# Governance News

27 November 2019


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Diversity

## Some way to go? The latest Hampton-Alexander review of FTSE women leaders released

**Report overview | Fourth Hampton – Alexander Review on FTSE Women Leaders and improving gender balance in FTSE Leadership**

**Key Takeout:** Though there has been some progress, unless the appointment rate of women is nearer 50% in the coming year — ie half of all available roles going to women and half going to men — the FTSE 350 will not achieve the 33% target by the end of 2020

In 2016, the Hampton-Alexander Review set five key Recommendations aimed at increasing the number of women in leadership positions of FTSE 350 companies, including a target of 33% by the end of 2020.

The 4th Hampton - Alexander report assesses progress, shares emerging best practice and sets out current challenges.

### Progress update

- FTSE 100 companies are close to the 33% target with the number of women on FTSE 100 Boards at 32.4% this year, up from 30.2% in 2018. However, the pace of change in leadership roles (in the combined executive committee and direct reports) is 'too slow' increasing from 27% in 2018 to 28.6% in 2019.
- There has also been an increase of women on FTSE 250 boards to 29.6% this year, up from 24.9% in 2018. However, the pace of change in other leadership roles (in the combined executive committee and direct reports) is slower, increasing from 24.9% in 2018 to 27.9% in 2019.
- If the FTSE 350 Combined Executive Committee and Direct Reports is to meet the 33% target by the end of 2020, a significant step-up in the appointment rate of women is required. If current progress continues, the FTSE 350 will miss their 33% target.

### Positive trends

- Just under a half of the FTSE 250 – that is, 111 boards, have met or exceed the 33% target.
- The number of all-male boards is down from five in 2018, to two in 2019.
- In 2019, 81 companies in the FTSE100 had at least three women in their boards.
- There are 85 more women serving on FTSE250 Boards in 2019 than 2018 , this means, on average, one in every three companies has increased the number of women on their boards in the last 12 months.

### Still work to do

- 61 FTSE 100 companies and 113 FTSE 250 companies are considered to have 'some way to go' before the 33% is achievable by the 2020 deadline.
- The number of female CEOs is virtually unchanged
- Overall, the report cautions that many companies remain well adrift from the 33% target and unless the appointment rate of women is nearer 50% in the coming year – that is half of all available roles going to women and half going to men, the FTSE 100 will not achieve the target by the end of 2020.

In their Joint Forward to the Report, Permanent Secretary, Department for Business Energy & Industrial Strategy Alex Chisholm and CEO of the Civil Service and Permanent Secretary for the Cabinet Office John Manzoni said that the results indicate that there has been some progress since 2011, adding that 'the excuses that circulated [at that time] about the difficulties around achieving more diverse business leadership can now be dismissed by the evidence that real change can come about where there is the conviction', but that ultimately 'more needs to be done'.

### Key barriers to progress?

A key barrier to progress identified in the report is the fact that the majority of leadership appointments continue to go to men. The report observes that despite the increased board turnover rate, the female appointment rate remains skewed towards male candidates. In the FTSE 100 and the FTSE 250, around two-thirds of all available roles go to men.

**'One and done' outlook on boards**

- In 2018, 74 boards in the FTSE350 has only one woman. This figure dropped to 28 boards in 2019. The report cautions that this tokenistic 'one and done' approach to gender equality is slowing overall progress on the issue.
- The report also observes that investors are increasingly concerned about the issue of diversity, and increasingly consider it to be a factor in securing long-term business success — ie consider that when companies bring a diverse mix of perspective and skills to the table, it will lead to greater productivity and sustainability. Accordingly investors are increasingly considering diversity as a voting issue when determining whether they can support individual Director Re-election at company AGMs. Jessica Ground – Global Head of Stewardship Schroders Plc is quoted as saying that 'Diversity is high up investors agenda and shows no sign of going away. Our commitment to invest in diverse and better run companies filters through in our engagement with management, our voting behaviour and our investment decisions. We are convinced that companies who take this seriously and pro-actively secure a diverse pipeline of talent, will make better decisions now and in the future, to the benefit of our clients.'
- In addition, the report references the emphasis in the UK Corporate Governance Code on the issue of diversity and the importance of succession planning. The report suggests that as companies apply the new Code in 2020, they will be expected to demonstrate how they have sought the right mix of skills and perspectives to drive their long term success.

*[Source: Hampton-Alexander Review 2019]*

**In Brief | In Brief | The Financial Times and Statista have released a report — Diversity Leaders 2020 — ranking 700 businesses from 10 European countries on how well their employees rate their approaches to equality and inclusion. The top three companies were: Booking.com (Netherlands); Colgate Palmolive (Switzerland); and Wilmott Dixon (UK)**

*[Source: [registration required] The FT 20/11/2019]*

## Meetings and Proxy Advisers

### Calls for more regulation of proxy advisers in Australia are getting louder?

**Context:** The Australian Institute of Company Directors (AICD) has reportedly suggested that consideration should be given to changing the way in which proxy recommendations are prepared, and more particularly that consideration should be given to following the proposals being considered by the US Securities and Exchange Commission, including a proposal to give companies more opportunity to review/respond to draft proxy advice before it is distributed to shareholders (see: Governance News 20/11/2019 at p7; 06/11/2019 at p8)].

**Calls for more regulation of proxy advisers?** The AFR reports that Wesfarmers CEO Rob Scott has joined Harvey Norman Chair Gerry Harvey in calling for more regulation of proxy advisers.

Reportedly, Mr Scott has said that the 'The world of proxy advisers is an unregulated environment and there would be some benefit from a greater degree of objectivity and quality control…I don't have a view on who it should be, [but] listed companies are under a high degree of scrutiny around continuous disclosure and all disclosures we make – there isn't that same level of objectivity and cross check around some of the reports of proxy advisers.'

Reportedly, Mr Scott went on to say that enabling companies to vet proxy reports prior to publication is 'good practice' and would enable any 'misunderstandings' to be corrected'.

'Often companies don't have the opportunity to actually contribute and help correct errors or mistakes or misunderstandings before reports are published…Some proxy advisers engage closely and that provides the opportunity to ensure errors are addressed, but it's not always the case….The issue is there should be some checks and balances in place to ensure that whatever reports are published are factually correct' Mr Scott reportedly said.

The AFR comments that Mr Scott's comments come amid growing concern among Australian companies about the influence of proxy advisers.

*[Source: [registration required] The AFR 20/11/2019]*

## Regulators

### APRA has no plans to send observers to board meetings?

**Context:** On 19 November, Australian Prudential Regulation Authority's (APRA's) released an information paper — Transforming governance, culture, remuneration and accountability: APRA's approach — outlining its proposed 'more intensive regulatory approach' to lift governance, culture, remuneration and accountability (GCRA) standards. Among other things, APRA said that it is considering benefits associated with observing board meetings, in line with international leading practice (see: Governance News 20/11/2019).

**Confirmation that APRA have no plans to send observers into board meetings?** The Australian reports that Treasurer Josh Frydenberg has said he had raised the issue with APRA and the regulator has 'confirmed that they have no plans to sit in as an observer in board meetings'.

'There is no doubt following the [Financial Services] Royal Commission that we need to restore trust in our financial system. This will require striking the right balance with regulation that is targeted and effective while not constraining commercial entities from going about their daily business…It is important to remember many of the revelations at the royal commission were already known to regulators. We do not need regulators to be further inserted into board meetings to find out what is going on' Mr Frydenberg is quoted as saying.

Mr Frydenberg reportedly concluded 'Boards should be able to engage in open and robust discussion knowing they are ultimately accountable, without having regulators sitting next to them.'

**Power to veto board/senior appointments?** APRA's paper also cited international 'leading practice' where regulators have the power to veto board and senior management appointments. Reportedly, APRA is engaging with government about maintaining board and management quality.

*[Source: [registration required] The Australian 23/11/2019]*

## Institutional Shareholders and Stewardship

### Growing in influence: Institutional investors hold an increasingly large share of the world's listed companies according to an OECD report

The OECD has published a report — Owners of the World's Listed Companies — looking at the ownership of the 10,000 largest listed companies globally and how owners perform their role as shareholders.

**Some Key Findings**

- **Institutional investors are by far the single largest category of investors globally** holding 41% of public equity or the equivalent to USD 31 trillion invested in public equity markets. According to the report, this is three times the amount invested by public sector owners and six times the value of investments by strategic individuals.
- **The second largest category of owner is the public sector**, which holds 14% of the global market capitalisation at a total value of USD 10 trillion. Central and local governments are the largest public sector owners accounting for 56% of public sector ownership in listed companies, followed by sovereign wealth funds (SWFs), public pension funds and state-owned enterprises (SOEs). The public sector in the People's Republic of China (China) accounts for 57% of the total public sector investments in global equity markets.
- **The relative importance and presence of different investor categories vary across individual markets**.
  - In the US, the UK and Canada institutional investors show a strong presence holding 72%, 63% and 47% of the listed equity, respectively.
  - Private corporations and holding companies are prominent owners in several markets, such as Chile, the Philippines and Turkey where they own 55%, 48% and 40% respectively of the equity capital in listed companies.

- Strategic individuals and family members own 34% of the total equity capital in listed companies in Mexico and are also important investors in Israel and Thailand where they hold 16% of the publicly listed equity capital.
- The public sector is an important owner in China, Saudi Arabia, Malaysia, Hong Kong (China) and Norway holding between 34% and 46% of the total equity capital of listed companies.
- In Australia, the largest category of investor is 'Other Free Float' (ie shares are in the hands of investors that are not required to disclose their holdings. It includes the direct holdings of retail investors who are not required to disclose their ownership and institutional investors that do not exceed the required thresholds for public disclosure of their holdings). The next largest category is institutional investors (29%), followed by 'strategic individuals' (13%), private corporations (10%) and the public sector (3%).

- **Increase in foreign ownership:** In recent decades, most advanced markets have seen a significant increase in ownership by foreign investors. For example, in Japan, foreign ownership increased from 3% to 30% of all public equity between 1980 and 2017. In the UK, foreign ownership increased from 4% to 54% and in the US it tripled from 5% to 15%.
- **Cross-border investments account for almost one-quarter of the investments in public equity markets in the world.** Almost 75% of the cross-border investments in public equity markets are held by investors domiciled in the United States and Europe.
- **Institutional investors that typically use diversified portfolio investment strategies and track indices engage more frequently in cross-border investments.** In half of the markets they account for more than 50% of all non-domestic ownership. In certain markets eg Chile, Indonesia, Poland, Saudi Arabia and Singapore, private corporations and holding companies are the largest category of nondomestic owners. By contrast, both public sector and strategic investors play a relatively limited role in cross-border public equity investments.
- **Ownership concentration:** In half of the world's publicly listed companies, the three largest shareholders hold 50% of the capital. In 75% of companies, the three largest owners hold more than 30% of the capital. In most markets, private corporations or strategic individuals appear as the largest shareholders in individual companies.

### The role of institutional investors in monitoring corporate performance

The report comments that in a number of jurisdictions, regulators/policy makers have acted to impose requirements to encourage institutional investors to adopt an active approach to investment.

For example, in 25 out of the 49 jurisdictions covered in the report, there is a legal requirement for institutional investors to disclose their voting policies and in 14 jurisdictions they are required to disclose their actual voting records. Similarly, 23 jurisdictions have some form of stewardship codes encouraging the disclosure of their voting policy and 19 encouraging the disclosure of actual voting records.

However, the report questions the effectiveness of these requirements, given ownership engagement is not necessarily part of the business model of every institutional investor. 'If shareholder engagement is not part of the institution's business model and investment strategy, mandatory requirements to engage…may be ineffective and lead to a box ticking approach' the report argues.

*[Sources: OECD media release 17/10/2019; OECD report: Owners of the World's Listed Companies]*

## Financial Services

### Top Story | Decision in Financial Services Royal Commission case study: ASIC won its case against Dover Financial Advisers Pty Ltd and Dover's sole director

**Case note | Australian Securities and Investments Commission v Dover Financial Advisers Pty Ltd [2019] FCA 1932**

**Key Takeouts**

- The Federal Court has found that Dover Financial Advisers Pty Ltd (Dover) and Dover's sole director Terrence McMaster misled and deceived clients in contravention of their legal obligations.

- The case largely focused on the question of whether Dover's conduct in providing a document entitled the 'Client Protection Policy' to clients (either with, or incorporated into statements of advice to clients) was 'misleading or deceptive' or 'likely to mislead or deceive' within the meaning of s 1041H of the Corporations Act 2001 (Cth) (Corporations Act) and s 12DA(1) of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) and/or a 'false or misleading representation' within the meaning of s 12DB(1)(i) of the ASIC Act.
- The court is yet to rule on what, if any, financial penalty Dover and Mr McMaster will be ordered to pay
- The case has received wide media coverage in light of the fact that it is the first decision to deal directly with a case study considered by the Financial Services Royal Commission and in light of ASIC's 'why not litigate?' approach to enforcement
- Commenting on the decision ASIC deputy chair Daniel Crennan is quoted in the AFR as saying that the ruling sends a clear message to financial services providers that if they mislead or deceive consumers, they should expect ASIC to take action.
- Mr McMaster has reportedly said he has no plans to appeal the decision, but does plan to commence litigation in 2020 against five law firms he claims were negligent in the advice they provided on the construction of the Client Protection Policy.

On 22 November, Justice O'Bryan handed down his decision in Australian Securities and Investments Commission v Dover Financial Advisers Pty Ltd [2019] FCA 1932. Justice O'Bryan found that Dover Financial Advisers Pty Ltd (Dover) and Dover's sole director Terrence McMaster misled and deceived clients in contravention of their legal obligations.

The case, brought by the Australian Securities and Investments Commission (ASIC), has received a high level of media coverage/interest given it is the first decision to directly deal with a case study considered by the Financial Services Royal Commission.

[Note: The final case study in the second round of Financial Services Royal Commission hearings concerned Dover Financial Advisers Pty Ltd (Dover) including the use of Dover's Client Protection Policy. For a discussion on the use of the Client Protection policy, and Commissioner Hayne's views see: Financial Services Royal Commission Interim Report, Volume 2 at p253-255.]

**The 'Client Protection Policy'**

The case largely focused on the question of whether Dover's conduct in providing a document entitled the 'Client Protection Policy' to clients (either with, or incorporated into statements of advice to clients) constituted misleading or deceptive conduct.

The Policy purported to set out a number of 'important consumer protections designed to ensure that every Dover client get the best possible advice and the maximum protection available under the law.'

In broad terms, ASIC alleged that this was not the case because the policy 'did not ensure that clients received the maximum protection available under the law' but in fact contained numerous exclusions, limitations, restrictions and/or dilutions of clients rights.

**Details: ASIC's case**

ASIC alleged that each time 'Client Protection Policy', was provided to a client together with a statement of advice, Dover engaged in conduct that was 'misleading or deceptive' or 'likely to mislead or deceive' within the meaning of s 1041H of the Corporations Act 2001 (Cth) and s 12DA(1) of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) and/or made a 'false or misleading representation' within the meaning of s 12DB(1)(i) of the ASIC Act.

During the period in which the policy was in use (from September 2015 to March 2018), the policy was provided to 19,402 of Dover's retail clients.

ASIC further alleged that Mr Terrence McMaster, as Dover's sole director was knowingly concerned in the conduct..

ASIC sought declarations that Dover contravened s 1041H of the Corporations Act, s 12DA(1) of the ASIC Act and s 12DB(1)(i) of the ASIC Act; and pursuant to s 21 of the Federal Court Act, declarations that Mr McMaster was knowingly concerned in Dover's contraventions of s 1041H of the Corporations Act, s 12DA(1) of the ASIC Act and s 12DB(1)(i) of the ASIC Act.

Both Dover and Mr McMaster (the defendants) accepted that the Client Protection policy was inaccurate, but advanced a number of arguments as to why ASIC's arguments should not be accepted, including that the approach taken by the High Court in Campomar Sociedad, Limitada v Nike International Ltd (2000) 202 CLR 45 was inapplicable to the case.

**Was the conduct likely to mislead or deceive?**

Justice O'Bryan observed that sections 1041H(1) of the Corporations Act 2001 (Cth) (Corporations Act) and 12DA(1) of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) are framed in very similar terms and the same principles are applicable to both provisions.

Further, His Honour observed that though section 12DB(1)(i) of the ASIC Act is framed in different terms, 'the prohibitions are similar in nature'.

'The central question' Justice O'Byran states, 'is whether the impugned conduct, viewed as a whole, has a sufficient tendency to lead a person exposed to the conduct into error (that is, to form an erroneous assumption or conclusion about some fact or matter)'.

**Unnecessary for ASIC to prove that any individual client was subjectively misled**

Justice O'Bryan rejected the defendant's argument that it was necessary for ASIC to plead/prove that any individual client (who had received the Client Protection Policy) was misled or deceived by the inaccuracy Client Protection policy or had suffered loss as a consequence.

'I regard the enquiry as to whether any individual client was subjectively misled by the Client Protection Policy as not determinative of the question whether Dover's conduct contravened the statutory prohibitions. The question whether conduct is misleading or deceptive or contains a false or misleading representation is an objective question to be determined by the Court by reference to the impugned conduct; the fact that a client may have been misled, and may have made a complaint about being misled, is admissible on the question but is neither necessary nor determinative…I do not consider that the absence of client complaints establishes that no clients were misled…the inference that the defendants ask me to draw requires speculation about a matter which is not essential to the causes of action advanced by ASIC' Justice O'Bryan writes.

Further, Justice O'Bryan states that whether the conduct in question was directed to the public generally/section of the public (to a class of persons) or to an identified individual, the question of whether the conduct is likely to mislead or deceive should be assessed 'in light of the objective circumstances'.

'In both cases, the relevant question is objective: whether the conduct has a sufficient tendency to induce error. Even in the case of an express representation to an identified individual, it is not necessary (for the purposes of establishing liability) to show that the individual was in fact misled'.

**The client protection policy was false, misleading or deceptive**

Justice O'Bryan agreed with ASIC that the client protection policy in this case, 'did not protect clients' but instead 'purported to strip clients of rights and consumer protections they enjoyed under the law'.

The 'Introductory Clause was false, misleading or deceptive because [despite purporting to do so] the Client Protection Policy did not ensure that clients received the maximum protection available under the law. Rather, the Limiting Clauses in the policy (other than the Best Efforts Clause and the Continued Retainer Clause) purported to remove or dilute the protections that clients would otherwise have under the law. In effect, the Introductory Clause represented that the Limiting Clauses constituted the maximum protections available to clients under the law when that was not the case' Justice O'Bryan writes.

Further, Justice O'Bryan considered that the fact that the Client Protection Policy was provided electronically to clients, and may not have been immediately read by them, to be irrelevant in the context of determining whether the document was misleading or deceptive. 'The conduct of electronically providing the document to clients in conjunction with statements of advice enabling the client to file the document electronically is equivalent to sending a paper copy by post, enabling the client to file the document in paper form. In both cases, the client may not read the document immediately, but may file the document for later use if it becomes necessary. In my view, if the contents of the document are likely to mislead or deceive when read, a person has engaged in misleading or deceptive conduct by successfully providing the document to the client'.

As such, his Honour found that the Introductory Clause contained in the Client Protection Policy was 'misleading or deceptive' or 'likely to mislead or deceive' within the meaning of s 1041H of the Corporations Act 2001 (Cth) (Corporations Act) and s 12DA(1) of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) and a 'false or misleading representation' within the meaning of s 12DB(1)(i) of the ASIC Act.

Justice O'Bryan also accepted ASIC's submission that, on each of the 19,402 occasions when a statement of advice was given to a client along with the Client Protection Policy, there was a separate contravention of the statutory prohibitions because there was a separate communication to a client that was misleading.

**Mr McMaster was 'knowingly concerned' in Dover's contraventions**

Justice O'Bryan observed that 'A person will be knowingly concerned in a contravention if that person was an intentional participant in the contravention, with knowledge of the essential elements constituting the contravention at the time of the contravention'.

In this instance, Justice O'Bryan found that as a question of fact, Mr McMaster, who was responsible for: a) determining the content of the Client Protection Policy; b) approving the content of the Client Protection Policy; and/or c) requiring Dover's authorised representatives to incorporate the Client Protection Policy into/provide the Client Protection Policy with, the statements of advice provided to clients, was 'knowingly concerned' in Dover's contraventions of the Corporations Act and the ASIC Act.

**Next steps?**

Justice O'Brien said he would hear further from the parties as to the forms of declaration that should be made and as to the orders timetabling a further hearing in respect of pecuniary penalties.

In particular, Justice O'Brien questioned whether there is a 'proper basis for the Court to make declarations that Mr McMaster was knowingly concerned in Dover's contraventions of s1041H or s12DA in circumstances where ASIC is not seeking remedial relief under any statutory provisions that requires such a finding.'

**ASIC response**

The AFR quotes ASIC deputy chair Daniel Crennan as commenting that the decision sends a clear message to financial services providers that if they mislead or deceive consumers, they should expect ASIC to take action. 'We've brought the case to the court and we've succeeded and [McMaster] is going to have to deal with the consequences of that' Mr Crennan is quoted as saying.

[Note: The decision follows ASIC's recent

**No appeal?**

The AFR reports that Mr McMaster has said he will not appeal the Federal Court's decision but is planning to commence litigation in 2020 against five law firms he claims were negligent in the advice they provided on the construction of the Client Protection Policy.

*[Sources: Australian Securities and Investments Commission v Dover Financial Advisers Pty Ltd [2019] FCA 1932; [registration required] The AFR 25/11/2019]*

## Top Story | AUSTRAC has launched civil proceedings against Westpac alleging AML/CTF contraventions

### Overview of the allegations, the lender's response and a brief overview of the response from regulators and investors

On 20 November The Australian Transaction Reports and Analysis Centre (AUSTRAC) commenced civil proceedings against Westpac alleging the lender contravened its obligations under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth) (Act).

AUSTRAC is seeking declarations of contravention and pecuniary penalties pursuant to s175(1) of the Act.

[Note: The Concise Statement, Statement of Claim and Originating Application are available on the AUSTRAC website here.]

**AUSTRAC's allegations**

In broad terms, AUSTRAC alleges that Westpac did not:

1. appropriately assess and monitor the ongoing money laundering and terrorism financing risks associated with the movement of money into and out of Australia through correspondent banking relationships and with the movement of money into/out of Australia
2. carry out appropriate due diligence on customers sending money to the Philippines and South East Asia for known child exploitation risks
3. report (approx) 19.5 million International Funds Transfer Instructions (IFTIs) to AUSTRAC
4. pass on information about the source of funds to other banks in the transfer chain
5. keep records relating to the origin of some of these international funds transfers

AUSTRAC alleges that Westpac contravened the Act on 23 million occasions.

In a statement, AUSTRAC said that 'Westpac's oversight of the banking and designated services provided through its correspondent banking relationships was deficient. Westpac's oversight of its AML/CTF Program, intended to identify, mitigate and manage the money laundering and terrorism financing risks of its designated services, was also deficient. These failures in oversight resulted in serious and systemic non-compliance with the AML/CTF Act'.

AUSTRAC CEO Nicole Rose said that AUSTRAC 'have been, and will continue to work with Westpac during these proceedings to strengthen their AML/CTF processes and frameworks. Westpac disclosed issues with its IFTI reporting, has cooperated with AUSTRAC's investigation and has commenced the process of uplifting its AML/CTF controls'.

**Westpac's response**

Since the 20 November when AUSTRAC announced it had commenced civil penalty proceedings, Westpac has released a number of statements providing updates on the lender's response. These include, a detailed response plan, responding to the allegations in AUSTRAC's statement of claim, and an announcement of leadership changes. A summary of Westpac's statements is below.

**Timeline and response**

**20 November:** Westpac released an initial statement acknowledging the commencement of civil proceedings by AUSTRAC and noting that the lender had previously disclosed (including in its Full Year 2019 reporting) that it had self-reported: a) a failure to report a large number of international funds transfer instructions (IFTIs) to AUSTRAC; and b) that AUSTRAC was also investigating a number of other areas relating to Westpac's processes, procedures and oversight.

**20 November**: Westpac released a second statement responding to AUSTRAC's statement of claim in which the lender acknowledged that 'these are very serious and important issues' and confirming its commitment to 'assisting AUSTRAC and law enforcement agencies to stop financial crime'. Westpac CEO Brian Hartzer went on to say that the 'issues should never have occurred and should have been identified and rectified sooner. It is disappointing that we have not met our own standards as well as regulatory expectations and requirements'. The statement also outlines the steps Westpac is making/has made to 'improve and bolster the management of financial crime risks including strengthening our policies, data feeding systems, processes and controls'.

**22 November:** Westpac issued a statement on behalf of the board, 'unreservedly' apologising, expressing the board's commitment to addressing the issues and to working with AUSTRAC. Westpac Chair Lindsay Maxsted said 'the notion that any child has been hurt as a result of any failings by Westpac is deeply distressing and we are truly sorry. The Board unreservedly apologises. Our Board, CEO, and management team are fully committed to fixing these issues and we are taking all steps necessary to urgently close any remaining gaps and fix our policies and procedures so that this can never happen again.' The statement goes on to outline the actions already implemented/being implemented by the lender including: reviewing and taking action on all of the individual customers mentioned by AUSTRAC; 'establishing a multi-layered review' of current processes/systems; committing to appoint independent experts to conduct a review of accountability as well as oversee the actions arising from the review; and commencing discussions with relevant community groups about any further steps the lender can take to 'fight child exploitation'. The statement adds that the board will continue to provide updates on the steps being taken.

**24 November:** On 24 November, Westpac Chair Lindsay Maxsted and CEO Brian Hartzer released a three point response plan — the plan is broken into 1) immediate fixes; 2) lifting standards; and 3) protecting people with actions and timelines under each — to address the issues raised by AUSTRAC.

**Actions under the response plan**

1. **Immediate fixes:** Westpac outlines seven actions (five of which have already been completed) to ensure 'issues cannot happen again'. They are: 1) closing the Westpac Australasian Cash Management product; 2) remediating and analysing all unreported IFTIs to AUSTRAC; 3) closing the LitePay international funds transfer system (the platform that facilitated low value international payments); 4) updating child exploitation filters into screening for the SWIFT payment channel to additional jurisdictions; 5) undertaking a further review of all child exploitation transactions types for the Phillippines over the past 12 months; 6) re-reviewing taking appropriate action (where appropriate) against the 12 customers (previously reported by Westpac to AUSTRAC); and 7) adding 200 resources to the existing 750 people in the financial crime resourcing team by 2020.

2. **Lifting standards:** The plan states that Westpac is reviewing all financial crime systems and processes 'to pursue best-in-class global standards'. The plan outlines five actions to lift standards including the introduction of priority screening. This means that where Westpac flags transactions that suggests potential child exploitation in high risk locations, the transactions are prioritised for action and reported to AUSTRAC within 24 hours (which is faster than the standards require).

   Other actions include: 1) the establishment of a board financial crime subcommittee chaired by a non-executive director to oversee the implementation of the enhanced financial crime program; 2) commissioning an external expert to independently review Westpac's program including a review of accountability; 3) improving cross industry data sharing (including seeking partnerships with industry, technology, telecommunication and government partners) and; 4) elevating the financial crime function to report directly to the Chief Risk Officer.

3. **Protecting people:** Finally the plan outlines a number of actions and investments aimed at reducing the human impact of financial crime. Actions include: 1) convening an expert advisory roundtable to develop a program of actions to support the prevention of online child exploitation and the provision of $10m per year for three years to implement the recommendations; 2) providing $6m over six years to SaferKidsPH; and $18m in funding over 3 years to the International Justice Mission to address online sexual exploitation of the children in the Philippines.

The plan also 'explain[s] some of AUSTRAC's allegations' and actions Westpac has taken to 'improve financial crime management' including (among others) 'dealing with and fixing individual issues' (eg IFTI non-reporting issues) and investing in the consolidation of different financial crime systems into a single group wide technology system.

**Short term incentives may be withheld/reduced pending the outcome of the accountability review**: In a statement accompanying the plan, Westpac Chair Lindsay Maxsted said the 'board understands the need for action and accountability' and that in consequence, the Board had determined 'that either all or part of the grant of the 2019 Short Term Variable Reward will be withheld for the full Executive team and several members of the general management team subject to the assessment of accountability. We recognise the seriousness of these events and that is why we will appoint an external expert to provide independent oversight of the process. We will make the recommendations public.'

**26 November:** On 26 November, Westpac announced a number of leadership changes.

- Group CEO Brian Hartzer will step down as CEO effective Monday 2 December. Peter King (current Westpac CFO) will replace Mr Hartzer as acting CEO while a permanent replacement is found. Current Chief Operating Officer, Gary Thursby will act as CFO.
- Chair Lindsay Maxsted will bring forward his retirement as Chair to the first half of 2020
- Long-standing Director, Ewen Crouch will not seek re-election at the upcoming Westpac AGM on 12 December.

**Remuneration arrangements**: The statement also outlines exit arrangements for outgoing CEO Brian Hartzer as follows.

- Mr Hartzer has been given 12 months' notice and will be paid his fixed remuneration of $2.686m over this period
- Both Mr Hartzer's unvested deferred Short-Term Variable Reward and unvested Long-Term Variable Reward will be forfeited
- In addition to forgoing his FY19 Short-Term Variable Reward, Mr Hartzer will also not be eligible for Short-Term Variable Reward in FY20 or FY21
- Westpac will not proceed to seek shareholder approval for the FY20 Long-Term Variable Reward outlined in the 2019 Notice of Meeting at the upcoming AGM

**Incoming acting CEO Peter King will be remunerated as follows**: Incoming acting CEO Peter King will receive annual total fixed remuneration of $2,100,000; annual Short Term Variable Reward at target of $2,100,000; and annual Long Term Incentive of $2,800,000 (face value), with any shares that are issued in respect of this award being purchased on market.

*[Sources: AUSTRAC Media release 20/11/2019; Concise Statement, Statement of Claim, Originating Application; Westpac media releases: 20/11/2019; 20/11/2019; 22/11/2019; 24/11/2019; 26/11/2019]*

### Response from regulators and investors

The AUSTRAC announcement, and Westpac's response, have received wide media coverage.

- **The Treasurer has said APRA is looking into the issues**: In an interview, Treasurer Josh Frydenberg said that the Australian Prudential Regulation Authority is considering action against Westpac executives, potentially under the Banking Executive Accountability Regime (BEAR), as well as the potential imposition of financial penalties. 'APRA has the ability under the Banking Executive Accountability Regime to disqualify boards and to disqualify executives where there is a failure to appropriately enforce and uphold the duties under the legislation. Now, that legislation came in to force in 2018, it's not retrospective and some of those alleged breaches date back to 2013 but the anti-money laundering laws are a prescribed activity under APRA and I know that APRA is looking at it' Mr Frydenberg said. Asked whether APRA can 'do more than just disqualify the executives' Mr Frydenberg said that APRA can apply to the court for fines of up to $500m. Mr Frydenberg went on to comment that the issue has further eroded trust in major financial institutions. 'There is a lack of trust and confidence among the public after the royal commission with some of our leading financial institutions. And now this…These issues develop a momentum of their own. They've (Westpac) got an AGM on December 12. And no doubt there will be some very hard discussions between now and then'. Subsequently, Mr Frydenberg welcomed the announcement by Westpac of the leadership changes at the lender on behalf of the government. 'As I said over the weekend, these issues develop a momentum of their own but there needed to be accountability' Mr Frydenberg said.
- **ASIC is also reportedly investigating**: According to media reports, the Australian Securities and Investments Commission (ASIC) has confirmed it is also investigating. The Guardian quotes an unnamed ASIC spokesperson as saying 'ASIC can confirm that it commenced an investigation on Thursday, 21 November 2019, concerning possible breaches of legislation it administers arising from AUSTRAC's actions in relation to Westpac'.
- **Reserve Bank of New Zealand:** In a statement, the Reserve Bank of New Zealand said it 'looking closely' at the Australian investigation. RBNZ is 'working closely with regulatory counterparts' following AUSTRAC' announcement, the statement reads. 'We have a regular onsite programme with New Zealand banks to ensure compliance with New Zealand's AML/CTF requirements, and will be looking closely at the Australian findings and if they have relevance for Westpac NZ'.

### Investor Response

[Note: The Westpac AGM will be held on 12 December. At the 2018 AGM, Westpac incurred a 'first strike'. Four directors will stand for re-election at the meeting (as director Ewen Crouch will not stand for reelection)]

- **Australian Shareholders' Association:** In a short statement, the Australian Shareholders' Association (ASA) said it 'is horrified by Westpac's disclosure of Austrac reporting breaches and implication of these failures'. The statement adds that 'ASA wants to know the board's response as a matter of urgency, and we will determine our actions when we have information. We will be meeting with Westpac Chair, Lindsay Maxsted, next week and will discover more'.

- **The Australian Council of Superannuation Investors (ACSI)** issued a statement welcoming the leadership changes at Westpac. ACSI CEO Louise Davidson said 'The actions taken today reflect the seriousness of the incidents and the failure of the bank to meet community expectations. ACSI will continue to engage with Westpac on a range of issues to determine whether further action is needed'. Ms Davidson went on to say 'It is still unclear how these significant issues came to occur, and why a fulsome investigation was not initiated earlier. Investors want to see Westpac's culture and governance strengthened to avoid a repeat of these issues. We believe that this crisis warrants further board renewal in the new year to support rebuilding public trust. We will be continuing to engage closely with Westpac to monitor its progress on remediation and improvement'.

- **Treasurer Josh Frydenberg has welcomed the announcement by Westpac of the leadership changes** on behalf of the government. 'As I said over the weekend, these issues develop a momentum of their own but there needed to be accountability' Mr Frydenberg said.

*[Sources: Australian Shareholders' Association media release 21/11/2019; The Guardian 25/11/2019; Treasurer Josh Frydenberg, Transcript of Interview with Fran Kelly Insiders ABC 24/11/2019; RBNZ media release 20/11/2019; ACSI media release 26/11/2019; Treasurer Josh Frydenberg Doorstop interview, Parliament House, Canberra 26/11/2019; [registration required] The AFR 26/11/2019]*

## Auditor finds Afterpay is a 'low risk business': Afterpay has released the final report form an external auditor into its compliance with AML/CTF laws

**Context:** Earlier in the year, The Australian Transaction Reports and Analysis Centre (AUSTRAC) announced that following a period of ongoing engagement with Afterpay Pty Ltd (Afterpay) identifying concerns with Aferpay's compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (the AML/CTF Act), AUSTRAC had ordered the appointment of an external auditor to examine its compliance with the AML/CTF Act. The purpose of the audit was to determine the extent of any compliance issues and whether further regulatory action concerning Afterpay is required (see: Governance News 19/06/2019 at p14).

**Afterpay has released the Final Audit Report:** On 25 November, Afterpay announced that the external auditor's final report had been provided to AUSTRAC and provided a summary of the report findings.

The report found that there were instances of 'historic non-compliance by Afterpay' and includes recommendations in relation to Afterpay's ongoing AML/CTF compliance (many of which have already been addressed).

However, the report also found that 'Afterpay's current program is aligned with AML/CTF Act and that Afterpay is a low risk business in regards to its vulnerability to be used for money laundering or terrorist financing. The Auditor also notes that Afterpay has a strong compliance culture and recommends Afterpay continues to maintain its current level of Board and senior management oversight of AML/CTF compliance as the business grows.'

Afterpay has said it 'fully accepts and is actioning all recommendations from the independent auditor'.

### Some Key findings

The report found that:

- board and governance oversight has 'matured significantly' over the course of Afterpay's evolution from start up to ASX 100 company and that there is now 'an appropriate level of awareness and engagement'.

- Afterpay's AML/CTF Program has evolved over time and is now 'appropriately aligned to the AML/CTF Act and Rules.'

- Afterpay is 'a low risk business in regards to its vulnerability to be used for money laundering or terrorist financing'. Notwithstanding this, the risk controls in place must 'remain commensurate with business growth' and therefore Afterpay must 'enhance its existing controls to identify politically exposed persons (PEPs) and the risk they may post'. The report notes that Afterpay has commenced a project to address this issue.

- The report identified that there was 'historic noncompliance with the AML/CTF Act and Rules' but that this was attributable to Afterpay's reliance on legal advice from [unnamed] 'top tier Australian law firms' in 2016 around appropriate AML/CTF controls which resulted in Afterpay initially focusing its AML/CTF controls upon merchants, rather than on consumers.

**Next steps:** Afterpay has submitted the auditor's report to the Australian Transaction Reports and Analysis Centre (AUSTRAC), which will now consider whether to take further action.

**Response?** The AFR reports that Afterpay's stock rose as much as 10% following Afterpay's announcement.

*[Sources: Afterpay ASX announcement: AUSTRAC update final audit report 25/11/2019; [registration required] The AFR 25/11/2019; [registration required] The AFR 25/11/2019; 26/11/2019]*

### NAB has agreed to pay $49.5m to settle a class action commenced in September 2018 against NAB and MLC Ltd in the Federal Court

NAB has agreed to pay $49.5m to settle a class action commenced in September 2018 against NAB and MLC Ltd in the Federal Court.

The action related to the sale of two Consumer Credit Insurance (CCI) products, NAB Credit Card Cover (NCCC) and NAB Personal Loan Cover (PLC).

Commenting on the announcement, NAB Chief Legal and Commercial Counsel Sharon Cook said 'the settlement is the right thing to do for our customers and shareholders. As we have said, we can only move forward if we deal with the past, so that we can earn trust among customers and the broader community and grow confidence in the future of NAB. It is important to note NAB no longer sells CCI products through any of its banking channels, and has implemented a remediation program for CCI customers.'

The payment amount was provided for in NAB's September 2019 full year financial statements.

The settlement is subject to approval of the Federal Court of Australia.

*[Source: NAB media release 20/10/2019]*

### The ACCC has authorised changes to the 2019 Code of Banking Practice implementing the ABA's response to the Financial Services Royal Commission recommendations

The Australian Competition and Consumer Commission (ACCC) has authorised changes to the Australian Banking Association's (ABA) 2019 Banking Code of Practice. The changes implement the ABA's response to the recommendations of the Financial Services Royal Commission.

The ACCC says that the changes were approved after several conditions were imposed to address to concerns that the ABA's original proposed changes needed to be stronger. The additional conditions are aimed at improving the code's benefits to low-income customers.

#### Changes

Changes include the following: a) banning charging default interest on distressed agricultural loans; b) providing inclusive and accessible banking services to those with limited English and those living in remote areas; c) providing concession card holders access to accounts with no overdraft and dishonour fees; and d) making the features of a basic, low and no fee bank account for low income earners uniform across the industry.

**Next steps:** The proposed changes will come into force on 1 March 2020, pending Australian Securities and Investments Commission (ASIC) approval of a second round of changes to the Banking Code separate to the ACCC review process.

*[Sources: ABA media release 21/11/2019; ACCC media release 21/11/2019]*

### Consumer group Choice has made a complaint to ASIC alleging some advertising claims by mortgage brokers may be misleading home loan customers

Consumer Group Choice announced that it has complained to the Australian Securities and Investments Commission (ASIC) about certain advertising claims by mortgage brokers (including Aussie Home Loans) that Choice considers are 'probably misleading home loan customers'.

#### Details: Choice's concerns

Choice alleges that Aussie Home Loans' advertising claims are potentially misleading and deceptive because they make the following representations: 1) brokers will find people a high quality loan; 2) brokers will scan the market to find the best product; and 3) mortgage brokers are 'free'.

Choice argues that such language misrepresents how Aussie Home Loans mortgage brokers and the industry as a whole actually operate. 'CHOICE is concerned that people who have seen these ads are likely to have formed the incorrect impression that mortgage brokers will scan the market to find them a high-quality loan, when the industry has failed to achieve this' Choice CEO Alan Kirkland said.

Choice says that it makes 'clear in the ASIC complaint that the Aussie Home Loans advertising claims are not an isolated case; they're indicative of what has long been happening across the mortgage broking industry'.

**Call for government to implement a 'best interests' duty for brokers**

Choice notes that one of the Financial Services Royal Commission recommendations [Recommendation 1.2] was the introduction of a best interests duty for brokers, and further, that the government has said it will introduce this law by the end of 2019.

Choice called for the government to 'turn this recommendation into law' and for ASIC to investigate 'dodgy broker claims across the industry'.

*[Source: Choice media release 23/11/2019]*

### 20,000 people have signed a petition calling on the government to urgently implement UCT reforms

**Context:** In July, the government released draft legislation — [exposure draft] Treasury Laws Amendment (Unfair Terms in Insurance Contracts) Bill 2019 — for consultation. The draft Bill proposes to extend the application of the unfair contract terms regime (UCT regime) to insurance contracts in line with Recommendation 4.7 of the Financial Services Royal Commission Final Report. The government announced that it would extend the UCT regime to insurance contracts on 4 February as part of its response to the Commission's recommendations. Consultation on the draft Bill closed on 28 August.

[Note: For a summary of the draft Bill see: Governance News 30/07/2019]

**Call to urgently act to implement the reforms:** 20,000 people have signed a petition coordinated by CHOICE and the Consumer Action Law Centre, demanding the government take action to implement unfair contract terms reforms this fortnight to close what they describe as 'a damaging loophole that has allowed insurance companies to profit by using confusing, tricky and unfair clauses to evade or reduce claims'.

The groups say the Government must review other industry carve-outs further. 'No industry should get special treatment to be unfair' the group's statement reads.

*[Source: Consumer Action Law Centre media release 25/11/2019]*

### APRA is consulting on proposed changes to the prudential standard governing insurance in superannuation (SPS 250)

The Australian Prudential Regulation Authority (APRA) is consulting on proposed revisions to Prudential Standard SPS 250 Insurance in Superannuation (SPS 250).

**Implement response to Financial Services Royal Commission and Post-Implementation Review**

APRA says that the proposed changes are the first step in implementing the enhancements identified in APRA's Post-Implementation Review of the superannuation prudential framework, and also address Financial Service Royal Commission recommendations 4.14 – Additional scrutiny for related party engagements and 4.15 – Status attribution to be fair and reasonable.

**Four key (proposed) changes**

- **Financial Services Royal Commission recommendation 4.15:** Revised SPS 250 proposes to introduce requirements to give effect to Financial Services Royal Commission recommendation 4.15 (Status attribution to be fair and reasonable), that any status attributed to a beneficiary in connection with the provision of insurance, is fair and reasonable. APRA says that the proposed amendments seek to strengthen the processes undertaken by RSE licensees in engaging related parties to provide insurance arrangements. APRA adds that they also address concerns highlighted by cases considered by the Financial Services Royal Commission where members were adversely impacted by being inappropriately attributed with a particular employment status under insurance arrangements.

[Note: In his Final Report, Commissioner Hayne suggested that ' Trustees must be required to make proper arrangements about the premiums that will be charged to default members. That can be achieved by APRA amending SPS 250 to require that any status attributed to default members (such as 'blue-collar', 'smoker', or other status affecting the premium to be charged for insurance) is fair and reasonable. Ordinarily that would require consideration of whether the status attributed is statistically appropriate. See: Financial Services Royal Commission final report, Volume 1, at p331]

- **Financial Services Royal Commission recommendation 4.14:** Revised SPS 250 proposes to introduce a new independent certification requirement for RSE licensees, where an insurance arrangement is with a related party insurer or gives a priority or privilege to an insurer, to give effect to Financial Services Royal Commission recommendation 4.14 (Additional scrutiny for related party engagements). APRA proposes that RSE licensees will need to provide the independent certification to APRA within five business days of its receipt, and no later than one calendar month prior to the RSE licensee entering into a new insurance arrangement or renewing an existing insurance arrangement. Where an insurance arrangement is for a term of, or exceeding, three years, the certification must be provided to APRA on a biennial basis.
- **The proposed change would require a process that enables beneficiaries to easily opt-out of insurance cover**
- **The proposed changes would require that the level/type of insurance cover not inappropriately erode the retirement income of beneficiaries.** The proposed change, 're-emphasises the existing SIS Act requirement in response to APRA's concern that some RSE licensees have not been giving adequate consideration to it' APRA states.

**Feedback on the compliance cost:** APRA requests that all interested stakeholders use this consultation opportunity to provide information on the compliance impact of the proposed changes and any other substantive costs associated with the changes.

**Timeline and next steps**

- The deadline for submissions is 3 February 2020
- Following consideration of submissions, in the first quarter of 2020 APRA will consult on a revised Prudential Practice Guide SPG 250 Insurance in Superannuation (SPG 250).
- APRA proposes that certain transitional requirements will commence on the date of registration of the Revised SPS 250 (anticipated to be in July 2020), with the remaining requirements to commence on 1 January 2021.

*[Sources: APRA media release 25/11/2019; Letter: Proposed revisions to Prudential Standard SPS 250 Insurance in Superannuation; Draft Prudential Standard SPS 250 Insurance in Superannuation - Clean - November 2019 ; Draft Prudential Standard SPS 250 Insurance in Superannuation - Marked up -November 2019]*

### In Brief | The PRA has imposed a combined financial penalty on Citigroup Global Markets Limited, Citibank NA. London branch and Citibank Europe Plc UK branch of £43.9 million for 'failings in relation to their internal controls and governance arrangements' underpinning compliance with PRA regulatory reporting requirements. The PRA notes that as Citi agreed to resolve the matter, a 30% reduction in the fine imposed by the PRA was applied. Without this discount, the fine imposed by the PRA would have been £62,700,000

*[Source: Bank of England media release 26/11/2019]*

### In Brief | Data sharing is key to addressing the risk of child exploitation: The AFR reports that Singapore based not-for-profit, the International Centre for Missing & Exploited Children, is due to hold its regular meeting with the major banks, major remittance providers (Western Union, MoneyGram and WorldRemit), the eSafety Commissioner, the NSW, Victorian and Queensland police forces, the Australian Institute of Criminology, AUSTRAC and the Federal Police to formulate plans for the better sharing of data. This is considered key to improving the quality of intelligence and therefore to tackling child exploitation in Asia

*[Source: [registration required] The AFR 26/11/2019]*

### In Brief | As part of the government's Retirement Income Review, Treasury has released a consultation paper setting out a number of questions it would like submissions to address. The deadline for submissions is 3 February 2020. The panel's first report is due by June 2020

*[Sources: Treasury media release 22/11/2019; Retirement Income Review Consultation Paper 22/11/2019]*

**In Brief | Transcripts of the recent parliamentary hearings on the superannuation sector, at which a number of funds and peak bodies were asked questions concerning their response to the Financial Services Royal Commission recommendations, their opinions on APRA's heatmaps, their approach to consolidating duplicate accounts and their approaches to investment decision making (among other issues) have been released**

*[Sources: House of Representatives Standing Committee: Australia's four major banks and other financial institutions: superannuation sector 21/11/2019; 22/11/2019]*

## Accounting and Audit

**Proactively lifting standards? The Australian reports that PwC will establish an external board to review the quality of its audit practice and change the way the performance of audit partners is assessed**

The Australian reports that PwC plans to establish an external, independent audit quality advisory board to review the quality of the firm's audit practice and enhance its approach to audit quality. Reportedly the three person board will be comprised of 'eminent people well known for their integrity, governance, knowledge of our world'.

In addition, PwC has reportedly said it is reviewing the performance of its audit partners against a new scorecard. The scorecard will incorporate feedback from partner's teams and audit committees and also review how they use automation and other specialist expertise as well as considering the results of internal/external inspection outcomes.

*[Source: [registration required] The Australian 25/11/2019]*

**In Brief | The transcript of ASIC's appearance before the first parliamentary hearing into the regulation of the audit sector has been released. The next hearing is scheduled for 29 November**

*[Sources: Parliamentary Joint Committee on Corporations and Financial Services: Regulation of Auditing in Australia transcript 19/11/2019; Program 29/11/2019]*

## Risk Management

**The UK Institute of Directors has released a corporate governance manifesto putting forward ten policy to lift governance standards**

Ahead of the UK general election, The UK Institute of Directors (IoD) has released a corporate governance manifesto, putting forward ten policy proposals to lift governance standards and 'reinforce the UK's pre-eminent position in the global corporate governance space'.

The proposals also offer, the IoD suggests, a mechanism through which business can rebuild community trust, without the need for 'heaving handed regulation'.

**Objectives of the ten proposals**

The proposals are underpinned by three objectives: 1) to increase the accountability of the UK corporate governance system to stakeholders and wider society; 2) to improve the competence and professionalism of UK board members as key business decision makers; and 3) to enhance the ability of board members to pursue longterm, sustainable business behaviour, including addressing the challenge of climate change.

**Proposals**

**Strengthening accountability of the UK governance system**

1. **Support the development of an industry-led, formal Code of Conduct for Directors of significant corporate entities** (ie companies exceeding a certain size threshold or level of importance for stakeholders and the wider UK economy) to guide their activities/behaviour as a professional group. The IoD comments that such Codes are already in place in other professions eg accountancy/legal professions. The 'absence of a professional framework of conduct or ethics – which goes beyond mere compliance with the law - is of particular concern at a time when public trust in directors and business more generally remains fragile' the IoD writes. Further, the IoD observes that in the 'wake of the recent high-profile corporate collapses, there is an understandable demand for board members to be held more accountable for failures of oversight and direction'.

2. **Deliver proposed reforms to the regulation of auditors:** The IoD calls on the incoming government to introduce the necessary legislation to enact Sir John Kingman's recommendations concerning external audit regulation, and more particularly to introduce the necessary legislation to create The Audit, Reporting and Governance Authority (to replace the Financial Conduct Authority (FRC)). 'The outgoing Government did not allocate Parliamentary time to this legislation in the Queen's Speech, and this urgently needs to be remedied by the incoming administration' the IoD states.

[Note: The Final Report of the Independent Review of the Financial Reporting Council led by Sir John Kingman (Kingman Review) was publicly released in December 2018. The full text of the Kingman Review can be accessed here. For a summary see: Governance News 16/01/2019]

3. **Establish an independent Corporate Governance Commission** to oversee the UK's corporate governance and stewardship codes framework and freeing up the Financial Reporting Council's (FRC's) successor (ARGA) to focus on its core task of improving company audits. 'Despite endorsing Sir John Kingman's recommendations concerning audit regulation, we believe that having corporate governance and investor stewardship regulated within the same body as statutory audit is a far from ideal approach' because it means 'corporate governance is just one concern amongst many' the IoD writes.

4. **Prioritise upgrades to the operation and functioning of Companies House**. The IoD writes that the current government has developed a range of proposals to improve the functioning of the UK Registrar of Companies at Companies House including measures to better scrutinise the accuracy of UK company data and reduce the likelihood of identity theft. The IoD argues that these reforms should be prioritised through the allocation of the necessary resources and parliamentary time through which to enact the required primary legislation.

**Proposals to increase the competence and professionalism of UK board members**

5. **Mandate minimum requirements for director training:** Noting that currently, there are no mandatory minimum educational/professional requirements in place for UK directors, the IoD proposes that the government should introduce a new requirement for all newly-appointed directors of significant entities to fulfil a minimum requirement in terms of director training and professional development. Further, the IoD suggests that 'directors at companies of all sizes can benefit from job-specific training and we call on the Government to increase the focus in this area'. The IoD suggests that revising the Corporate Governance Code to increase the expectation that directors had undertaken some formal training would be a positive step.

6. **Encourage the adoption of a Code of Practice for board evaluation:** Currently, the UK Corporate Governance Code requires an independent board evaluation to be undertaken at least once every three years, but there is little consistency in the way in which such evaluations are undertaken which, IoD argues, reduces their value to stakeholders. To support improved consistency, the IoD proposes that the government should 'push forward with the introduction of a voluntary Code of Practice for the providers of board evaluation services and formal arrangements for implementing and monitoring such a code'.

**Proposals to encourage a longer-term, sustainable approach to business behaviour**

7. **Create a framework through which companies 'can project their Business Purpose':** The IoD proposes that the government should 'encourage' companies to adopt clearly defined 'business purpose' clauses/business purpose statements, either in their constitutional framework or elsewhere in their annual report, to enable companies to communicate their expected social impact beyond 'merely maximising profits'.

8. **Encourage a consistent approach to Climate-Related Corporate Disclosures:** The IoD proposes that the government – working together with other relevant bodies - should mandate a consistent framework of corporate reporting on climate change to be implemented by UK companies. The IoD notes that consistent with the government's Green Finance Strategy, asset owners and listed companies are expected to report in accordance with the requirements of the Task Force on Climate-Related Financial Disclosures by 2022. However, the IoD argues that 'an appropriate reporting framework should be implemented for UK listed companies as soon as possible. The FCA has indicated that it would like to see such a reporting framework implemented in 2020, and the government should get behind this ambition'.

9. **Explore opportunities to establish an ESG oriented Sovereign Wealth Fund** to invest in 'the green and sustainable companies of the future and in doing so embed the highest standards of corporate governance across the economy'. The IoD suggests that this entity could be funded through the sale of

government backed bonds to institutional investors looking for secure ESG (Environment, Social, Governance)-oriented investments. Further, it's suggested that the entity should be overseen by an arms-length body and insulated from political control in order to ensure that the right decisions are made for the long term.

10. **Establish a newly-defined corporate form – the Public Service Corporation - through which the outsourcing of public services and related activities could be delivered.** It's proposed that like a private company, such a vehicle would have shareholders and operate on a commercial basis, but its underlying legal framework would require a balance to be maintained between the interests and obligations relating to its various stakeholders, including its shareholders, employees, pensioners, creditors and public sector clients. This duty would be defined in the general legal duties of its board of directors.

    The composition of the board would also 'reflect a more pluralistic approach'. In particular, the IoD proposes that 'key stakeholders' would have input into the appointment or dismissal of directors (in addition to shareholders).

    The IoD does not propose that this corporate form should be imposed on outsourcing companies on a mandatory basis, but rather should be 'encouraged through government procurement decisions on the basis that such entities would embody a good balance between commercial know-how, prudent governance and social legitimacy'.

*[Sources: IoD Manifesto for Corporate Governance; [registration required] The FT 20/11/2019]*

### Trends in managing cybersecurity risk: The structure and composition of S&P 100 boards is changing in response to increasing concern and acceptance of the threat cybersecurity incidents pose to business

The Nasdaq Center for Corporate Governance has published a report — Boards through the lens of cybersecurity — into the different approaches S&P 100 boards are taking to cybersecurity risk oversight.

Overall, the report found that the continuous rise of high-profile cybersecurity incidents and their cost to the business has raised awareness of the need for boards to view cybersecurity risks as 'an existential threat to longterm business sustainability' and that this has translated into changes in board/committee composition, board committee structure, oversight and reporting processes.

**Some Key Findings**

- **2019 proxy statements showed that 27% of companies disclosed insights on recent cybersecurity activities taken by boards**. The top three most common disclosed activities included: 1) the company discussed cybersecurity as part of its investor engagement conversations; 2) cybersecurity was an investment priority or key area of focus in the past year; and 3) new directors with relevant expertise had been added to the board.
- **Most S&P 100 companies (88%) have charged at least one board-level committee, usually the audit committee (64%), with cybersecurity oversight.** Outside of the audit committee, the board committees that were frequently delegated cybersecurity oversight responsibilities included the risk, technology, or compliance focused committees. It was rare to see a board-level committee exclusively dedicated to cybersecurity.
- **32% of board level committees charged with cybersecurity oversight included a board leader** (the lead independent director) and 48% at least one other board committee chair. For example, where the audit committee has been charged with cybersecurity oversight, committee members might include the risk or technology committee chair. In some cases, this overlap appears intended to enhance oversight and communication. Over three-quarters of those committees charged with cybersecurity oversight (78%) identified at least one individual with a background in cybersecurity or technology (72%) or risk (41%).
- **The report found that the way in which management reports to the board differs widely**. In 27% of cases, management reports to a named executive/executives, with that executive reporting to the board/committee. The most common executive title was Chief Information Security Officer, followed by Chief Information Officer and Chief Technology Officer. Some companies also had a dedicated Chief Privacy Officer charged with safeguarding consumer information and data. Most companies said that they report on a 'regular' or periodic basis, with only 13% saying that they report at least annually/quarterly.

- **Directors charged with cybersecurity oversight tend to be younger, have cybersecurity expertise:** A review of the directors charged with cybersecurity oversight found that the majority were in the 50 to 63 age group followed by those in the 64 to 70 age group and those in the 70+ age group. Directors under the age of 50 comprised less than 5% and most were recent appointments, having board tenure of two years or less. In terms of expertise, just under two-thirds of directors under the age of 50 were associated with cybersecurity or technology experience, compared to just under one-quarter of those over the age of 70. Risk expertise was associated with exactly one-third of directors under the age of 50 and over one-third of those over the age of 70. Women directors represented exactly half of the directors under the age of 50, compared to just under one-fifth over the age of 70.
- **Overall, women directors accounted for one-third of S&P 100 directors charged with cybersecurity oversight.** Women directors were generally younger, with an average age of 59 compared to 63 for men. Given that board tenure was similar for both groups (around 6.6 years), the age difference suggests that the women directors had joined boards earlier in their careers.

*[Source: Nasqaq Centre for Corporate Governance report: Board through the lens of cybersecurity 22/11/2019]*