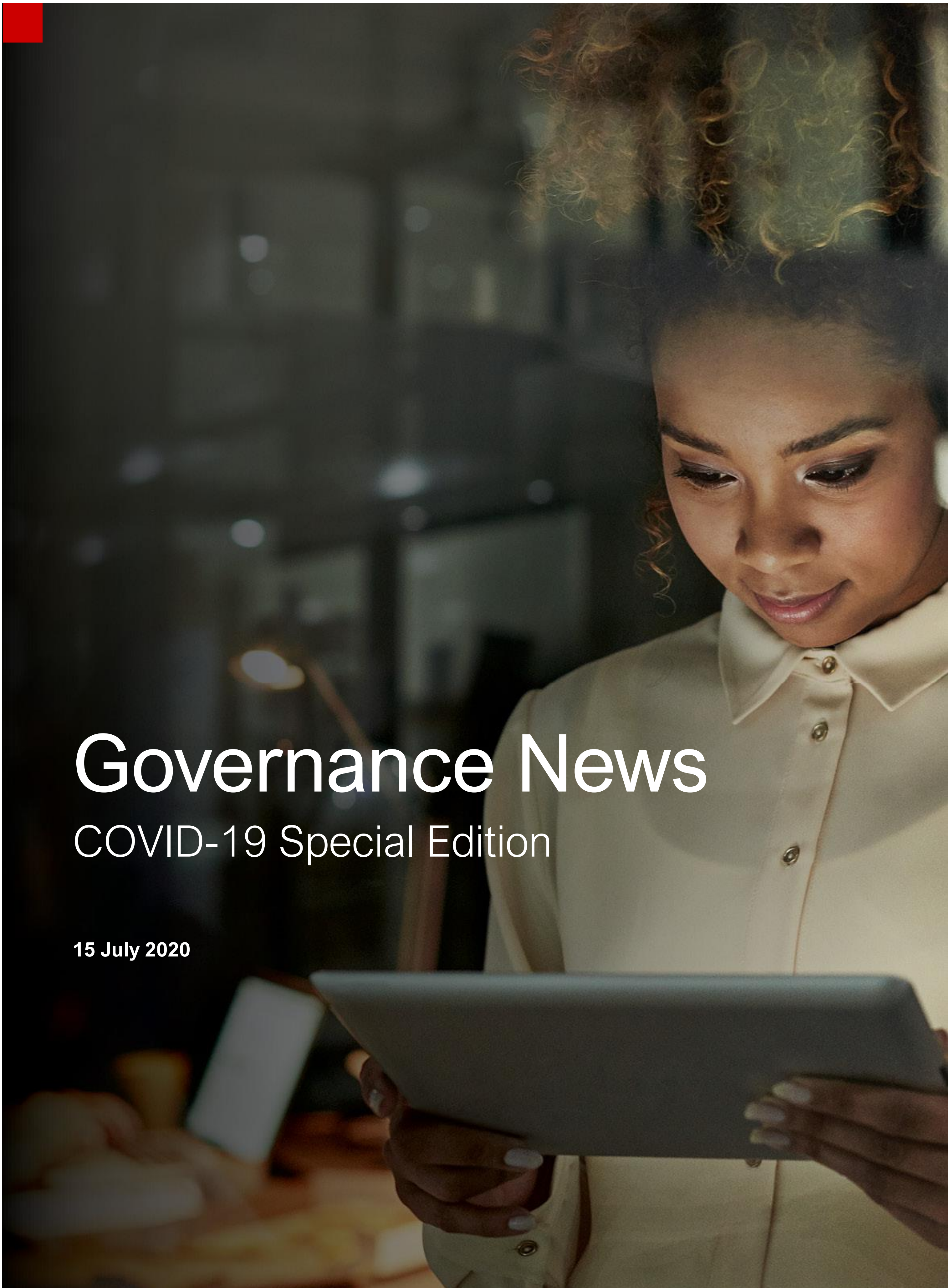


Governance News

COVID-19 Special Edition

15 July 2020

Contents

Remuneration __ 4

Equilar finds that median CEO pay remained overall stable in 2019, the impact of COVID-19 on pay is as yet unclear 4

Institutional Investors and Stewardship __ 5

(Potentially) shutting the door on ESG investments? Proposed DOL rule changes would make it difficult for US pension funds to make ESG investments, unless they are able to justify doing so purely on the basis of financial returns 5

Shareholder Activism __ 6

Snapshot of activist activity H1 2020: Activist Insight report reveals activist activity in Australia has declined 50% on H1 2019 levels 6

Disclosure and Reporting __ 8

SEC proposes to do away with the requirement for 'smaller' institutional investment managers to report quarterly on their US stockholdings 8

What does effective reporting on stakeholder issues look like? The FRC's financial reporting lab is set to conduct a review of corporate stakeholder reporting including s172 statements 8

COVID-19: Trends in COVID-19 disclosure by US companies 9

No need? SEC Commissioner Elad L Roisman thinks SEC shouldn't mandate ESG disclosure for public companies (but should consider doing so for asset managers) 10

Financial Services __ 12

Top Story | Protecting vulnerable consumers: ASIC targets continuing credit contracts 12

COVID-19: So far funds have paid out $19.1bn under the government's early release of superannuation scheme according to APRA's latest update 14

COVID-19: Four month extension of temporary emergency capital raising relief 14

BCCC will inquire into compliance with the vulnerability provisions in the Banking Code 15

First enforcement action by a regulator against a financial institution for dealings with Jeffry Epstein: Deutsche Bank has agreed to pay $150m penalty 15

Leadership change at ME Bank: CEO to step down at the end of July 16

In Brief | Westpac has announced that KPMG Partner Michael Rowland has been appointed as Westpac's CFO, subject to regulatory approval. Acting CFO Gary Thursby will continue acting in this role until Mr Rowland joins Westpac later in the year 16

In Brief | Better than outsourcing as we know it? Academics have suggested that introducing a 'mentorship regime' to provide a 'reliable regulatory framework' for partnership agreements between fintechs and regulated banks would put outsourcing of banking services on firmer footing 16

Accounting and Audit __ 17

Results of FRC audit inspections: 33% of firms still falling short 17

'Professionalising' the role of corproate director? Preventing future audit scandals will require looking not just at auditors but at boards says the IoD 18

Ensuring international audit standards are responsive to the public interest: The Monitoring Group has released recommendations to strengthen the international standard setting system 18

In Brief | A failure of corporate culture? Columbia academic Todd Baker has written a summary of what is known so far about the Wirecard scandal, which includes some reflections on its causes. One conclusion he draws is that the company's supervisory board appears to have failed in their oversight duties. 'Theirs [the supervisory board] is a failure of corporate culture and of independence and integrity – reflected in their blind loyalty to management despite mounting problems and their hostility to shoe who asked legitimate questions about the company's operations' 19

Risk Management __ 20

Climate Risk 20

Certified as 'carbon neutral': Telstra and separately Local Government Super have announced they have each been certified as carbon neutral by Climate Active 20

First State Super divests fossil fuel investments 21

UNSW report finds Australia is the world's largest exporter of fossil fuel emissions and therefore a major contributor to global climate change 22

In Brief | Study confirms that pricing carbon works to lower emissions: Analysis of data from 142 countries over more than two decades has concluded that countries with carbon prices on average have annual carbon emissions growth rates that are lower than countries without a carbon price 22

Technology, Cybersecurity and Privacy 22

ClearView AI Inc's use of 'scraped data' and the biometrics of individuals is under investigation: Joint UK/Australian probe into Clearview AI Inc announced 22

Investment Association warns investors about the risk of 'impersonation scams' after a sudden spike in scam activity 23

In Brief | A major cyber incident could have more of an economic impact that COVID-19? AustCyber found that a four-week digital disruption resulting from a significant cyber incident could cost the economy AU$30 billion, the equivalent of around 1.5% of GDP 23

Other Developments 24

Brexit: IoD research finds less than a quarter of directors feel their organisation is fully prepared for the end of the Brexit transition period, the IoD has called for a phased approach to introducing changes 24

Remuneration

Equilar finds that median CEO pay remained overall stable in 2019, the impact of COVID-19 on pay is as yet unclear

Equilar's latest CEO Pay Trends report tracks CEO compensation data at the largest 500 largest listed companies in the US over the past fiscal year.

Some Key Points

In a short statement Equilar highlighted a number of key insights from the report. These include the following.

- Overall there was no increase in median pay in 2019: Equilar found that median CEO pay overall remained stable at 2018 levels at $12.3m. Equilar observes that though there was no increase on 2018 levels, median CEO pay has increased by 22% since 2015.
- Some sectors did see increases: In some sectors – consumer, healthcare, industrial, utilities, defence - CEO pay increased 2018 to 2019. The largest increase (11.3%)was in the healthcare sector.
- Impact of COVID-19: 91 of the 500 companies included in the report reduced CEO pay in response to COVID-19. Equilar comments that the overall impact of the pandemic on executive compensation plans is still unfolding with many companies still working out how to adapt/what adjustments to make. One impact of this may be, it's suggested, that companies may elect not to set multi-year financial goals and/or reduce the number of performance shares granted to CEOs.

[Source: Equilar media release 09/07/2020]

Institutional Investors and Stewardship

(Potentially) shutting the door on ESG investments? Proposed DOL rule changes would make it difficult for US pension funds to make ESG investments, unless they are able to justify doing so purely on the basis of financial returns

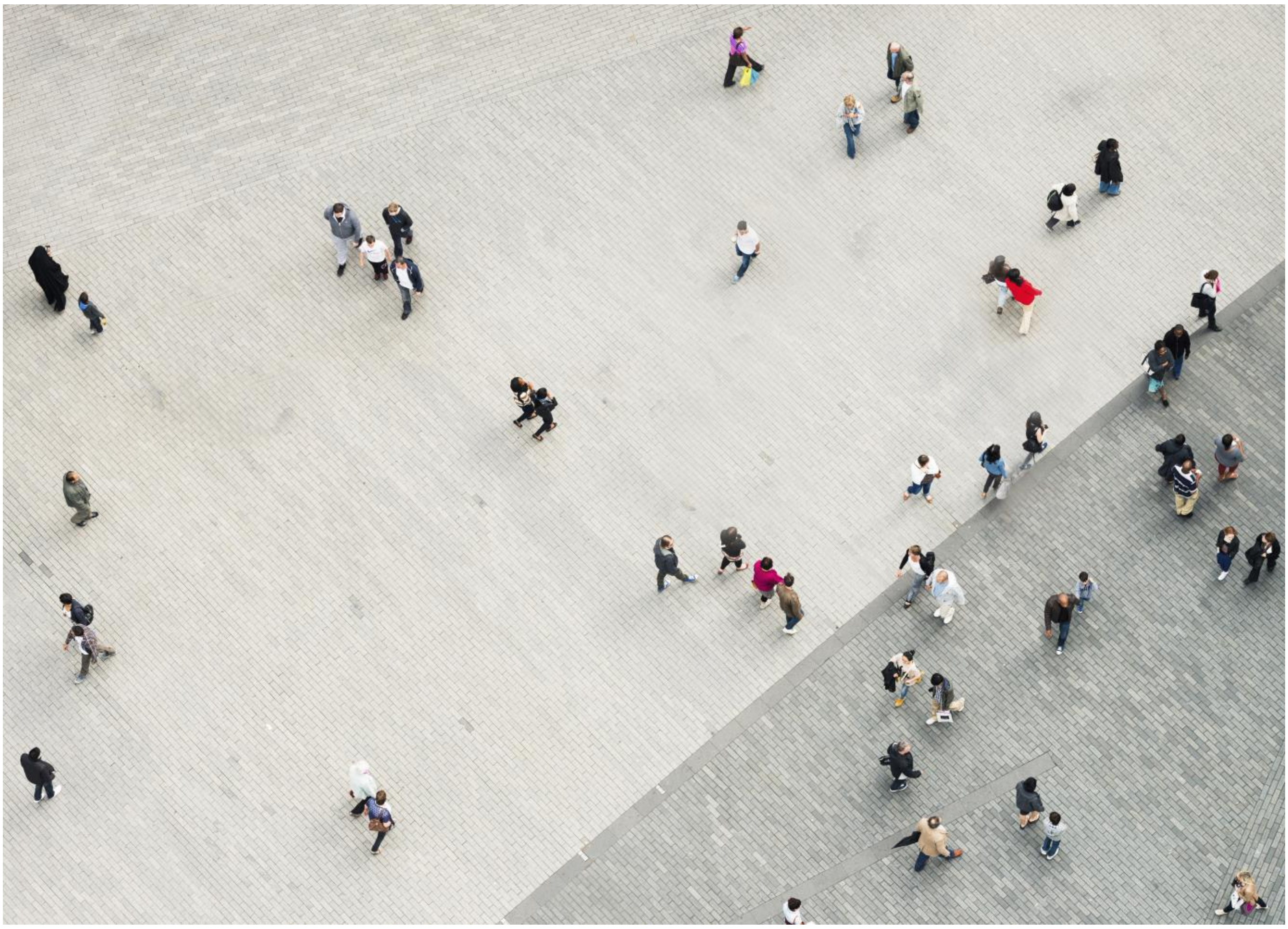
On 23 June, the US Department Of Labor (DOL) proposed a rule to make clear that 'ERISA [Employee Retirement Income Security Act of 1974] plan fiduciaries may not invest in ESG vehicles when they understand an underlying investment strategy of the vehicle is to subordinate return or increase risk for the purpose of non-financial objectives'.

In other worlds, DOL proposes to require pensions funds to select investments and investment courses of action based on financial considerations and to prohibit fiduciaries from 'subordinating the interests of plan participants and beneficiaries in retirement income and financial benefits under the plan to non-pecuniary goals'.

The proposal is open for a 30 day comment period.

Manifest Minerva reports that democratic representatives Patty Murray and Bobby Scott have called for an extension of the comment period.

[Sources: Department of Labor media release 23/06/2020; Department of Labor Fact Sheet 23/06/2020; Manifeset Minerva 09/07/2020]



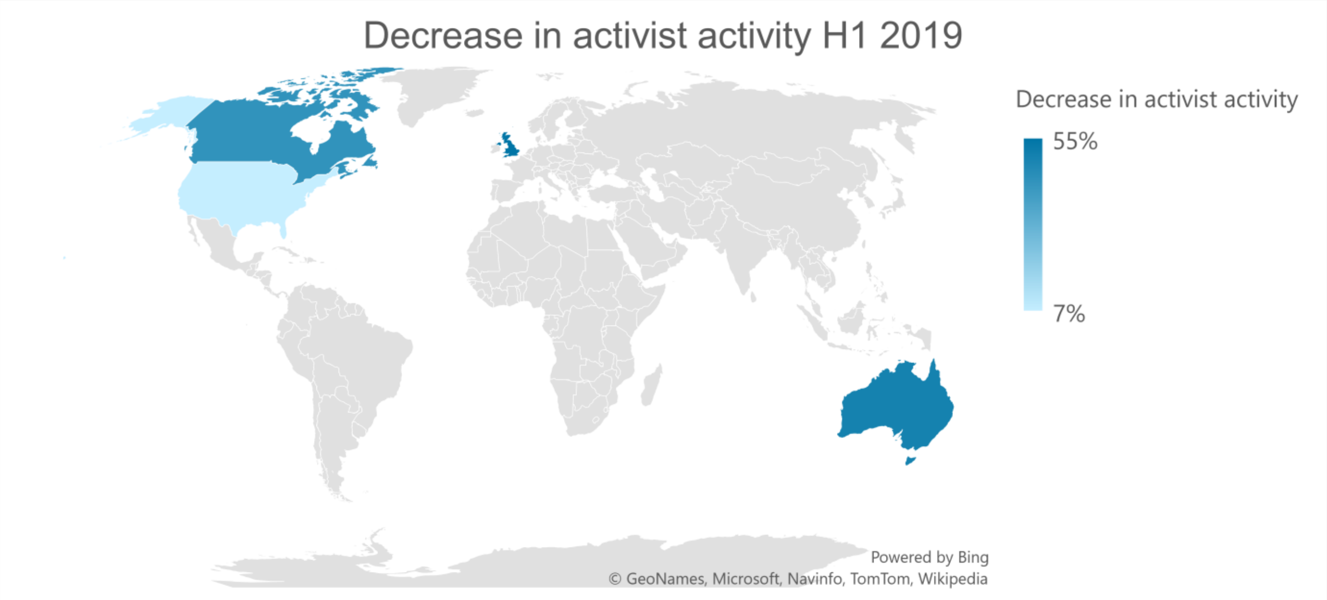
Shareholder Activism

Snapshot of activist activity H1 2020: Activist Insight report reveals activist activity in Australia has declined 50% on H1 2019 levels

Key Takeouts

- 522 companies were publicly subjected to activist campaigns in H1 2020. This is down on the seven year average for the same period (564) and significantly down on H1 2019 (628).
- Activist activity declined everywhere, but the level of the decline varied across regions.
- Australia was one of the three countries that saw the greatest decrease in activity: The level of the decline was greatest in the UK (55% decline in activist activity on H1 2019 levels), Australia (50% decline on H1 2019 levels) and Canada (43% decline on H1 2019 levels).

Activist Insight has released its latest report – The Activist Investing Half Year Review – into global activist activity over the first six months of 2020. A key finding is that globally activist activity has significantly declined but that the decline is not uniform across regions.



Some Key Points

Overall decline in activist activity

- The number of activists worldwide making public demands on companies fell 31% on H1 2019 levels to 332.
- 522 companies were publicly subjected to activist campaigns in H1 2020. This is down on the seven year average for the same period (564) and significantly down on H1 2019 (628).
- Activist activity declined everywhere, but the level of the decline varied across regions.
- The level of the decline was greatest in the UK (55% decline in activist activity on H1 2019 levels), Australia (50% decline on H1 2019 levels) and Canada (43% decline on H1 2019 levels).
- Activist activity in the US decreased least as compared with other regions (there was a 7% on H1 2019 levels).
- The report found that there were some differences between the US and other regions. For example, in the US, activists made more balance sheet demands than they did in the same period in 2019. In contrast activists'

balance sheet demands in all other regions were down on H1 2019 levels. In the US, M&A related demands fell 51%, but only 19% elsewhere.

Vulnerability to activism

The report includes an interview with senior managing director and practice leader, activist and M&A solutions at FTI consulting Jay Frankl on the reasons for the slowdown in activist activity, which sectors are most vulnerable to activism and how companies can reduce their vulnerability.

Why the slowdown in activist activity? Mr Frankl is quoted in the report as saying that he considers that the lack of clarity around the impact of COVID-19 on the profits of companies explains in part the immediate decrease in activity. He also suggested that 'optics' has played a role in the slowdown. 'Many funds, especially those who think of themselves as constructivists, would have difficulty convincing others of their constructivist nature by continuing a campaign in such an environment, especially as many companies must shift into cost containment mode. No amount of PR by the funds will convince investors that the funds are in it for the long-term by running a proxy contest during a pandemic' he said.

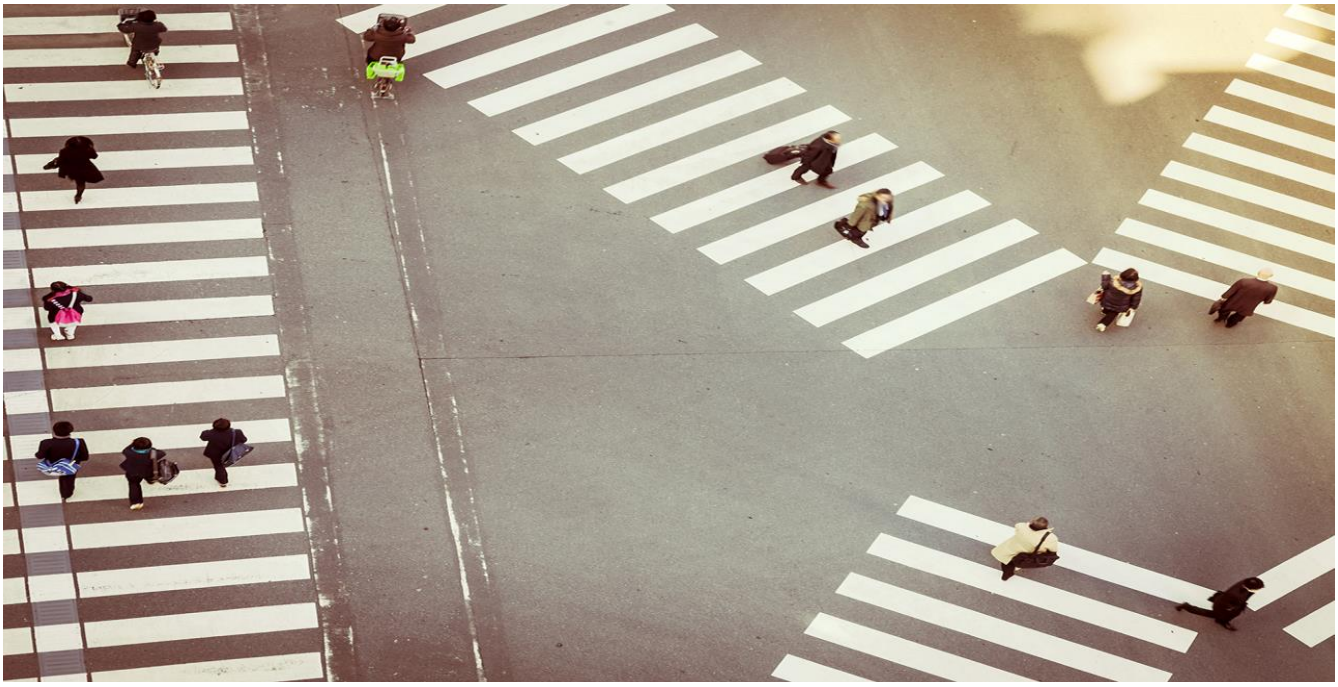
Sectors most vulnerable to activism?: Mr Frankle said that going into the crisis, sectors experiencing high levels of structural change – media, telecommunications and publishing – were the most vulnerable, but that this has shifted. Activists are increasingly targeting companies in the professional services sector and separately energy/power companies.

Reducing vulnerability? Asked how companies can reduce their vulnerability to activism, Mr Frankl said that 'self-awareness' including awareness of ESG issues, is the key in this type of environment'. Mr Frankl states,

> 'Management teams and boards of directors must be vigilant about liquidity, governance, and performance relative to peers. This comes with the added challenge of tossing out historical metrics, such as general costs and gross margin trends, and below the line expenses and write-offs. ESG has also been on the rise; as such, it is increasingly important to consider how companies have handled their employees, especially in situations where layoffs, furloughs, and pay cuts have been necessary. A lot of scrutiny is being applied to companies that are instituting pay cuts that do not begin in the C-suite'.

[Note: Lazard's latest review of activist activity - Lazard's Review of Shareholder Activism - Q1 2020 – also identified consistent that activist activity had sharply declined and consistent with Mr Frankl's statements, suggested that ESG will remain a key focus for activists. For a summary see: Governance News 22/04/2020]

[Source: [registration required] Activist Insight Report: The Activist Investing Half Year Review]



Disclosure and Reporting

SEC proposes to do away with the requirement for 'smaller' institutional investment managers to report quarterly on their US stockholdings

Proposal to reduce reporting under 13F

- Context: Currently, institutional investment managers with holdings of more than $100 million are required to file quarterly reports with the Securities and Exchange Commission (S EC) on their US stockholdings.
- Proposed change: SEC is proposing to raise the reporting threshold (in Form 13F) from $100 million to $3.5 billion. SEC says that 'proposed adjusted threshold would provide relief [ie relieve the compliance burden and deliver costs savings] to smaller managers who are now subject to Form 13F reporting, while retaining data on over 90% of the dollar value of the securities currently reported'. Announcing the proposal, SEC Chair Jay Clayton said that it will 'update, for the first time in over 40 years, the 13F reporting threshold to a level that furthers the statutory goal of enabling the SEC to monitor holdings of larger investment managers while reducing unnecessary burdens on smaller managers.'
- The proposal also makes provision for the threshold to be further adjusted every five years, by mandating five yearly reviews of the threshold by SEC staff.

Opposition to the proposed change

- SEC Commissioner Allison Heron Lee has issued a statement publicly criticising the proposal and explaining why she is unable to support it. Commissioner Lee's concerns are threefold.
  1. The proposed change will 'limit visibility into portfolios controlling $2.3 trillion in assets'.
  2. It is unclear, on the data provided in support of the proposal, that the proposed change will necessarily deliver the projected cost savings. Commissioner Lee points out that the estimated cost is four times greater than previous estimates and is based on assumptions that 'vastly overstate the complexity and resulting burden of the reporting requirement'. 'I am concerned that the projected cost savings in today's proposal are greatly overstated and wholly inconsistent with the Commission's past analysis—and, importantly, that the actual cost savings do not justify the loss of visibility into portfolios controlling $2.3 trillion in assets' she states.
  3. Commissioner Lee also questions whether SEC has the statutory authority to raise the reporting threshold in any case. 'The enabling statute, at section 13(f)(1), provides no support for increasing the reporting threshold' Commissioner Lee states.

Next steps

The proposal will be published on the SEC's website and in the Federal Register for a 60 day comment period.

[Sources: SEC media release 10/07/2020; Commissioner Allison Heron Lee 10/07/2020]

What does effective reporting on stakeholder issues look like? The FRC's financial reporting lab is set to conduct a review of corporate stakeholder reporting including s172 statements

Context

Section 172 of the Companies Act 2006 (UK) states that

> '(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—
>
> (a) the likely consequences of any decision in the long term,
>
> (b) the interests of the company's employees,

(c) the need to foster the company's business relationships with suppliers, customers and others,

(d) the impact of the company's operations on the community and the environment,

(e) the desirability of the company maintaining a reputation for high standards of business conduct, and

(f) the need to act fairly as between members of the company'.

Section 414CZA (section 172(1) statement) of the Companies (Miscellaneous Reporting) Regulations 2018 introduced a new requirement for large companies to publish a s172 statement describing how the directors 'have had regard to the matters set out in section 172(1)(a) to (f) when performing their duty under section 172.'

2020 is the first year that all large companies will be required to prepare a s172 statement.

New project into corporate stakeholder reporting

The Financial Reporting Council's (FRC) financial reporting lab will conduct a review of corporate stakeholder reporting, including s172 statements, with a view to identifying: a) how companies approach reporting of stakeholder information (ie information about customers, employees, suppliers and their operating environment); b) which areas of reporting are the most challenging for companies; c) how information about stakeholders can be reported most effectively; and d) examples of best practice. In addition, the project will explore investor expectations and requirements. The lab states that the scope of the project is likely to evolve over time.

Call for participants

The lab has called for investors and companies to volunteer to participate in the project. FRC has not provided a project or completion timeline.

[Sources: FRC media release 09/07/2020; Financial Reporting Lab – further information]

COVID-19: Trends in COVID-19 disclosure by US companies

Associate Professor of Accounting at the Wharton School of the University of Pennsylvania Daniel Taylor has released a summary of the findings of research into COVID-19 disclosure by 3644 US listed companies. The research is based on a review of SEC filings (forms 8-K, 10-Q, and 10-K) during the period 1 January 2020 to 29 May 2020.

The full paper on which Professor Taylor's summary is based is available here.

Some Key Points

- **References to COVID-19 increased as rates of infection increased/restrictions were imposed:** By 31 January only 0.7% of companies had referenced COVID-19, increasing to 22% by 29 February. As coronavirus restrictions were implemented in the US and across Europe, disclosure also increased. By 15 March 41% of disclosures referenced COVID-19 and by the end of the month this had risen to 64%. By the end of May, 99.6% of companies had made some level of disclosure about the impact of the pandemic.
- **Exposure to China:** Companies with greater exposure to China (10% of their revenue from China) tended to disclose COVID-19 impacts earlier than companies with lower exposure.
- **Approach to disclosure varied by industry:** By 31 March 100% of travel/airline companies had made some level of disclosure about the impact of the pandemic in SEC filings as had 91% of companies in the entertainment industry. However, other sectors were slower to make any level of COVID-19 disclosure. For example only 55% of financial services firms had done so by 31 March.
- **Topic of disclosure:** The most prevalent forms of COVID-19 disclosure over the period 1 January to 29 May have been: 1) disclaimers to forward looking statements (59%); 2) the impact of the pandemic on cash (47%); 3) the impact of the pandemic on sales (44%); 4) the impact of the pandemic on supply chains (40%); and the impact of the pandemic on debt (also 40%). Disclosure about the impact of the pandemic on workers (eg layoffs or furlough) was the least prevalent form of disclosure over the period.
- **Emphasis in disclosure changed over time as the impact of the pandemic became clearer.** The research identified that in the early months of the year, supply chain impacts were the most common issue disclosed, but

that by May disclaimers to forward looking statements were the most common form of disclosure. This is line, its suggested, with the spread of the virus outside China.

- **Link between COVID-19 disclosure and (higher) fall in share-price:** According to the research, though most companies share prices fell in March to some degree, where companies issued COVID-19 related disclosure in March, the fall was 'significantly more negative'. The share price at companies that issued COVID-19 related disclosure in March fell 22.5%. In contrast, where companies made no COVID-19 disclosure the fall was 12.5%. However, when examined by industry, the data suggests that this is likely due to the companies' greater exposure/risks.

Professor Taylor suggests that these findings are interesting and potentially relevant in the context of considering how boards/management make decisions around when/what to disclose and also in the context of considering how companies can plan for/respond to a future 'black swan' events.

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 08/07/2020]

No need? SEC Commissioner Elad L Roisman thinks SEC shouldn't mandate ESG disclosure for public companies (but should consider doing so for asset managers)

The focus of Securities and Exchange Commission (SEC) Commissioner Elad L Roisman's keynote address to the Society for Corporate Governance National Conference was primarily on the Commissioner's own views on two aspects of ESG disclosure. Namely: 1) why SEC shouldn't mandate ESG disclosure for public companies; and 2) the case for the regulator mandating ESG disclosure for asset managers.

The speech was delivered following the SEC's Investor Advisory Committee's (IAC) recent recommendations that the regulator amend reporting requirements to include ESG factors.

Why SEC shouldn't mandate ESG disclosure for public companies

- **No consensus on what ESG means:** Commissioner Roisman opened his speech by observing that there is no 'consensus on what exactly "ESG" means'. He went on to question whether environmental and social considerations necessarily have the same relevance as governance issues from a disclosure perspective, given that 'governance reform focuses on the company itself and what is best for its optimal operation as well as its shareholders' when 'the same is not necessarily true of "E" or "S".'
- **Not practical to prescribe ESG reporting criteria:** Commissioner Roisman said that environmental and social issues are 'usually subjective and constantly evolving based on current events'. In consequence, he considers that ' 'requiring prescriptive disclosure would be difficult'.
- **Mandating ESG disclosure is often 'fraught with subjectivity and agendas that are often unrelated to "investor welfare"'** Commissioner Roisman said. In too many cases, 'people appear to blur their personal views on environmental and social issues with how they believe the federal securities laws should operate to regulate the actions of others'.
- **Mandating ESG disclosure is beyond the ambit of SEC's mission:** Commissioner Roisman said that he considers mandating ESG disclosure to be inconsistent with SEC's mission as a regulator. 'If I were to use the securities laws to pursue my own environmental and social vision for the world, I would be subordinating the SEC's mission to my personally held objectives. In other words, I would be acting outside the scope of my responsibility and authority. Imagine the unintended consequences that could flow from such an abuse of power'. Commissioner Roisman added that he considers that financial regulators lack the expertise to assess/address 'all of the potential negative effects that may result' from mandating ESG disclosure.
- **The existing principles-based materiality standard for disclosure is the best approach:** Commissioner Roisman considers that the existing principles-based approach, which requires companies to disclose material information (including information about material environmental risks) is the optimal approach because it: a) allows companies to tailor their disclosure according to the circumstances to be useful to their investors; and b) it has the effect of limiting the information being disclosed so that 'important information is not lost in a sea of inapplicable information'.
- **The existing framework provides incentives for companies to disclose material risks.** Commissioner Roisman observed that companies are not only subject to enforcement action by regulators should they fail to disclose

material information, and also to litigation risk. On this basis he considers that 'companies are on the hook — to a lot of different people — for everything they do (or do not) disclose in their filings. That seems like good incentive to me to disclose material information, ESG or otherwise'.

- Voluntary disclosure is already occurring: Commissioner Roisman welcomed the fact that a number of public companies are voluntarily providing ESG disclosure/acting on ESG related issues in response to calls from various quarters including calls from large investors and activists without government/regulatory action. 'I am happy to see this sort of private ordering take place. It is important to realize and acknowledge that companies provide information and act without the government telling them to do so for many different reasons, including because their customers, employees, and others motivate them to do so' Commissioner Roisman said.

The case for requiring asset managers to provide more ESG disclosure

Commissioner Roisman outlined a number of reasons to justify mandating ESG disclosure from asset managers.

In particular, he suggests that there is a case for requiring asset managers to provide more information around the meaning of labels such as 'ESG', 'green' and 'sustainable' in the context of advertising/other material. Additional disclosure, he considers would enable investors and regulators to understand how these considerations are reflected in funds' strategy and voting decisions and help address the risk of 'greenwashing'.

In addition, Commissioner Roisman raised concerns that there is a lack of clarity/lack of understanding on the part of investors that asset managers may be prioritising ESG issues at the expense of financial returns. He said, 'To me, it seems likely that a significant portion of those who invest in ESG funds want to "do well" while "doing good"—seems like a win/win. But, some of these funds invest and vote proxies primarily to achieve some environmental or social good, possibly at the expense of investment returns. This is less of a win/win, especially if a fund's disclosure is not transparent on this point. Do asset managers believe this is the appropriate trade-off for their investors, and how are they evaluating their own performance in this regard? Do retail investors know if they are leaving money on the table?'

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 08/07/2020]

Financial Services

Top Story | Protecting vulnerable consumers: ASIC targets continuing credit contracts

Overview | ASIC consultation paper 330 Using the product intervention power: Continuing credit contracts (CP 330)

Key Takeouts

- The Australian Securities and Investments Commission (ASIC) proposes to use its product intervention power to target certain 'continuing credit contracts' that it considers cause 'significant consumer detriment' to vulnerable customers.
- ASIC observes that the continuing credit contracts being targeted 'appear to have been introduced into the market following ASIC's previous product intervention order relating to short term credit' and are provided by/managed by (some) of the same entities (Cigno and BHFS).
- ASIC proposes to impose an industry wide product intervention order that would impose a cost cap on the total fees that can be charged under continuing credit contracts targeted at low income/unemployed retail clients.
- Before ASIC can take action, it is required to consult on its proposed intervention. The due date for submissions is 6 August 2020.
- The Consumer Action Law Centre has issued a statement welcoming ASIC's proposed action and calling on the Federal government to prioritise implementation of the Small Amount Credit Contract Bill to permanently strengthen consumer protections

Overview

The Australian Securities and Investments Commission (ASIC) has released a consultation paper - ASIC consultation paper 330 Using the product intervention power: Continuing credit contracts (CP 330) - setting out its proposal for using its product intervention power under Pt 7.9A of the Corporations Act 2001 (Cth) to address what it considers to be the significant consumer detriment resulting from the circumstances in which certain continuing credit contracts are marketed to vulnerable consumers.

Targeting 'payday loans' marketed to low income/unemployed people

ASIC proposes to use its product intervention power (PIP) to impose a cost cap on the total fees that can be charged under certain continuing credit contracts targeted at low income/unemployed retail clients.

The proposed cost cap is intended to address what ASIC considers to be the significant consumer detriment resulting from the very high fees/charges for services attached to loans (under continuing credit contracts and accompanying service agreements) marketed to consumers on Cigno Pty Ltd's (Cigno) website as 'payday loans', 'centrelink loans', 'bad-credit loans', 'no credit loans', 'loans for unemployed people', 'emergency loans' and 'fast cash loans'.

To access these loans, customers enter into a continuing credit contract with BHF Solutions Pty Ltd (BHFS) under which they agree to pay a fixed fee for every advance of funds under the contract up to a maximum of $120 in any twelve month period.

They also enter into a services agreement with Cigno, under which they pay Cigno for various services.

Combined, the fees and charges imposed under the continuing credit contract and services agreement exceed the maximum charges prescribed by the continuing credit exemption and reg 51 of the National Credit Regulations. They often exceed the total loan amount by a significant degree. In the four examples included in the consultation paper, the fees and charges to clients exceeded the original loan amounts by between 220% and 490%.

Significant Consumer Detriment

ASIC says that the very high cost of the loans, which are targeted at low income and/or unemployed consumers, can result in significant consumer detriment eg by impacting borrowers' ability to meet basic living expenses over an extended period; and/or 'exacerbating' existing financial stress and/or adding to financial exclusion.

ASIC considers these impacts may be 'further exacerbated' by the impact of the COVID-19 pandemic given the projected uptick in the unemployment rate.

ASIC's proposed order

ASIC proposes to make an industry-wide product intervention order banning credit providers and their associates (including directors of such entities) from 'issuing continuing credit contracts in circumstances where total fees exceed the maximum permitted under the continuing credit exemption and reg 51 of the National Credit Regulations'.

ASIC's proposed order is here.

Timeline: The due date for submission is 6 August 2020.

Initial response: CALC has welcomed ASIC's proposed use of the PIP

In a statement welcoming ASIC's proposed action, Consumer Action Law Centre CEO Gerard Brody said 'The short-term lending market is desperately in need of additional consumer protections. The evasive business model being used by Cigno to avoid responsible lending laws is yet another clear example of short-term lenders causing significant harm'.

Mr Brody went on call for the government to prioritise implementation of the Small Amount Credit Contract Bill as a means of permanently strengthening consumer protections.

> 'This industry is in desperate need of an overhaul to protect consumers. The only long-term answer is legislative reform that addresses this behaviour and the Federal Government needs to deliver on its commitment to the reforms recommended by the 2016 Small Amount Credit Contract Review. Over 1,300 days have passed since the Government accepted the recommendations of the review, which included a broad anti-avoidance provision. The Small Amount Credit Contract Bill, if passed, would have prevented both of these harmful lending models. It needs to be passed as a matter of priority' Mr Brody said.
>
> [Note: The Bill referred to is the National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2019 (No. 2) which was introduced into the Senate by Labor Senator Jenny McAllister and Centre Alliance Senator Stirling Griff on 2 December 2019. The explanatory memorandum states that the 'Bill replicates word for word the Government's Exposure Draft legislation, released on 23 October 2017'. The Bill was referred to the Senate Standing Economics Committee which is due to report by 21 September 2020.]

Background

- In September 2019, the Australia Securities and Investments Commission (ASIC) deployed its new product intervention power for the first time to target a specific short term lending model, used by Cigno Pty Ltd (Cigno) and Gold-Silver Standard Finance Pty Ltd, MYFI Australia Pty Ltd and BHF Solutions Pty Ltd (BHFS), that it considered caused 'significant consumer detriment' to vulnerable customers.

- Cigno subsequently applied to the Federal Court for judicial review of the product intervention order, but the order was upheld (Cigno Pty Ltd v Australian Securities and Investments Commission [2020] FCA 479). Cigno filed an appeal on 13 May 2020.

- ASIC has subsequently issued final guidance - RG 272 Product intervention power - outlining how it will use its product intervention power. The guidance makes clear that 'significant consumer detriment' may arise as a result of a product's inherent design features and/or consistent with the decision in Cigno Pty Ltd v Australian Securities and Investments Commission [2020] FCA 479, as a result of the circumstances in which the product is offered (eg marketed or targeted at) consumers.

[Sources: ASIC Media release 09/07/2020; ASIC consultation paper 330 Using the product intervention power: Continuing credit contracts (CP 330); Draft instrument; Consumer Action Law Centre 09/07/2020]

COVID-19: So far funds have paid out $19.1bn under the government's early release of superannuation scheme according to APRA's latest update

The Australian Prudential Regulation Authority (APRA) has released industry-level and fund-level data on the early release of superannuation scheme for applications received during the period 20 April (inception of the scheme) to 5 July 2020.

The data includes both initial applications and repeat applications

Under the early release of superannuation scheme, people financially impacted by COVID-19 can apply to withdraw up to $10,000 in FY 2019/20 and up to $10,000 in FY 2020/21.

APRA notes that the statistics for this week include both initial applications (made in both time periods) and repeat applications. APRA comments that:

> 'It is important to note that the number of applications reflected in the statistics exceeds the number of individuals that have applied as some applications relate to more than one superannuation fund. APRA is therefore unable to identify precisely how many superannuation members have withdrawn benefits during both eligible time periods. The data collection is also unable to precisely determine how many applications apply to the 2019/20 financial year as opposed to the 2020/21 financial year, given the reporting windows and lags that exist in the application and reporting process'.

APRA comments that high volumes of applications are expected to come through in July and that processing time may be impacted in consequence.

Statistics

- Total payments made since the inception of the scheme have taken an average of 3.3 business days to process, with 95.2% of payments made within five business days.
- Over the week to 5 July, superannuation funds received 511,000 applications, a 'significant increase' on the 127,000 received in the week to 28 June, but a lower volume than the 665,000 applications received during the first week of the early release scheme (in the week to 27 April).
- Of the 511,000 applications received, 165,000 were for members applying for early release for the first time (initial application) and 346,000 were for members applying for the second time (repeat application). The average amount applied for by those making an initial application was $7476, the average amount applied for by those making a repeat application was $8,904.
- Over the week to 5 July, superannuation funds made payments to 132,000 members worth close to $1 billion, with $19.1 billion paid since inception. The average payment made over the period since inception is $7,511.

[Sources: APRA media release 14/07/2020; Infographic 14/07/2020]

COVID-19: Four month extension of temporary emergency capital raising relief

- **Context:** ASX announced in the 31 March 2020 Listed@ASX Compliance Update that it had introduced two class order waivers implementing temporary emergency capital raising measures for the purpose of assisting listed entities adversely impacted by the pandemic, to raise capital. These waivers were subsequently updated on the 22 and 23 April and were set to expire on 31 July 2020.
- **Four month extension announced:** In the 13 July 2020 Listed@ASX Compliance Update, the ASX announced that the relief measures have been extended for four months until 30 November 2020 by the publication (on 9 July) of two replacement class waivers: 1) Temporary Extra Placement Capacity Class Waiver; and 2) Non-

renounceable Offers Class Waiver. The replacement Class Waivers apply to all relevant capital raisings announced on or after 9 July 2020 and on or before 30 November 2020.

- **Rationale for the extension:** ASX says that the decision to extend the relief was made in light of: a) the increasing levels of COVID-19 infections in major overseas markets; b) the recent uptick in COVID-19 infections in Victoria; and c) the uncertainty around the nature and extent of government economic stimulus that will be available post September 2020.

[Source: 13 July 2020 Listed@ASX Compliance Update]

BCCC will inquire into compliance with the vulnerability provisions in the Banking Code

The Banking Code Compliance Committee (BCCC) is conducting a nine month inquiry into member banks' compliance with Part Four of the Banking Code of Practice which has been in effect since July 2019. Part Four includes requirements aimed at protecting vulnerable/disadvantaged customers (eg accessibility requirements, requirements for banks to inform low-income customers about low fee/no fee account options).

Details:

The BCCC says that the inquiry will have two aspects:

1. Compliance with Part Four requirements in the context of service delivery, product design, complaint handling/resolution and debt recovery; and
2. What processes/systems have been put in place to support Code compliance ie 'how banks have established 'cultural, system and training frameworks to support staff to comply with the Code'.

The BCCC says that ensuring compliance with Part Four of the Code is a key priority under its business plan and follows up on the BCCC's earlier inquiry into banks' transition to the 2019 Code..

Feedback

The BCCC invites feedback from individuals and small business customers (and their representatives) on their experiences, any areas of concern as well any examples of good practice.

[Source: BCCC media release 10/07/2020]

First enforcement action by a regulator against a financial institution for dealings with Jeffry Epstein: Deutsche Bank has agreed to pay $150m penalty

The New York State Department of Financial Services (DFS) has announced that Deutsche Bank has agreed to pay a penalty of $150 million as part of a consent order for 'significant compliance failures in connection with the bank's relationship with Jeffry Epstein and correspondent banking relationships with Danske Bank Estonia and FBME bank'.

Details

Broadly, the consent order identifies three issues.

3. Deutsche Bank did not adequately monitor the activity of 'high risk' customers, including Jeffrey Epstein (despite publicly available information concerning his criminal misconduct), and in consequence did not detect or prevent millions of dollars worth of suspicious transactions.
4. The DFS found there were 'procedural failures, mistakes, and sloppiness in how the Bank managed and oversaw the Epstein accounts'. One example of this, cited by the DFS is that conditions imposed on the Epstein accounts by the bank's reputational risk committee that may have detected/prevented many suspicious transactions: a) were not communicated to the majority of the account relationship team; and b) were 'misinterpreted by a compliance officer in a way that resulted in very little actual change in how the monitoring of the accounts occurred'. Overall, the DFS says that that 'very few problematic transactions were ever questioned' and when they were questioned, they were 'usually cleared without satisfactory explanation'.

5. The DFS found that Deutsche Bank failed to properly monitor the activities of their foreign bank clients (Danske Estonia and FBME), with respect to their correspondent and dollar clearing business.

The consent order outlines these issues in more detail.

According to the DFS, the settlement is the first enforcement action by a regulator against a financial institution for dealings with Jeffry Epstein.

[Source: New York State Department of Financial Services media release 07/07/2020]

Leadership change at ME Bank: CEO to step down at the end of July

ME Bank has announced that ME bank CEO Jamie McPhee has resigned effective from 31 July, after ten and a half years in the role.

The statement quotes Mr McPhee as saying

> 'In deciding to call time, I know the Bank is in a strong position financially and is well placed for the future, but that the industry challenges ahead and resulting need for change, will require a long-term commitment. After ten and a half years as CEO, I believe now is the best time to hand over the reins to give ownership of the Bank's post-COVID strategy development and long-term execution to a new CEO.'

ME Bank states that CFO Adam Crane will act as CEO until a new CEO is appointed.

Media reports (The Australian, The AFR, Investor Daily) have commented that Mr McPhee's departure follows questions from the House of Representatives Standing Committee on Economics into the bank's communication to customers around its decision to make changes to its mortgage redraw facility (the transcript of the hearing is here). This is not referenced in ME's statement.

[Source: ME Bank media release 14/07/2020]

In Brief | Westpac has announced that KPMG Partner Michael Rowland has been appointed as Westpac's CFO, subject to regulatory approval. Acting CFO Gary Thursby will continue acting in this role until Mr Rowland joins Westpac later in the year

[Source: Westpac media release 14/07/2020]

In Brief | Better than outsourcing as we know it? Academics have suggested that introducing a 'mentorship regime' to provide a 'reliable regulatory framework' for partnership agreements between fintechs and regulated banks would put outsourcing of banking services on firmer footing

[Source: Oxford Law School Blog 08/07/2020; Enriques, Luca and Ringe, Wolf-Georg, Bank-Fintech Partnerships, Outsourcing Arrangements and the Case for a Mentorship Regime (May 30, 2020). European Corporate Governance Institute - Law Working Paper No. 527/2020, Available at SSRN: https://ssrn.com/abstract=3625578 or http://dx.doi.org/10.2139/ssrn.3625578]

Accounting and Audit

Results of FRC audit inspections: 33% of firms still falling short

The UK Financial Reporting Council (FRC) has released the results it latest audit inspections at the seven largest audit firms. Overall, the FRC reviewed 88 audits conducted by these firms.

Some Key Findings

- The FRC set a target for the firms that at least 90% of FTSE 350 audits should be assessed as requiring no more than limited improvements by the end of the 2018/19 inspection cycle. Zero firms achieved this. Overall, 29 (33%) of the 88 audits reviewed in the 2019/20 inspection cycle required more than limited improvements. The FRC describes this result as 'unacceptable'
- The FRC found that though some improvement have been made, further work is needed including in the following three areas: 1) impairment of goodwill and intangibles; 2) revenue and contracts; and 3) provisions, including loan loss provisions. The FRC comments that over the past three years 46% of findings 'driving reviews requiring more than limited improvements' have been in these same three areas. The FRC flags that the findings in these areas often relate to 'insufficient challenge of, and standing up to, management in areas of complexity and forward looking judgement'.
- The FRC also made findings for more than one firm in the following areas: audit of inventory, group oversight, going concern and investment property valuations.
- The FRC says that in light of the results, it will: continue to measure firms' audit quality against the 90% FTSE 350 target and expect all firms to meet that target; and extend the 90% target to all other audits within the scope of our inspection.

[Sources: FRC media release 14/07/2020; Audit firm specific reports]

'Professionalising' the role of corproate director? Preventing future audit scandals will require looking not just at auditors but at boards says the IoD

Reflecting on the Financial Reporting Council's action, in the wake of recent audit scandals, to require the big four firms to ringfence their audit practices, (see: Governance News 08/07/2020) UK Institute of Directors Head of Corporate Governance Roger Barker suggests that though a good first step, more is required to prevent the recurrence of similar scandals going forward.

More particularly, Mr Barker argues that consistent with the approach taken by Sir Donald Brydon in his review of the sector, the focus needs to broaden beyond auditors to encompass corporate governance more generally, and directors in particular.

Mr Barker argues that one of the recommendations of the Brydon Review – the creation a new corporate auditing profession – has real value in this context, and suggests that the idea could be extended to corporate directorships.

> 'Brydon's argument that corporate auditing should be established as a distinct profession is equally applicable to corporate directorship. Both audit and directorship are crucial areas of governance in need of a professional framework which goes beyond a legal baseline and encompasses conduct, ethics and relevant training' Mr Barker states.

From a practical perspective, this would involve, the introduction of a Code of Conduct and professional development/education requirements for corporate directors (including the adoption of professional qualifications such as Chartered Director).

A second area where the Brydon recommendations have applicability for directors, Mr Barker argues, is the need to focus not deliver short-term shareholder returns, but on stakeholder value. Mr Barker states.

> 'The Brydon report also emphasizes the importance of a greater orientation towards a wider group of stakeholders in the work of auditors. In particular, it recommends that 'the audit report should include a new section in which the auditor states whether the company's section 172 statement is based on observed reality...responding to the needs of stakeholders in this way is part of restoring trust in business'. A greater emphasis on stakeholders is also a pressing need for directors'.

In making this observation, Mr Barker acknowledges that during the pandemic, many companies have demonstrated a 'much stronger stakeholder orientation' than has been the case previously, but citing Boohoo as an example, he maintains that in a number of cases, companies are yet to do so.

[Source: IoD article 08/07/2020]

Ensuring international audit standards are responsive to the public interest: The Monitoring Group has released recommendations to strengthen the international standard setting system

Following consultation, the Monitoring Group – the Basel Committee on Banking Supervision, European Commission, Financial Stability Board, International Association of Insurance Supervisors, International Forum of Independent Audit Regulators, International Organization of Securities Commissions, and the World Bank Group - has released its recommendations to strengthen and improve the international audit related standard setting system.

Scope/application of the recommendations

The recommendations relate to the structure, role and responsibilities and funding goals of the: International Auditing and Assurance Standards Board (IAASB); International Ethics Standards Board for Accountants (IESBA); and Public Interest Oversight Board (PIOB).

Rationale for the changes

The changes are intended to deliver a number of benefits including:

- Increased focus on public interest in standard setting which is hoped to 'have a mitigating impact on the risk of audit failure in future'

- Increased transparency and accountability eg the IAASB and IESBA will be required demonstrate how effective a standard has been in meeting the objectives set for it by conducting post implementation reviews.
- The delivery of more timely and relevant standards

Primary objectives

The recommendations have three primary objectives:

- establishing an independent and inclusive, multi-stakeholder standard-setting structure
- reinforcing 'consideration of the public interest within the standard-setting process and throughout the full cycle of standards' development, including through appropriate independent oversight'
- fostering the development of timely, high quality standards that respond to an accelerating pace of change.

The recommended changes are also aimed at increasing transparency and accountability of the PIOB, IESBA and the IAASB.

Timeline: The Monitoring Group plans to have a transition plan in place over the next nine months with a view to full implementation of the recommendations within three years. During this time, the Monitoring Group does not expect there will be any impact on those using the standards.

[Sources: IOSCO media release 14/07/2020; International Audit and Ethics Standard-Setting System]

In Brief | A failure of corporate culture? Columbia academic Todd Baker has written a summary of what is known so far about the Wirecard scandal, which includes some reflections on its causes. One conclusion he draws is that the company's supervisory board appears to have failed in their oversight duties. 'Theirs [the supervisory board] is a failure of corporate culture and of independence and integrity – reflected in their blind loyalty to management despite mounting problems and their hostility to shoe who asked legitimate questions about the company's operations'

[Source: Columbia Blue Sky Blog 08/07/2020]

Risk Management

Climate Risk

Certified as 'carbon neutral': Telstra and separately Local Government Super have announced they have each been certified as carbon neutral by Climate Active

Telstra's announcement: Telstra has announced its operations have been certified as carbon neutral by Climate Active. The certification was achieved, Telstra says, through a combination of purchasing 2.3 million carbon offset credits and the implementation of energy efficiency initiatives (eg retiring old equipment).

Telstra comments that the company experienced difficulty in purchasing carbon offset credits from Australia based projects because there are so few and suggested that this is an issue that should be 'addressed'.

Telstra says that it will continue to towards its target of 50% reduction in overall emissions by 2030 and that until this target is achieved, it will continue to buy carbon neutral credits to counteract its environmental impact.

The AFR quotes Telstra CEO Andy Penn as saying that certification is part of Telstra's commitment to being environmentally and socially responsible as well as profitable. Mr Penn is quoted as saying,

> 'If there was ever any lingering belief in the Friedman theory that the sole purpose of companies is to focus only on its shareholders, it has been finally put to rest. Community trust in the corporate sector had reached a new low point at the end of the last decade and yet in a short space of time more and more corporates are standing up on important issues. Companies are demonstrating they understand the expectations upon them and our responsibility to the communities in which we operate. Thoughtful companies realise they will only be successful for their shareholders if their customers, employees and communities enjoy success too'.

Local Government Super's announcement: Separately, Local Government Super (LGS) announced it has met the requirements for Climate Action certification as carbon neutral. The certification includes all LGS employees, the Sydney head office and the funds' regional offices.

LGS CEO Phil Stockwell said that the certification underlines the funds' 'long standing commitment to reducing emissions and contributing to a low carbon economy. It demonstrates to our members and the wider community that it is possible to effectively reduce emissions through targeted action'.

Government approved, Climate Active certification

- Carbon Active explains the requirements for a company to be certified as carbon neutral as follows. 'To become carbon neutral, businesses and organisations calculate the greenhouse gas emissions generated by their activity, such as fuel or electricity use and travel. They reduce these emissions as much as possible by investing in new technology or changing the way they operate. Any remaining emissions can be 'cancelled out' by purchasing carbon offsets. Carbon offset units are generated from activities that prevent, reduce or remove greenhouse gas emissions from being released into the atmosphere. When the offsets purchased by an organisation equal the emissions produced they are carbon neutral.'
- According to the Climate Active website there has been a 50% increase in the number of organisations receiving certificate over the past twelve months, with over 120 now certified.

[Sources: Telstra media release 09/07/2020; LGS media release 09/07/2020; [registration required] The AFR 09/07/2020]

First State Super divests fossil fuel investments

First State Super has announced that as part of its updated plan for mitigating the impact of climate related financial risks on members' savings and in the interests of supporting the transition to a low carbon economy, it has committed to a number of actions including:

- divesting investments in thermal coal: from October 2020, First State will commence divesting from businesses who derive 10% or more of their revenue from thermal coal mining
- reducing emissions in the fund's listed equities portfolio by 30% by 2023
- advocating an economy-wide 45% reduction in greenhouse gas emissions by 2030 and looking to 'replicate' it across the funds portfolio in the same timeframe
- undertaking an ongoing review of the fund's energy portfolio mix to 'mitigate the potential for stranded assets'
- setting fund-wide targets for investments in renewable energy and new technologies

Acting in the best long term interests of members

Announcing the new commitments First State CEO Deanne Stewart said that climate change is one of the most significant risks to members' retirement savings and that it is critical that superannuation funds act now to mitigate the long-term risks. 'It is essential that as a responsible owner super funds set strong, ambitious and transparent targets to deliver the kind of action we need no to prepare for a more prosperous and sustainable future' Ms Steward said.

Commenting specifically on the fund's decision to divest from thermal coal Ms Stewart said that it is an 'important first step but we recognise there is more to do, which is why we have committed to bold actions and real targets to shift the dial on climate change which will assist us to continue to deliver strong sustainable long term returns to our members.'

[Source: First State Super media release 09/07/2020]

UNSW report finds Australia is the world's largest exporter of fossil fuel emissions and therefore a major contributor to global climate change

A UNSW report – Australia – An Emissions Super Power – has found that Australia is the world's largest exporter of coal and gas, and therefore of fossil fuel emissions. As such, Australia is a 'major contributor' to global climate change.

The report argues that in light of this, and in light of the Federal government's position that Australia is not a major contributor to global warming, future international climate agreements should include:

- measures to constrain not only demand for fossil fuels, the supply of fossil fuels. For example, the report suggest that wealthy fossil fuel exporters, like Australia, should be required to sign a fossil fuel non-proliferation treaty as part of their emissions reduction commitments
- measures to rapidly phase out of domestic fossil fuel subsidies to make renewables more competitive
- measures to implement the 'fair phase out' of fossil fuels: The international energy agency (IEA) estimates that if climate targets are to be met, two thirds of known fossil fuel reserves must be left in the ground. Given that Australia is a wealthy nation and the fact that it has already substantially contributed to climate change, the report argues that Australia 'ought to make deeper and faster cuts to fossil fuel production than countries less able to bear the burden of climate transition'.

[Sources: Climate Justice media release 09/07/2020; Full text report: Australia – An Emissions Super Power]

In Brief | Study confirms that pricing carbon works to lower emissions: Analysis of data from 142 countries over more than two decades has concluded that countries with carbon prices on average have annual carbon emissions growth rates that are lower than countries without a carbon price

[Sources: The Conversation 14/07/2020; Study: Carbon pricing efficacy: Cross-country evidence]

Technology, Cybersecurity and Privacy

ClearView AI Inc's use of 'scraped data' and the biometrics of individuals is under investigation: Joint UK/Australian probe into Clearview AI Inc announced

- **Context:** Clearview AI Inc sells a facial recognition app that enables users to upload a photo of an individual and match it to photos of that person on Clearview AI's database of three billion images which have been 'scraped' from public internet sources eg social media platforms. Clearview markets the product to law enforcement agencies.
- **Joint investigation by UK and Australian privacy commissioners:** The Office of the Australian Information Commissioner (OAIC) and the UK's Information Commissioner's Office (ICO) have announced that they are jointly investigating Clearview AI's personal information handling practices 'focusing on the company's use of "scaped data" and biometrics of individuals'.
- **Canadian investigations:** The announcement follows separate announcements from the Office of the Privacy Commissioner of Canada, that it is conducting an investigation into the use of Clearview AI's app by the Royal Canadian Mounted Police (RCMP) and privacy commissioners of Canada, Quebec, British Columbia and Alberta are conducting a joint investigation into Clearview AI's use of personal information (allegedly) without consent.
- **Clearview it is no longer offering its services in Canada:** In response to the ongoing Canadian investigations, Clearview AI has informed the Office of the Privacy Commissioner of Canada that it is no longer offering its facial recognition services in Canada. The Canadian Privacy Commissioner says comments that 'this step includes the indefinite suspension of Clearview AI's contract with the RCMP, which was its last remaining client in Canada'.

[Sources: OAIC media release 09/07/2020; ICO media release 09/07/2020; Office of the Privacy Commissioner of Canada media releases 06/07/2020; 21/02/2020; 28/02/2020; Clearview AI website]

Investment Association warns investors about the risk of 'impersonation scams' after a sudden spike in scam activity

Spike in 'impersonation scams': The UK Investment Association (IA) has issued a statement cautioning retail investors about a spike in 'impersonation' scam activity ie where scammers clone a real product (eg investment bonds) and market it to investors, using fake documentation.

The IA attributes the sudden increase in reports to the fact that investors are only now becoming aware that they're victims of fraud because only after they contacted the genuine firms (to follow up on their expected quarterly interest payment) did they realise what had occurred.

The IA says that in the three months since the start of the COVID-19 lockdown, asset managers have reported 300 incidences. Losses to investors are estimated to be approximately £4 million.

The IA has called on investors to exercise caution: The IA says that investment managers are working with regulators and with law enforcement to address the issue and has called on their customers and the public to be aware of the risk and to exercise caution.

Director of Financial Crime Risk at Aviva Investors and Chair of the Investment Association Financial Crime Committee, Steve Hyndman advised investors be 'particularly on the lookout for the details of the contracts offered to them, and instances of cold calls. Contact from people claiming to be from investment firms should be verified with the genuine investment firm involved. In some instances the bank accounts used are not in the names of the purported investment management firm and do not match the pre-sale literature. Investors should also be vigilant if they are placed under time pressure to invest - a common feature of fraud'.

[Source: IA media release 13/07/2020]

In Brief | A major cyber incident could have more of an economic impact that COVID-19? AustCyber found that a four-week digital disruption resulting from a significant cyber incident could cost the economy AU$30 billion, the equivalent of around 1.5% of GDP

[Source: AustCyber media release 13/07/2020; Full text report: Australia's Digital Trust Report 2020; [registration required] The AFR 13/07/2020]

Other Developments

Brexit: IoD research finds less than a quarter of directors feel their organisation is fully prepared for the end of the Brexit transition period, the IoD has called for a phased approach to introducing changes

The UK Institute of Directors (IoD) has released the results of its survey into directors' attitudes to Brexit and the likely impact on their own organisations.

Among other things, the survey found that:

- less than a quarter (24%) of the 978 survey respondents felt that their organisation was 'fully prepared' for the end of the Brexit transition period
- 19% said that their organisation was 'somewhat prepared' (and that they intend to make further preparations)
- nearly a third (31%) said that they will make adjustments once final changes are clear
- 14% said that they are unable to focus on the issue because of the COVID-19 pandemic.

In light of this uncertainty and lack of preparedness, and the ongoing impact of the COVID-19 pandemic, Director General of the IoD Johnathan Geldart called for a staged approach to introducing changes. Mr Geldart said,

> 'A commitment to some form of reciprocal phasing-in of changes once clear is a long-standing ask from our members, and the benefits would be significant. At a time when government is rightly straining every sinew to help firms deal with widespread disruption, it would be counterproductive not to seek to minimise it at the end of the year. Unilateral actions like staggering import controls would be a welcome step from Government, but are by no means enough, we need to mitigate disruption across many different sectors on both sides. A phased implementation is in everyone's interests, and direct financial support for smaller firms would be a huge boost at a difficult time.'
>
> [Source: IoD media release 13/07/2020]

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