by 66% of shareholders, though support for the measure increased 9% to 34% as compared with last year (when a similar measure was proposed). Both Institutional Shareholder Services and Glass Lewis reportedly supported the proposed phased approach to splitting the dual Chair/CEO role, and advised shareholders to vote in favour of the resolution on that basis.

[Sources: [registration required] The WSJ 29/04/2019; MorningStar 29/04/2019; Bloomberg 17/04/2019]

Santos and Woodside: Though both Institutional Shareholder Services (ISS) and CGI Glass Lewis reportedly both advised shareholders to support all resolutions ahead of the Santos and Woodside AGMs (both of which were held on 2 May) they also reportedly raised concerns regarding bonuses paid, and the rigour of hurdles in place. More particularly, Glass Lewis reportedly raised concerns about Woodside's new incentive scheme, which combines short-term and long-term incentive plans on the basis that it considers that it overly focused on short term rather than long term performance. It's principle concern was reportedly the payment of 99.5% of the maximum short term incentive to the CEO which it viewed as 'overly generous'. Reportedly Glass Lewis said that its recommendation to support Santos's remuneration report was 'made on a very fine balance' and called on the company to address various matters in future. ISS also reportedly viewed the payment as 'excessive' compared to peers. Despite these concerns, remuneration reports at both companies received strong shareholder support. At Santos, the remuneration report received 98.41% support and the grant of share acquisition rights to the CEO received 98.46% support. At Woodside the remuneration report received 90.67% support (9.33% against). Directors seeking reelection also received strong support (all received less than 5% 'against' votes).

[Note: Both Santos and Woodside received notices from the Australasian Centre for Corporate Responsibility (ACCR) in March requesting resolutions be put to shareholders on carbon emissions targets/disclosure but both firms determined the resolutions to be invalid. As such they were not considered at the AGMs. See: Woodside media release 04/03/2019; Governance News 13/03/2019.]

[Sources: Woodside ASX Announcement: Results of Annual General Meeting: 03/05/2019; Santos ASX Announcement: Results of Annual General Meeting: 02/05/2019; Glass Lewis Blog 17/04/2019; [registration required] The AFR 24/04/2019; [registration required] The Australian 03/05/2019; [registration required] The AFR 03/05/2019]

In Brief | #MeToo resolutions? Google is reportedly facing a number of shareholder resolutions calling on the company to implement various governance changes to address the 'diversity crisis'. One proposals reportedly calls on the company to disclose how it deals with sexual abuse claims

[Source: [registration required] The Times 06/05/2019]

Directors' and Officers' Duties and Liabilities

What does 'challenging' management effectively look like in practice? The AICD has published insights from three experienced directors describing how they approach the challenge of balancing maintaining positive relations with management against testing executive views

The Australian Institute of Company Directors (AICD) writes that in the context of recent calls for boards to more effectively 'challenge' management (eg in APRA's report into the CBA, and the Financial Services Royal Commission's Final Report) the question of how boards manage to balance the need to test executive views while also maintaining relations is increasingly topical.

'Boards that aggressively challenge executives, treat management information like homework that needs checking, or play "gotcha" to catch out people, can do irreparable damage. Inevitably, management becomes

guarded and less communicative with the board. Equally, boards that are too polite or unwilling to call out management – and keep the blowtorch on issues until they are satisfied – can destroy stakeholder value. Worse, such boards become cheerleaders for the organisation and blinded to management shortcomings' the AICD observes.

How do directors navigate the need to test executive views and the need to maintain positive relations? Three approaches

The article outlines insights from three experienced directors into how they navigate this challenge. All agree, and emphasise that a constructive (as opposed to a combative) approach to testing management decisions is key.

Collaborative approach: Frank Cooper AO FAICD, a non-executive director of South32 and Woodside Petroleum, Chair of the Insurance Commission of WA, and Division Council president of AICD WA, says the starting point for boards challenging management is to take a constructive and collaborative (as opposed to a combative approach): 'In essence, I'm asking management to break down an issue and show me how it got to the result. For example, assumptions behind a forecast might be discussed. If they are not able to satisfy me, we will usually agree that there is something that needs more work' he says. For example, he suggests directors should start by: establishing a mutuality of interest, focus on the issue/problem rather than on the person; frame queries carefully and give management sufficient notice of any material issues.

Mr Cooper also suggests that directors should endeavour not to automatically dismiss what they may consider to be the 'left field' views of other directors. 'Good boards take time to understand why a director is uncomfortable with an issue, even if the other directors do not see it as a problem…The value of diversity is having directors with different skills and perspectives coming together to test complex issues – and not being afraid to raise them with management or pursue the matter if they are not satisfied with the answer' he is quoted as stating.

Finally, Mr Cooper suggests that 'creative tension' on the board is valuable in combatting 'group think'. 'The last thing you want is boards being too polite, afraid to ask seemingly basic questions and every director nodding in agreement as group-think sets in' he is quoted as stating.

Industry experience on boards is critical: Dr Sarah Ryan, a non-executive director of Woodside Petroleum, Viva Energy Australia, MPC Kinetic and Akastor ASA, a Norwegian oil-services investor, reportedly emphasised the importance of industry experience on boards as key to enabling the board to challenge management constructively (though she said that directors without industry experience also add value). She also suggested that planned board interaction with the executive team, middle management and front line staff assists the board to understand the firm's 'pulse'.

In addition, Dr Ryan made the point that a collaborative approach to testing board decisions was likely to be more productive than the alternative. 'I'll ask an executive to take me through an issue and I'll provide feedback where necessary. The goal is to provide a different insight rather than take a bruising approach. I find management really appreciates it when you give a view it has not considered and it encourages new thinking' she is quoted as stating.

Boards should take a proactive approach to addressing concerns with management to avoid an adversarial relationship building up: Steven Cole, FAICD, chairman of Neometals, Perth Markets and the Queen Elizabeth II Medical Trust, and a non-executive director of Matrix Composites & Engineering, is quoted as stating that boards should take a 'proactive rather than reactive' approach to addressing concerns with management. 'When directors let these doubts linger for too long, inevitably an adversial relationship between board and management forms. Executives start to detest board meetings, guard information and discount the board's view. It becomes harder for the board to challenge management views because it starts to appear to become personal. If the board senses that management is not up to the job, it needs to make changes, rather than keep fighting the CEO and executive team.'

Mr Cole added that he considers it to be good practice for boards to end each meeting with a closed session where executives leave the room. 'It's better to raise any concerns about management in this session rather than have directors talking in the background, losing confidence in the CEO and attacking management every time it presents something to the board' he reportedly said.

Finally, Mr Cole said that executive teams also need to be prepared to engage with the board. 'In my experience, the best executive teams want board input, they engage with directors, share information and value being challenged by the board. They don't want directors who agree with everything they say. They value the opportunity of working with people that encourage a high level of thinking, can pull apart ideas, add value and are not afraid to hold others accountable. They are accepting of board meetings that are a little uncomfortable at times because of productive debate' he is quoted as stating.

[Source: AICD blog 11/05/2019]

Canada | Bill C-97 proposes (among other things) to amend s122 (duty of care of directors and officers) to include a new subsection 'Best interests of the corporation'

Among other things, Bill C-97 (*Budget Implementation Act 2019 No 1*) proposes to amend the Canada *Business Corporations Act 1985* to:

1. **set out factors that directors and officers of a corporation may consider when acting with a view to the best interests of that corporation:** Section 122 of the *Canada Business Corporations Act 1985* (Duty of care of directors and officers) provides (in subsection (1)) that 'Every director and officer of a corporation in exercising their powers and discharging their duties shall (a) act honestly and in good faith with a view to the best interests of the corporation; and (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances'. The Bill proposes to add a new subsection 122 (1.1) Best interests of the corporation, which would provide that: 'When acting with a view to the best interests of the corporation under paragraph (1)(a), the directors and officers of the corporation may consider, but are not limited to, the following factors: (a) the interests of (i) shareholders, (ii) employees, (iii) retirees and pensioners, (iv) creditors, (v) consumers, and (vi) governments; (b) the environment; and (c) the long-term interests of the corporation'.
2. **require directors of certain corporations to disclose information relating to 'diversity, well being and remuneration'** to shareholders.

The Bill has progressed to second reading stage in the House of Commons and has been referred to committee for consideration.

[Source: Bill C-97 An Act to implement certain provisions of the budget tabled in Parliament on March 19, 2019 and other measures]

In Brief | Artificial intelligence as an antidote to board groupthink? A recent post on Harvard Law School Forum argues that AI has the potential to be more effective than existing strategies to counter group think on boards and thereby aid and improve (if not replace) board decision making

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 01/05/2019; [registration required] Kamalnath, Akshaya, The Perennial Question for Board independence — Artificial intelligence to the rescue? (March 26, 2019). Albany Law Review, Forthcoming. Available at SSRN]

Disclosure and Reporting

In Brief | The AASB and AUASB have released the latest version of Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2. Originally published in December 2018, the paper contains several updates and guides directors, preparers and auditors when preparing and auditing financial statements. Even though the guidance is not mandatory, the AASB and AUSB states that it represents the IASB's best practice interpretation of materiality

[Source: Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2 April 2019]

In Brief | What does effective climate related disclosure look like? The Climate Disclosure Standards Board (CDSB) and the Sustainability Accounting Standards Board (SASB) have jointly released guidance to assist firms to more effectively implement the Task Force on Climate-related Financial

Disclosure (TCFD) recommendations. The guidance includes examples of what effective disclosure looks like

[Sources: Sustainability Accounting Standards Board media release; [registration required] Climate Disclosure Standards Board, Sustainability Accounting Standards Board: TCFD implementation guide]

Financial Services

Top Story | (Maybe) CAMAC 2.0? Labor plans (if elected) to establish a new Treasury based taskforce to 'fill the gap' left by the abolition of the Corporations and Markets Advisory Committee

Shadow Assistant Treasurer, Andrew Leigh has announced that if elected, the Federal Labor party plans to establish a Treasury based, Competition and Growth Taskforce to 'fill the gap' left by the abolition of the Corporations and Markets Advisory Committee (CAMAC). Mr Leigh said that the taskforce will complement Labor's policies for the cooperative or mutual sector by streamlining regulations and breaking down barriers for new competitors.

Mr Leigh added that 'Through the Taskforce, Labor will look at ways to encourage managers to take a long view; examine the market concentration of firms and what steps could be taken to encourage capital ownership across firm types; and explore the recognition of non-corporate forms and potential government policy responses to the findings'.

Details

- **Composition:** The Taskforce will be based within the Treasury and include staff from diverse backgrounds including not-for-profits, superannuation and the cooperative and mutuals sector.
- **Funding:** The Taskforce would be allocated $3 million over the forward estimates.
- **Responsibilities:** The Competition and Growth Taskforce's 'overarching responsibilities' will be to 'examine the structure, distribution and effects of capital ownership in Australia.' This will encompass issues tasked to it by government, and independent research and policy development.

Five immediate priorities:

1. **Corporate governance reform**, 'filling the gap left by the abolition of the Corporations and Markets Advisory Committee'. The Taskforce would be asked to immediately focus on completing the Annual General Meeting and Shareholder Engagement report that the CAMAC commenced.

[Note: CAMAC's discussion paper on AGM and shareholder engagement and submissions received in response can be accessed on the CAMAC website here.]

2. **'Guiding the remaining recommendations' of the Senate Economics References Committee Inquiry into Co-ops and Mutuals**

[Note: This appears to be a reference to the 2015 inquiry into the role, importance, and overall performance of cooperative, mutual and member-owned firms in the Australian economy. The report, the government's response (which was released 8 November 2017) and submissions can be accessed on the parliamentary website here.]

3. **Reviewing national harmonisation of cooperative laws**, including: a) exploring the referral of state powers (legislated under the Cooperatives National Law) to the federal government; and b) bringing cooperatives into the proposed Director Identification Number (DIN) regime.

[Note: Bills to introduce Director Identification Numbers and to 'modernise' business registers — The *Commonwealth Registers Bill 2019* and the *Business Names Registration (Fees) Amendment (Registries Modernisation) Bill 2019* were introduced during the last parliament but are not proceeding. The Bills (and related Bills*: Business Names Registration (Fees) Amendment (Registries Modernisation) Bill 2019*, the *Corporations (Fees) Amendment (Registries Modernisation) Bill 2019* and the *National Consumer Credit Protection (Fees) Amendment (Registries Modernisation) Bill 2019*) were referred to the Economics Legislation Committee on 14 February, for report by 26 March. The Committee made three recommendations, including that the Bills be passed. See: Governance News 20/02/2019]

4. **Making recommendations to government on small business transition policies** – particularly in relation to small business owners who wish to sell their business to their employees upon retirement as a worker-owned cooperative.
5. **Guiding policy on encouraging employee ownership**, including employee share ownership schemes.

Industry response to Labor's announcement has reportedly been positive

- **Governance Institute of Australia (GIA)** CEO Megan Motto is quoted as welcoming the announcement and approving of the Taskforce's immediate focus on completing the Annual General Meeting and Shareholder Engagement Report that CAMAC started. 'In an election campaign that hasn't had much of a focus on business and the regulatory burdens it faces, it's good to see politicians taking up the challenge…We support any measure by government to streamline regulatory burdens, boost growth and productivity, and encourage healthy competition.'
- **Australian Institute of Company Directors (AICD)** CEO Angus Armour is quoted in The AFR as saying that it is importance to have an said independent expert voice on corporate law, 'with the speed and significance of changes to corporate law, there is a genuine need for a CAMAC-style function'.
- The AFR quotes **Business Council of Co-operatives and Mutuals** CEO Melina Morrison as welcoming the announcement stating that 'rediscovering this transparent, member-owned business model can provide Australia with a model and a road map in an era in which we are all demanding more accountability of our institutions.'
- In a statement, the **Customer Owned Banking Association** (COBA) has welcomed' Labor's announcement as a positive development for the sector.

[Sources: Andrew Leigh MP media release 02/05/2019; [registration required] The AFR 02/05/2019; [registration required — accessed via LexisNexis Capital Monitor] Customer Owned Banking Association media release 02/05/2019; MyBusiness 03/05/2019]

ASIC not industry should write and administer mandatory codes of conduct? Choice and the Superannuation Consumers' Centre's joint submission to Treasury argues that the existing model of self-regulation needs to be rethought to better protect consumers against harm

Context: Treasury released a consultation paper seeking feedback on relevant considerations in amending the law to implement Financial Services Royal Commission Recommendation 1.15 (enforceable code provisions) on 18 March. Consultation closed on 12 April. (See: Governance News 20/03/2019).

Choice/Superannuation Consumers' Centre submission to Treasury on how best to implement Financial Services Royal Commission Recommendation 1.15

The submission argues that the Hayne Commission demonstrated that self-regulation in financial services has failed and that industry codes have proven to be inadequate in addressing widespread consumer harm. The submission cites the Insurance in Superannuation Voluntary Code of Practice as an example of this.

The submission makes eight recommendations.

- **ASIC should draft industry codes:** The incoming Federal government should legislate to enable the Australian Securities and Investments Commission (ASIC) to draft and administer industry codes
- **Entire industry codes (not specific provisions) should be enforceable** and mandated by ASIC
- **Stronger powers for ASIC**: The incoming Federal government should grant ASIC broad rule-making powers, similar to the United Kingdom Financial Conduct Authority
- **Civil penalties should be attached to individual breaches of industry codes.** Breaches of a civil penalty provisions should have a maximum penalty the greater of 300 penalty units or three times the benefit derived or detriment avoided
- **Serious breaches:** Breaches of industry codes that are 'egregious or systematic in nature' should be considered breaches of

the obligations under s912A(1) of the *Corporations Act 2001 (Cth).*

- **Monitoring bodies:** To ensure compliance with industry codes, strong and independent code monitoring bodies are required. As a minimum these bodies should: be independent from industry; be well funded and resourced to ensure compliance; have adequate powers to guarantee compliance; and have a balance of ASIC appointed consumer advocates, industry members and independent experts on its panel.
- **Name and shame companies in breach:** The code monitoring body should publicly report breaches of industry codes; name companies that breach the code; and provide specific reasoning for breaches of the code to guide future policy making
- **existing consumer protections need to be upheld** 'to ensure that ACFA's [sic] decisions are non-binding so individuals are free to pursue the decision in a court or tribunal'.

Industry is opposed? According to the Age, banking and insurance sectors have responded by rejecting the recommendations, arguing against the need to move away from the existing model of self-regulation.

[Sources: [registration required] The Age 06/05/2019; Choice media release 06/05/2019; Choice Submission to Treasury; Making Industry Codes Work]

Time to act to address unpaid superannuation: Unpaid Super Guarantee entitlements total $5.94bn according to an Industry Super Australia commissioned report

A report commissioned by Industry Super Australia (ISA) entitled *Super Scandal: unpaid super guarantee in 2016-17*, based on Australian Tax Office data from 2016/17 has found:

- a total of 2.85 million workers (up 90,000 since 2013-14) have missed out on $5.94bn in unpaid superannuation entitlements (more than $2,000 per employee each year)
- on average, a worker who receives their superannuation guarantee entitlements ends up with 50% more super than a worker underpaid their super entitlements
- the average gap in retirement savings (due to unpaid superannuation guarantee entitlements) has widened to $24,506 for 2016-17 (up from $19,709 in 2013-14)
- super guarantee underpayment occurs over several years and leads to cumulative disadvantage
- the three main risk factors for being underpaid superannuation are identified as: 1) being aged under 35; 2) earning under $30,000 per annum; 3) having a blue collar occupation (eg machinery operator, labourer, technician or trade worker). ISA estimates that 2.13 million of the 2.85 million super guarantee eligible people (75%) who are underpaid (75%) have one of these main risk factors. The group with one or more of the main risk factors has a 36.3% chance of being underpaid compared to the general risk of 31.3%.
- rogue employers are using salary sacrifice contributions to reduce their super guarantee obligation for those workers. Consequently, over 370,000 workers who contribute to their superannuation through salary sacrifices have lost over $1.5bn due to employers counting this as a superannuation contribution.

Four suggested reforms to address the problem

The report includes four suggested actions to address the issue.

1. **Mandate payment of superannuation with payment of salary to reduce noncompliance:** Under current laws, employers can make super contributions on a quarterly basis. The ISA writes that research shows that some employers take advantage of this flexibility by delaying super contributions well beyond three months leading to large liabilities that cause cash-flow difficulties. The report argues that changing the law to mandate employer's payment of superannuation at the time of an employee's will allow payments to be more closely tracked by both employees and the ATO, thereby reducing non-compliance.
2. **Better monitoring and stronger enforcement**: The report argues that the Australian Taxation Office, despite collecting significant quantities of data, 'carries out too

little proactive enforcement of unpaid super' and argues that the monitoring, reporting and enforcement obligations on the ATO should be strengthened. In addition, the report calls for other relevant agencies to have greater scope to work with the ATO to recover unpaid super including the Fair Work Ombudsman and super funds acting on behalf of members.

3. **Penalties should be utilised:** The report observes that under current laws, company directors are personally liable for unpaid super and financial penalties for employers of up to 200% can be imposed, though rarely occurs in practice. In addition, new laws include criminal penalties for employers who refuse to pay a superannuation guarantee charge liability. The report argues that to provide 'adequate deterrence' such penalties must be utilised rather than being discretionary. 'Few other breaches of the law involve optional penalties' the report states.

4. **Extending the safety net for unpaid entitlements:** The report argues that the Fair Entitlements Guarantee (FEG) should be expanded to include unpaid superannuation.

Commenting on the report, Australian Council of Trade Unions (ACTU) Assistant Secretary Scott Connolly said that the report findings indicate the lack of action on addressing the issue, and noted that the Federal Labor Party have agreed to support measures to recover unpaid superannuation. He added that 'We need to change the rules to make sure people can recover the super they're owed. Working people shouldn't have to wait for the ATO to chase up underpayments. They should have fast, efficient access to justice when their super is unpaid.'

[Sources: Super Scandal: unpaid super guarantee in 2016-17; The ABC 03/05/2019; ACTU media release 03/05/2019]

The AFR suggests that the joint venture between Catholic Super and Equip Super could provide a pattern for other smaller funds, seeking economies of scale, to follow

The AFR reports that Catholic Super and Equip Super have entered into a joint venture which creates a $26 billion fund. Reportedly, the joint venture has a number of advantages including:

1. it utilises Equip Super's extended public offer licence to allow default super arrangements to remain in place for the separate funds while merging the administration and investment management to deliver better member outcomes.
2. The two funds have also agreed to have a single trustee board with 12 members comprised of one third employer directors, a third member directors and a third independent directors. Seven directors will be drawn from the existing Equip Super board and five from the Catholic Super board.

The AFR comments that the move appears to be in line with the Australian Prudential Regulation Authority's expectations and suggests that the joint venture would serve as a good pattern for other smaller funds to follow.

[Source: [registration required] The AFR 01/05/2019]

One regulatory regime for financial advisers? The FSC has issued a statement calling for the regulation of tax financial advisers to be streamlined under FASEA

The Financial Services Council (FSC) has called for the regulation of tax financial advisers (TFAs) to be streamlined into a single regulatory regime under the Financial Adviser Standards Ethics Authority (FASEA) in a submission to the Government's independent review of the effectiveness of the Tax Practitioners Board (TPB) and the Tax Agent Services Act 2009 (TASA).

Collapsing the two regimes into a single regime would mean consumers do not need to engage with the TPB for the tax component of the advice they receive, as well as a monitoring body under the FASEA framework for the financial advice received. It would also lift standards overall, according to the FSC.

[Source: Financial Services Council media release 06/05/2019]

APRA has called on the life insurance industry to urgently address concerns about the sustainability of individual disability income insurance (DII)

The Australian Prudential Regulation Authority (APRA) has written to life insurers calling on them to urgently address concerns about the sustainability of individual disability income insurance (DII) (also called income protection insurance). APRA said it has been concerned about DII sold to individuals (rather than provided through superannuation in the form of group insurance) due to its ongoing poor performance. The industry has collectively lost $2.5 billion through this product offering over the past 5 years, with no signs of improvement, APRA said.

In a letter to DII providers APRA said its thematic review of the industry, which included onsite reviews with the eight largest providers of DII, found issues with insurers' strategy and risk governance, pricing and product design, as well as inadequate data and resourcing.

APRA Executive Board Member Geoff Summerhayes said most life companies have long been aware of the issues, but their efforts to address them have so far been inadequate. 'Unless these adverse trends are reversed, there is a risk some life companies will ultimately exit the market for DII, worsening consumer outcomes through reduced competition, accessibility and affordability' Mr Summerhayes said.

Deadlines for providers to action APRA's concerns

APRA said it is setting deadlines for each life insurer to start taking a range of steps in response to its concerns, including formulating a strategy to address the issues identified by the thematic review, and reviewing DII product design and pricing practices.

More particularly:

- **The life companies involved in the thematic review have eight weeks** to provide APRA with a detailed outline of how they intend to fulfil these requirements. If either their action plan or progress implementing it is inadequate, APRA states that it will 'step up our supervisory intensity of that life company and consider imposing an increase in its minimum capital requirements'.
- **Other life companies involved in the provision of DII products are also required to take action by submitting a self-assessment against APRA's findings**. Mr Summerhayes added that APRA's expectation is that all life companies examine whether the same types of issues exist in their other product groups eg total and permanent disability insurance.

[Sources: APRA media release 02/05/2019; APRA Letter: Thematic review of individual disability income insurance — phase two 02/05/2019; [registration required] The Australian 03/05/2019; SBS 02/05/2019; Investor Daily 03/05/2019]

In Brief | The Australian reports that Federal Labor leader Bill Shorten has said that Labor (if elected to government) would consider creating a government owned bank out of Australia Post possibly modelled on the NZ government controlled Kiwi Bank which is a subsidiary of New Zealand Post

[Source: [registration required] The Australian 07/05/2019]

In Brief | APRA has released a letter to non-authorised deposit-taking institution (ADI) lenders seeking feedback on proposed amendments to the Economic and Financial Statistics data collection. The proposed changes would capture lending volumes from the non-ADI sector in a manner that allows direct comparisons to the ADI sector allowing APRA and the Council of Financial Regulators to assess the impact of non-ADI lending activity on financial stability and whether measures are required to address a potential escalation in risk. Submissions on the proposed changes are due by 1 June 2019

[Sources: APRA letter 01/05/2019; [registration required] The Australian 02/05/2019]

Accounting and Audit

In Brief | The International Auditing and Assurance Standards Board (IAASB) has published a discussion paper exploring possible options to address the challenges of applying the International Standards on Auditing (ISAs) to less complex entities and views on possible actions to address these

challenges. Consultation closes on 12 September 2019. Feedback on this document is requested to the AUASB by 31 August 2019 from all interested stakeholders

[Sources: International Federation of Accountants media release 29/04/2019; AASB media release 29/04/2019; Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the International Standards on Auditing (ISAs)]

In Brief | The AFR reports that the big four consulting firms: Deloitte, EY KPMG and PwC have faced/are facing a number of court actions over their auditing and advisory work

[Source: [registration required] The AFR 07/05/2019]

Risk Management

Cybersecurity and Privacy

Top Story | New board requirements and responsibilities: information security

APRA prudential standard CPS 234 imposes additional obligations on regulated entities in matters of information security, and requires company boards to take more responsibility in ensuring the security of the data they hold.

MinterEllison's Anthony Borgese, Alexander Horder, Aaron Bicknell have written an article providing their insights into the implications of the new requirements.

The full text of the article can be accessed on the MinterEllison website here: https://www.minterellison.com/articles/new-board-requirements-and-responsibilities-information-security

Companies leading in cybersecurity share certain traits according to a Deloitte report

Deloitte (in collaboration with the Financial Services Information Sharing and Analysis Center (FS-ISAC)) has released a report: *Pursuing cybersecurity maturity at financial institutions* presenting the results of a survey measuring 'good stewardship' of cybersecurity budget and the maturity of cyber-risk management programs in financial institutions.

Some Key Points

- **Leading companies (from a cybersecurity perspective) share certain traits:** Companies that have reached the highest cybersecurity maturity level ('adaptive companies') as defined by the National Institute of Standards and Technology (NIST) were found to share several core traits including: a) involvement of senior leadership, executives and the board; b) cybersecurity's profile within the organisation was raised beyond the IT department to give it greater prominence; and c) cybersecurity efforts were more closely aligned with the company's business strategy.
- **Spend on cybersecurity?** Respondents spent between 6 to 14% of their IT budget on cybersecurity, with an average of 10%. This amount equates to a range between 0.2% to 0.9% of company revenue. Overall, larger companies spend more than smaller organisations. Small firms spent a lower percentage of their revenue (0.2%) on cybersecurity than did midsize (0.5%) or large (0.4%) companies.
- **Spend alone is not an indication of maturity level:** The survey found that those with the highest maturity level did not necessarily spend more than the overall average on their cybersecurity programs. 'That likely means exactly how—and how well—financial institutions go about securing their digital fortress is at least as important as the amount of money devoted to cybersecurity'.
- **Ongoing task:** Even highly mature organisations need to continue to adapt and to prioritise cybersecurity due to the rate at which change is occurring. 'Cybersecurity will remain a work in progress for all financial organisations. Indeed, regardless of who is ultimately in charge and how governance is structured, cybersecurity awareness, responsibility, and accountability should be part of every department within every financial services firm'.

[Source: Deloitte Insights: Pursuing cybersecurity maturity at financial institutions 01/05/2019]

Climate Risk

United Kingdom | UK parliament has declared a state of Environment and Climate Emergency, CCC report recommends a new net-zero emissions target for the UK

Last week, the UK parliament passed a non-binding resolution declaring a climate emergency. Separately, the Committee on Climate Change report, *Net Zero - The UKs contribution to stopping global warming* recommended setting a new zero emissions target to be achieved by 2050. In Australia, the Greens and climate groups are calling for a similar declaration to be passed.

A high level overview of these development is below.

The UK Parliament has declared a climate emergency

On 1 May, the British Labour party moved a non-binding motion in the House of Commons to declare 'an environment and climate emergency', which was passed with bi-partisan support.

The Motion: 'That this House declares an environment and climate emergency following the finding of the Inter-governmental Panel on Climate Change that to avoid a more than 1.5°C rise in global warming, global emissions would need to fall by around 45 per cent from 2010 levels by 2030, reaching net zero by around 2050; recognises the devastating impact that volatile and extreme weather will have on UK food production, water availability, public health and through flooding and wildfire damage; notes that the UK is currently missing almost all of its biodiversity targets, with an alarming trend in species decline, and that cuts of 50 per cent to the funding of Natural England are counterproductive to tackling those problems; calls on the Government to increase the ambition of the UK's climate change targets under the Climate Change Act 2008 to achieve net zero emissions before 2050, to increase support for and set ambitious, short-term targets for the roll-out of renewable and low carbon energy and transport, and to move swiftly to capture economic opportunities and green jobs in the low carbon economy while managing risks for workers and communities currently reliant on carbon intensive sectors; and further calls on the Government to lay before the House within the next six months urgent proposals to restore the UK's natural environment and to deliver a circular, zero waste economy.'

Opposition Leader Jeremy Corbyn explained that the 'whole point' of the declaration is to 'focus the attention of all of us on the sheer urgency of the issue because it is not going to go away; it is going to get considerably worse unless we act and set an example to other nations to also act'.

The Conversation observes that though there is no 'precise definition' of what constitutions action to meet such an emergency, the declaration has been likened to putting the UK on a 'war footing' ie making climate change the centre of policy, rather than a peripheral consideration.

The declaration occurred in the context, The Conversation observes, of recent climate protests, a visit from Climate Activist Greta Thunberg, the broadcast of David Attenborough's documentary *Climate Change: the facts*, and after several days of protests by environmental group Extinction Rebellion.

[Sources: UK House of Commons Hansard Volume 659 1 May 2019: Environment and Climate Change; The Conversation 02/05/2019; The Independent 02/05/2019]

Could Australia follow the UK?

- **The Greens support a similar declaration in Australia:** In a statement, Greens climate and energy spokesperson Adam Bandt MP has welcomed the UK Parliament's declaration of a climate and environment emergency. Mr Bandt said the Greens would seek to move and pass a similar motion as soon as possible in the new Parliament after the election.

[Source: Adam Bandt MP media release 02/05/2019]

- **A 'petition storm' calling for a similar climate declaration?** Climate groups are also collaborating or working independently in support of a campaign for the Australian government to pass a similar declaration of a climate emergency and have started a number of petitions (described as a 'petition storm' on the campaign website).

[Source: Climate Emergency Declaration: Call to declare a climate emergency]

Brief Overview: Committee of Climate Change report, Net Zero - The UKs contribution to stopping global warming

In response to a government request, the UK Committee on Climate Change (CCC) has published report on the UK's long-term emissions targets. The report includes recommendations and outlines the steps necessary to transition the UK to a net zero carbon dioxide and greenhouse gas (GHG) emissions economy by 2050.

Some Key Points

- **The CCC recommends a new emissions target for the UK: net-zero greenhouse gases by 2050**
- **In Scotland, the CCC recommends a net-zero date of 2045,** reflecting Scotland's greater relative capacity to remove emissions than the UK as a whole
- **In Wales, the CCC recommends a 95% reduction in greenhouse gases by 2050**
- **Current policy is insufficient for even the existing targets**
- **A transition to a net zero UK economic by 2050 is technically achievable:** Provided that 'clear, stable and well-designed policies to reduce emissions further are introduced across the economy without delay' a net zero target for 2050 is 'technically achievable'. This includes 'firm plans' for housing and domestic heat; for industrial emissions; carbon capture and storage; road transport; agriculture; aviation and shipping.
- **Cost is 'manageable'**: The target can be met with known technologies, alongside improvements in people's lives, and within the expected economic cost that parliament accepted when it legislated the existing 2050 target for an 80% reduction from 1990. The report states that there is 'a manageable cost to tackling these challenges, and the lesson of the last decade is that costs fall when there is a concerted effort to act'

[Sources: Committee on Climate Change media release 02/05/2019; Full report: Net Zero - The UKs contribution to stopping global warming; The Conversation 02/05/2019]

Out of step with businesses on climate? A number of Australian businesses are reportedly reviewing their association memberships in response to Business Council of Australia

The SMH reports that a number of companies (including Rio Tinto, BHP, Westpac and Telstra) are reviewing the alignment between their own stated views on climate change as compared with the views of the industry associations to which they belong including the Business Council of Australia (BCA).

Reportedly, The Australasian Centre for Corporate Responsibility (ACCR) has said that some BCA members have expressed concern with respect to the BCA's climate stance. According to The SMH, though the BCA supports Australia's commitment to the Paris Agreement, it has reportedly faced criticism over its approach to climate risk and more particularly it's characterisation of Federal Labor's proposed 45% emissions target as 'economy wrecking'.

According to The SMH, Telstra has questioned whether industry bodies should advocate on topics where there is no consensus. 'We believe industry associations should refrain from advocacy in areas where no broad industry consensus exists – in these areas individual members are best placed to advocate their views independently' said Telstra's chief sustainability officer Tim O'Leary is quoted as stating. Reportedly, Telstra has said that should material differences between its own climate stance and the stance of industry associations to which it belongs be identified, Telstra will engage directly with the associations. Reportedly, Telstra has made no decision to leave the BCA.

According to The SMH, BCA CEO Jennifer Westacott responded by acknowledging that some CBA members are undertaking reviews and observing that BCA members are involved in developing BCA policy.

[Source: The SMH 02/05/2019]

In Brief | Human action is causing mass global extinction: A landmark study, the Global Assessment of the Intergovernmental Science-Policy Platform for Biodiversity and Ecosystem Services (IPBES Assessment) presents evidence that biodiversity is necessary to human survival, that human action

threatens more species with global extinction now than ever before, that existing goals are inadequate and makes the case for immediate, transformative change

[Sources: IPBES media release 06/05/2019; IPBES Global Assessment Summary for Policy Makers; The Conversation 07/05/2019;

Other Developments

United States | The CFTC has said that whistleblowers who report internally first, may be eligible for an 'enhanced' payment

The Commodity Futures Trading Commission (CFTC) has announced a whistleblower award of approximately $1.5 million to be paid to an individual whistleblower. The CFTC granted the whistleblower's award application for both a CFTC action and a related action brought by another federal regulator.

In ordering the award, the CFTC's Enforcement Director James McDonald said that the 'growing line' of whistleblower awards demonstrate the CFTC's commitment to the program and underlines the 'integral' role whistleblowers play in enforcement efforts. Since issuing its first award in 2014, through 2018, the CFTC has awarded more than $85 million to whistleblowers. DOE actions associated with those awards have resulted in sanctions orders totaling more than $675 million.

The CFTC adds that though there is no requirement for a whilstleblower to report internally before approaching the commission, 'today's award demonstrates that the Commission may pay enhanced awards to those that do – that is one of the positive factors set out in our rules for the Commission to consider in making its award determination…To be clear, the Commission's rules do not require a whistleblower to undertake internal reporting efforts in order to be eligible for the benefits and protections of our program. Instead, a whistleblower can contact us directly whenever he or she wishes – and may do so anonymously.'

[Note: If elected, the Federal Labor Party has said that it plans to introduce a whistleblower reward scheme in Australia. See: Labor Leader Bill Shorten media release 03/02/2019; Governance News 13/02/2019. Labor's response to the Financial Services Royal Commission Final Report states that Labor plans to set up a Whistleblower Rewards Scheme; establish a Whistleblower Protection Authority; 'overhaul our whistleblowing laws with a single Whistleblowing Act'; and fund a special prosecutor to bring corporate criminals to justice. See: Governance News 27/02/2019]

[Sources: CFTC media release 06/05/2019; FCPA blog 06/05/2019]