Governance News

COVID-19 Special Edition

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Contents

Diversity

On the road to extinction: There is only one remaining all-male ASX 200 board, down from 30 in 2015

Key Takeouts

- The latest Australian Institute of Company Directors (AICD) report tracking gender diversity on ASX 200 boards has identified that as at 1 August, there was only one remaining ASX 200 board with no female representation, down from 30 in 2015 when the target for 30% female board representation was set.
- The uptick in female board representation over the past five years has continued. As at 31 July, women accounted for 31.5% of ASX 200 board positions and 29.3% of ASX 300 board positions.
- Both the AICD and the 30% Club have cautioned against complacency noting that though the 30% target has been met overall, almost half of ASX 200 boards are yet to meet it.
- Both the AICD and the 30% Club have called on companies to work towards 40:40:20 (40% men; 40% women; and 20% open) representation on their boards going forward.

The Australian Institute of Company Directors (AICD) has released its latest report tracking the level of female board representation on ASX 200 boards: Gender Diversity Progress Report: May to July 2020.

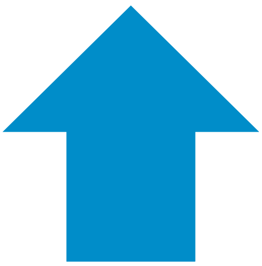
Some Key Takeaways

Trending upwards

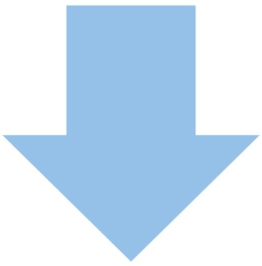
The overall level of female representation on ASX 200 boards has consistently risen since the 30% voluntary target was set in 2015.

At the end of 2019, the level of female representation on ASX 200 boards stood at 30.7%, as at 31 July the proportion was 31.3%.

Big end of town is leading the way on gender diversity



ASX 20: 5.1% above target
ASX 50: 3.5% above target
ASX 100: 2.5% above target
ASX 200: 1.3% above target



ASX 300: 0.7% below target

As at 31 July 2020 women accounted for:

- 35.1% of ASX 20 board positions
- 33.5% of ASX 50 board positions
- 32.5% of ASX 100 board positions
- 31.3% of ASX 200 board positions
- 29.3% of ASX 300 board positions

Going extinct?

The proportion of ASX 200 boards with no female representation has also fallen from 30 in 2015 to a single board (as at 1 August 2020). In contrast, according to Bloomberg the last remaining S&P 500 company with an all- male board added a female director last year.

Room to improve: As at 31 July, women accounted for only 18 ASX 200 board chair roles.

Work still to do?

Despite the fact that taken overall, the 30% female board representation target has been reached and indeed exceeded overall, almost half of all ASX 200 boards are still yet to reach it.

Likewise, more than half of companies include only one woman, or in one case, no women.

Both Chair of the 30% Club Nicola Wakefield and AICD CEO Angus Armour individually emphasised the importance of addressing these issues. Mr Armour observing that, the 'true value of diversity is recognised not through representation alone, but when that representation translates to contributions that are heard and valued'.

Both the AICD and the 30% called on companies to aim for 40:40:20 board representation (40% women, 40% men, and 20% open) to promote stronger decision making.

[Sources: AICD media release 19/08/2020; Gender Diversity Progress Report: May to July 2020]

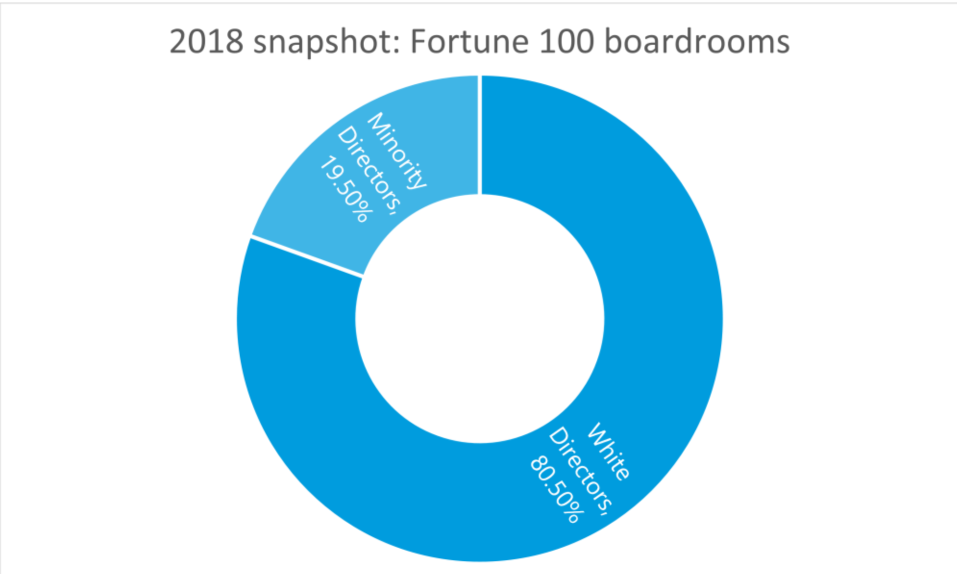
New quotas? Californian Bill proposes to impose new diversity quotas and to fine companies with all white boards

Under existing Californian law, publicly held domestic or foreign corporations whose principal executive office is located in California are required to meet minimum female board representation quotas, or risk fines for non-compliance.

Broadly, if passed AB-979 would impose an additional requirement on the same companies to meet minimum representation requirements for 'underrepresented communities' from the close of the 2021 calendar year. In addition, consistent with existing gender reporting requirements, the proposed law would authorise the secretary of state to impose fines for non-compliance, with the money from these fines to be used to offset the cost of administering the requirements.

Ethnic/Racial diversity in US boardrooms?

Though the ethnic/racial diversity of US boards is difficult to assess, given there is no requirement for boards to disclose the information, a study of the gender/ethnic composition of boards conducted by Deloitte and released in 2019 found that in 2018 Fortune 100 boards were overwhelmingly white and predominantly male. Overall, minority directors accounted for less than 20% of board seats. Minority men accounted for 13.7% of board seats and minority women accounted for 5.8%.



According to Bloomberg data, there are presently approximately 12 companies in the S&P 500 index with no Black board representation. Bloomberg suggests that there are signs that following the recent Black Lives Matter Protests of increased interest in appointing Black board representatives.

[Sources: AB-979 Corporations: boards of directors: underrepresented communities; Harvard Law School Forum on Corporate Governance and Financial Regulation 05/02/2019]

Remuneration

Top Story | Executive pay during COVID-19: Glass Lewis outlines its approach going into Australian meeting season

Key Takeouts

- With respect to bonuses for the last financial year, Glass Lewis states that its approach will be dependent on individual circumstances, including how heavily a company has been impacted by the pandemic.
- In addition to the extent to which COVID-19 has/has not impacted company performance, companies should consider 'employee welfare' and community expectations in the context of remuneration decisions. In addition 'pay for performance' should remain top of mind.
- Where a company's performance has remained strong on a 'relative and absolute basis' despite the pandemic Glass Lewis indicates that it will (likely) support payment of 'relatively generous' bonuses provided that the link between pay and performance is strong. That is, provided that the company's strong performance can be sheeted home to the efforts of executives and not to an unexpected windfall.

COVID-19 and executive pay heading into the Australian meeting season

Heading into the Australian, New Zealand and Indian meeting seasons, Glass Lewis has provided some insights into how it will approach payment of executive bonuses as well as its expectations around how boards should approach the task of setting short term incentives (STIs) for the next financial year.

Bonuses for the last financial year: Glass Lewis to take a 'pragmatic approach'

Glass Lewis states that ultimately the likelihood that it will support payment of bonuses will be dependent on individual circumstances, including how heavily companies have been impacted by the COVID-19 pandemic. However, other factors including employee welfare, community expectations and ensuring bonuses are justified on the basis of performance are also important in this context. On the issue of employee welfare Glass Lewis comments,

> 'Not only will this be considered an alignment of pay and company performance, this is also a matter of reputational management – boards and executives would do well to ensure they do not appear disconnected from their wider employee base during this difficult time, particularly in Australia where compulsory superannuation (pensions) means almost every employee in the economy is also a shareholder'.

COVID-19 and bonuses: Glass Lewis' likely approach based on four different scenarios

SITUATION	(LIKELIHOOD) OF SUPPORT FOR THE PAYMENT OF BONUSES?	ADDITIONAL COMMENTS
Companies most impacted by COVID-19: Situations in which a company has been 'devasted' by the pandemic and the company's prospects are on 'life support'	No: Glass Lewis expects that 'nil or nominal bonus payments should be made in respect of performance of the last financial year'.	▪ A possible alternative? Glass Lewis suggests that companies in this position could consider 'forward looking retention arrangements' as a means of both retaining management and incentivising them to turnaround the company's prospects. However, where boards elect to do so, they should also: a) ensure that the arrangements are clearly differentiated from backward looking performance bonus outcomes; b) ensure the intention behind putting the arrangements in place is clearly communicated; and c) communicate to investors how the arrangement is justified in the circumstances ie 'justify the arrangements relative to the realistic employment prospects of executives in a badly impacted industry'.

SITUATION	(LIKELIHOOD) OF SUPPORT FOR THE PAYMENT OF BONUSES?	ADDITIONAL COMMENTS
		▪ **Possible reputational damage:** Glass Lewis also suggests boards should consider the reputational damage that could arise if the arrangements put in place later deliver 'windfall gains' to executives as a result of improved operating conditions that lie outside of executive control'.
Companies moderately (negatively) impacted	**Probably not:** Glass Lewis expects 'very limited STI [short term incentive] bonus payments, if any, for executives in this category'.	▪ **A 'low appetite' for bonuses in this context:** 'The concept of pay-for-performance –with poor shareholder returns in mind – will be front and centre to our considerations of remuneration proposals…We have a low appetite for STI bonuses in this scenario. Sizeable STI awards will need to be accompanied by strong justification to overcome the misalignment with pay-for-performance to avoid an against recommendation from Glass Lewis and shareholder protest votes'.
Performance has been 'modestly and negatively impacted, and the company has outperformed the market on a relative basis'.	Probably (where the outcome is reasonable).	▪ **Well designed remuneration structures:** Glass Lewis comments that 'well designed remuneration structures should lead to reasonable outcomes without significant board discretion'. ▪ **Rewarding 'outperformance':** However, Glass Lewis also makes clear that where bonuses are paid, there should be no 'upward adjustments', 'we do not expect any upward adjustments to pay for relative outperformance. Any upward adjustments in any of the described scenarios in this note will need to be properly justified as they will be scrutinised at the company's shareholder meeting'.
Performance has remained strong on a 'relative and absolute basis'	▪ Yes (for defensive companies): Glass Lewis will support payment of 'relatively generous' bonuses where the company's performance can be sheeted home to the efforts of executives and not to an unexpected windfall. Glass Lewis comments, ▪ Probably yes for other strong performers (though companies are should exercise restraint):	▪ **Defensive companies:** Glass Lewis comments, 'Defensive companies that remain resilient throughout the COVID-19 crisis can expect Glass Lewis to support relatively generous bonus outcomes where the remuneration structure had been set up to pay counter-cyclically. We intend to support fit-for-purpose remuneration structures throughout the cycle and believe that failure to do so throughout this challenging time will undermine the credibility of any nonbullish remuneration structure'. ▪ **Other strong performers:** Where very strong performance is due to the current circumstances, rather than to executive performance, Glass Lewis considers that companies should exercise restraint when awarding bonuses – 'bonuses may be pulled back from stretch or maximum levels' Glass Lewis suggests. ▪ **Community expectations:** Glass Lewis also considers that strong performers especially, should factor in community expectations. Glass Lewis states, 'These companies are likely to face significant scrutiny, including in the media, as such outcomes risk topping the rankings of executive pay for the year. In these cases, downward discretion should to be considered if pay does not meet community or shareholder expectations'.

Target setting for executive bonuses for the next financial year?

Acknowledging the difficulty of forecasting in the present environment, Glass Lewis states that it will be 'supportive' of actions taken by boards to adjust remuneration to meet current challenges. For example, boards may change existing remuneration structures to account for a range of different COVID-19 scenarios; or opt to reduce the variability of pay 'with a corresponding reduction in quantum'.

Where vesting of long term incentives become certain as a result of these adjustments, Glass Lewis expects boards to consider reducing them by 50%.

Glass Lewis also emphasises that should changes be made to remuneration structures, clear communication will be critical – boards 'will need to excel at justifying and communicating such changes' Glass Lewis states.

[Source: Glass Lewis blog 05/08/2020]

COVID-19: Have US companies gone far enough in adjusting executive pay? Cuts to executive pay announced in response to the COVID-19 pandemic have largely been cuts to base salary, the smallest component of CEO pay according to CGLytics

CGLytics has released the results of analysis of adjustments to executive pay made in response to the COVID-19 pandemic by US companies. The analysis is based on 554 Russell 3000 companies that had made pay adjustments to Executives and their Board as at 31 May 2020.

Some Interesting Points

- Most companies applied reductions beyond the CEO: 57% of sample companies adjusted compensation for both executives and the board. Relatively few companies (7%) adjusted compensation for only the CEO.
- Lack of specificity about the extent of the cuts:
  - Of companies that announced cuts to CEO pay, 17% did not specify the amount of the reduction.
  - Of the companies that adjusted compensation beyond the CEO, 27% did not disclose the specifics of the pay reduction for named executive officers and 40% did not disclose the specifics of pay adjustments for the board.
- The most common form of pay adjustment was reducing base salary and board fees rather than to long-term incentive compensation or annual cash bonuses.
- Strength of base salary reductions:
  - CEO base salary reductions: Almost half of companies that announced base salary reductions reduced their CEO's base salary by 50% or more. More than a quarter of these companies zeroed out their CEO's base salary. The median 'strength' of CEO base salary cuts for this group of companies CEO's is 40%.
  - Board of director fee reductions: 52% of companies in the sample reduced board fees by 50% or more and 32% of companies zeroed out cash fees for directors entirely. CGlytics comments that 50% of companies which imposed 100% reduction in CEO base salary also did the same to Board of Directors' fee. The median cash fee reduction for boards was 35%.
- Other measures: Of the companies that opted for other measures eg deferral of base salary or payment of a proportion of salary in restricted stock units (RSUs) more than half opted to pay their CEOs and named executive officers (NEOs) 50%-100% of their base salaries in RSUs. Where companies opted to defer part of CEO and NEOs salaries, the proportion was lower, ranging from 25%-50% of base salary.
- Pay Adjustments by Industry – hardest hit sectors had the biggest reductions:
  - Over half (52%) of companies in the 'Consumer Discretionary sector' (hospitality, restaurants, retail etc) made some form of compensation adjustments in response to the pandemic. Pay reductions at these companies also tended to be higher. For Consumer Discretionary companies, the median pay cut is 50% for CEO's, 20% for NEOs and 25% for Board Members.
  - 29% of companies in the industrial sector announced some form of compensation adjustment.
  - Though the Financial sector has the largest representation in the Russell 3000 (764 companies), only 5% of the companies made changes to Executive and/or Board compensation in response to the pandemic.
  - 15% of companies in the health care sector have announced some form of pay reductions.
  - Only 7% of the 107 Consumer Staples companies (household products, personal products) and 1% of the 76 Utilities companies made pay adjustments.

Are the reductions enough?

CGyltics queries whether the salary reductions for executives are sufficient given they represent 'only a fraction of the often enormous compensation packages granted to CEO's and other Executives'. CGyltics comments,

> 'Even though 80% of the Russell 3000 companies have disclosed 2019 compensation for Executives, we have not witnessed any companies making adjustments to these figures in light of the crisis, even for companies in hard-hit industries…Furthermore, activist investors have begun to feel unhappy about some executive pay actions amid the pandemic'.

Likewise, concerns have been raised that some executives may actually receive a windfall when conditions improve.

> 'the practice of issuers deferring executive salary cuts into RSUs will give rise to huge payouts in the future when the market eventually recovers and share value increases. This means that Executives who deferred their base salary have made a sacrifice that ultimately will benefit them, defeating the purpose of pay cuts' CGYltics comments.

[Note: In the UK context, The High Pay Centre and CIPD's latest annual review of executive pay raises similar questions around whether executive pay cuts in response to the pandemic are sufficient. Our summary of the report is here.]

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 21/08/2020]

Rethinking remuneration for customer-facing staff: Westpac axes variable short term incentive pay

Westpac Group has announced that it will replace the existing short term variable incentive scheme for 4000+ branch and customer care staff at Westpac, St.George, Bank of Melbourne, and BankSA with a new fixed pay increase.

Announcing the change in approach Westpac Acting Chief Executive Consumer, Richard Burton said that the removal of variable incentives will: 1) give employees more certainty around their remuneration; 2) reward them for 'the individual service they provide to customers'; and c) 'give our customers confidence that the service they receive is wholly focused on their banking needs'.

The new remuneration arrangement will come into effect from 1 October 2020 to coincide with the Group's new performance year.

[Source: Westpac media release 19/08/2020]

There is something you can do if you are 'offended' by very high CEO remuneration: tell your fund, says Professor Elizabeth Sheedy

In a comment piece reflecting on the findings of Australian Council of Superannuation Investors (ACSI's) latest report into CEO pay (the full text of the report is here, our summary is here) Professor Elizabeth Sheedy writes that there are 'promising signs' that ACSI's engagement efforts are having an effect in driving more accountability. For example, boards appear more willing than previously to exercise discretion on bonuses.

However, Professor Sheedy argues that superannuation funds could and should be more active on the issue. For example, Professor Sheedy suggests that superannuation funds could: a) push to ensure bonus shares don't vest until two years after the CEO's departure; and/or b) push to ensure executive pay is conditional (ie can be clawed back if the executive is later found to have 'acted badly').

Professor Sheedy concludes by calling on superannuation members to also be more active on the issue: 'If you're offended by chief executive pay there are things you do. One of the first is to contact your super fund and tell them you're concerned' Professor Sheedy states.

[Source: The Conversation 21/08/2020]

Disclosure and Reporting

What Australian and New Zealand investors want to see: IGCC report identifies the improvements investors would like to see companies make to their climate risk reporting

The Investor Group on Climate Change (IGCC) has released a report – Full Disclosure: Improving Corporate Disclosure on Climate Risk – outlining how Australian and New Zealand investors use company reports on climate risk and the improvements that they would like to see companies make to align their climate risk reporting with investor needs/expectations.

In a statement announcing the release of the report, Principal, Policy and Strategy at Energetics, Olivia Kember said that the study underscores the value investors place on climate disclosure and its relevance in the context of investment decision making. Ms Kember states,

> 'investors are already using climate disclosures, not just to engage with companies on their climate change responses, but also to inform their own integration of climate risk in investment decisions. Judging by the speed of evolution in climate risk analysis, this is only going to increase. A company that can show a clear pathway from its understanding of climate risk to its strategy and performance presents an increasingly valuable investment proposition'.

How investors are using the climate disclosure information

The report highlights two key ways in which investors are using climate information.

- To inform engagement with companies: The report found that most investors (84%) use climate disclosures as a basis for engagement with companies. 72% of investors indicated that they use climate disclosures in the context of their direct engagement with companies. Examples of the topics for engagement include (among others): a) clarifying executive accountability for climate risk management and more particularly linking executive responsibility to remuneration metrics; b) seeking detail around risk mitigation actions; and c) various aspects of scenario analysis including in some cases pushing for 'higher decarbonisation ambition'. The report also found that 68% of investors use climate disclosure to inform their voting decisions. The report comments that engagement efforts are likely to both continue and to become more targeted as familiarity with the TCFD framework increases, analytics develop and financial regulators clarify expectations/requirements.
- As part of ESG integration: The report also found that most investors (76%) are using climate risk disclosure as part of ESG integration ie as part of the 'explicit and systematic inclusion of ESG issues in investment analysis and investment decisions'. According to the report, investors are increasingly using disclosures 'as an input to investment assessments' of companies to help gauge the level of risk exposure.

What institutional investors would like to see improved

Broadly, the report identifies six ways that investors consider TCFD disclosure could be improved.

1. 'Demonstrate board, director and executive level skills and expertise in climate change
2. Report links between climate-related performance and executive remuneration
3. Demonstrate links between risks and opportunities identified and the company's strategic and organisational response
4. Extend reporting of emissions metrics and targets to scope 3 emissions, where material
5. Report on both transition and physical risks, costs and implications
6. Provide auditing and assurance of results'.

Further detail: Improving TCFD disclosure

The report provides commentary and insights into investor perceptions of the current approach to TCFD reporting as well as insights into the changes they would like to see to improve it.

The table below provides a high level overview of the aspects of climate disclosure that are most valued by investors/the areas investors would like to see companies prioritise in their climate disclosure, and some of the changes that investors would like to see made.

TCFD PILLAR	INVESTOR REPORTING PRIORITIES	INVESTOR VIEWS ON THE CURRENT APPROACH AND HOW IT CAN BE IMPROVED
Governance	▪ Investors regard board and executive expertise and responsibility as the most important aspect of governance disclosure (76% of investors indicating it was 'very important' and 24% indicating it is 'important'). ▪ Likewise, the link between executive remuneration and climate targets disclosure/performance was regarded as a key aspect of disclosure (52%). ▪ Disclosure of trade association memberships was ranked as the least important aspect of governance disclosure with 36% of investors rating it as 'very important' and 56%	▪ According to the report, investors feel that companies have made progress on clarifying accountability structures/processes and are increasingly focused now on board and executive expertise. ▪ Increasingly, investors want to see more detailed disclosure around whether committees/boards/individuals have the expertise to provide sufficient oversight. ▪ Investors also want companies to more clearly report the links between climate-related performance and executive remuneration.
Strategy	▪ Investors regard all elements of strategy as important but ultimately gave equal highest priority (76% indicating it is very important) to companies 'having a strategy and investment plan to meet ambitions and targets' or a 'low carbon transition plan'. ▪ Investors also ranked scenario analysis on transition risk (68%) and scenario analysis on physical risk (64%) as high on their list of priorities. ▪ Lowest on the investors' list of priorities was information on the financial impact under analysed scenarios (with only 44% of investors indicating it is 'very important').	▪ Overall, the report found that investors are looking for evidence that climate change has been 'appropriately embedded into strategic decision making'. For example, investors would like to see disclosure include a 'credible plan' to achieve targets as well as information around how short-term and medium term objectives align with longer term ambitions. ▪ In addition to information about the management of the risks, investors are also interested in the opportunities presented by the shift to a low carbon economy. Scenario analysis: Broadly, investors consider that scenario analysis could be improved in four key ways. 1. 'Apply credible scenarios drawn from commonly referenced sources to promote standardisation and disclose the core input assumptions (e.g. technology costs, demand factors carbon price, national emission reduction target assumptions and

TCFD PILLAR	INVESTOR REPORTING PRIORITIES	INVESTOR VIEWS ON THE CURRENT APPROACH AND HOW IT CAN BE IMPROVED
		scope of portfolio analysis applied to for example) 2. If applying a bespoke scenario analysis model disclose the input assumptions and variance to the standard set of assumptions (e.g. avoid black box disclosures) 3. Report scenario analysis impacts at both the company-wide and project/asset levels, and increase balance and credibility by reporting negative impacts 4. Report on the impact on company strategy and actions taken as a result of the scenario analysis, as well as the outputs of the analysis'.
Metrics and Targets	▪ Investors gave the highest priority to disclosure of the carbon footprint of a company and/or its key products (72% rated this as very important). ▪ Disclosure of ambitions and targets (eg net zero targets) and targets covering Scope 2 and 2 emissions was also ranked among investors' top priorities (with 68% of investors rating it as very important) ▪ Targets for scope 3 emissions ranked as the lowest priority with only 32% of investors ranking it as very important. The report suggests that this reflects the view that scope 3 targets are very important only to some industries or companies.	▪ The report identifies that the key metrics investors use for purposes of comparison are: emissions and emissions intensity of key projects/products; past performance in achieving emissions reduction; and emissions reduction targets (preferably net zero targets). ▪ The report flags that investors' appetite for seeing reporting of emissions metrics and targets extended to include scope 3 emissions is high ('where material').

About the report: The report is based on a survey of 25 IGCC investor members conducted in mid-June 2020 and on a workshop with 50 investors to test the survey findings and their implications.

[Sources: Investor Group on Climate Change media release 20/08/2020; IGCC report: Full Disclosure: Improving corporate disclosure on climate risk]

The CFA Institute is developing new disclosure requirements for investment products to assist investors in evaluating their ESG credentials

The CFA Institute (CFA) is developing a new voluntary disclosure Standard for investment products with ESG-related features. The new Standard (once drafted) is primarily intended to enable asset managers to more clearly communicate the ESG-related features of their products 'so that investors can more comprehensively evaluate whether or not an investment product will meet their needs'.

The consultation paper sums up the purpose of the proposed Standard as follows:

> 'The Standard will establish fundamental requirements and disclosure requirements for investment products with ESG-related features, procedures for independent examination of disclosures, and a classification of

> ESG-related features by ESG-related needs. The fundamental requirements will address applicability of the Standard, recordkeeping, and distribution of ESG-related marketing materials. The disclosure requirements will provide investors with a way to more clearly understand and compare investment products based on a consistent set of information. The independent examination will provide a level of assurance that an investment product's disclosures meet the requirements and fairly describe the investment product. The classification of ESG-related features will provide investors with a way to more easily choose an investment product that aligns with their ESG-related needs'.

It's intended that the new standard will improve existing disclosure, rather than materially adding to it ie that it will 'fit within the landscape of existing and developing ESG-related regulations, standards, labels, and initiatives'.

A 'disclosure based approach'

The CFA emphasises that it is not proposing that the new Standard will set prescriptive requirements for corporate issuer ESG disclosures. In particular, the CFA states that the proposed new standard is not intended to: a) 'prescribe criteria for the design or implementation of investment products with ESG-related features'; b) 'provide a label or rating for investment products'; or c) 'apply to the issuers of securities or the information they provide to investors'.

Rather, it's proposed that the new standard will set disclosure requirements aimed at enabling asset managers to 'describe investment products with ESG-related features in a complete and clear way, so that investors can determine how well such investment products meet their ESG-related needs'.

The consultation paper argues that this disclosure based approach has a number of benefits: 1) it provides a 'common way to describe investment products that should not inherently conflict with regional regulations or prescriptive standards'; 2) it will provide asset managers with flexibility to 'port' their investment products to other markets; 3) it enables investors to better understand/compare products across markets; and 4) it provides flexibility and scope to adopt to both changes in investment needs and product innovations.

Next steps: The CFA plans to release an initial draft of the new requirements in May 2021.

[Sources: CFA media release 19/08/2020; Consultation paper]

Meetings and Proxy Advisers

Less information about company performance and less opportunity to hold leaders to account: The rapid shift to the virtual meeting format has been a negative one overall for shareholders according to a US study

A study into how the transition to virtual meetings in the US context as a result of pandemic restrictions has impacted shareholder's experience of meetings and their ability to participate has determined that the rapid shift to the virtual meeting format has in practice, been a negative one from a shareholder perspective.

For example the study found that

- Meetings were significantly shorter: The average length of shareholder meetings decreased an average of 18% (as compared with physical/hybrid meetings in 2019) with less time dedicated to providing business updates (average decrease of 40%) and on answering shareholder questions (decrease of 14%).
- The virtual meeting format made it more difficult for shareholders to hold leaders to account: For example, submitting questions was frequently not a straightforward process for shareholders due to convoluted technical requirements that would not exist in a physical meeting format. At the same time, the virtual format made it easier for firms to evade questions either by (falsely) claiming that there were no further questions to be answered (as occurred in 10% of the meetings sampled) or by announcing during the meeting, that only questions relating directly to proposals would be answered (as occurred in 18.3% of the meetings sampled).

Four ways to improve the shareholder virtual meeting experience

The author makes four suggestions as to how communication between companies and shareholders could be improved.

- mandate the publication of audio recordings and transcripts of meetings
- mandate the disclosure of the number of questions submitted and the number of shareholders who logged into the virtual meeting (to identify firms that have unusually small numbers of questions submitted)
- mandate the disclosure of all shareholder questions and require 'transparency on the question selection mechanism'
- either allow unidentified shareholders to submit questions or put systems in place to make it simpler for Broadridge's competitors to immediately identify shareholders.

[Note: In Australia, consideration is being given to modernising existing requirements to enable companies to hold electronic meetings. The Australian Institute of Company Directors and the Governance Institute have each called for temporary reforms to the Corporations Act 2001 (Cth) in Corporations (Coronavirus Economic Response) Determination (No 1) 2020 to be made permanent (see: Governance News 10/06/2020) as have other business groups (see: Governance News 24/06/2020). The government appears to be open to considering modernising Corporations Act requirements (see: Governance News 17/06/2020). Senate Select Committee on Financial Technology and Regulatory Technology Chair Andrew Bragg has said that he considers 'virtual AGMs, electronic signatures replacing "wet" signatures and letting people execute documents electronically are all no brainers' (see: Governance News 08/07/2020). The Australian Shareholder Association has however raised concerns about the prospect of making temporary changes enabling virtual meetings and electronic communication with shareholders, permanent unless appropriate safeguards are not put in place to protect shareholders (see: Governance News 19/08/2020).]

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 18/08/2020; Full text of the study is here: Schwartz-Ziv, Miriam, How Shifting from In-Person to Virtual Shareholder Meetings Affects Shareholders' Voice (August 16, 2020)]

Short and Long-termism

How to fix short-termism? The European Commission has released a report into the key drivers of 'short-termism' in corporate governance and suggested a range of potential options to address the issue

Key Takeouts

- The report identifies seven root causes or drivers of short termism among listed cmpanies within the EU including the current formulation/interpretation of directors' duties.
- The report states that any future EU intervention to tackle the root causes of short-termism should be underpinned by three objectives:
  - Strengthening the role of directors in pursuing their company's long-term interests by 'dispel[ling] current misconceptions and errors in relation to the purpose of the company and the duties of directors, which lead directors to prioritise short-term financial performance over the long-term interest of the company';
  - Strengthening director accountability: EU intervention should 'bring about a higher level of responsibility for sustainable value creation by making directors more accountable for the sustainability of their business conduct' and
  - Removing barriers to the integration of sustainability into company decision making for example in the area of corporate reporting, board remuneration, board composition, stakeholder involvement.
- The report suggests and provdies an assessment of the likely effectiveness of various measures. Among other things, the report suggests that a new EU directive providing an EU-wide formulation of directors' duties and company's interest should be considered.

The European Commission has released a report examining the 'root causes' or drivers of 'short termism' in corporate governance and putting forward potential EU level solutions to address them.

The problem: EU companies are focused on delivery of short term financial returns to shareholders

According to the report, data collective over the 1992-2018 period indicates that publicly listed companies within the EU are increasingly focused on delivery of short-term financial return to shareholders rather than on the long-term interests of the company. The report points to two trends in support of this. The steady decrease in capital expenditure and R&D investments coupled with the steady uptick in shareholder payouts over the period. According to the report to shareholder pay-outs have increased from less than 1% of revenue in 1992 to almost 4% in 2018.

Why the EU should intervene to address it

The report argues that EU policy intervention is both justified and is necessary to 'lengthen the time horizon in corporate decision-making and promote a corporate governance that is more conducive to sustainability' on the basis that:

- the continued failure of companies to act in their own long-term interests has potential negative impacts outside the companies and could 'amount to overwhelming environmental, social and economic consequences for companies, shareholders, investors, and society at large';
- if things continue as they are, the achievement of the goals of the Paris Agreement on climate change and the UN SDGs 'is unlikely'; and
- 'only EU action can ensure a level playing field for European companies'.

The trend towards short-termism is being driven by seven root causes

The report identifies seven key drivers or 'root causes' of the issue. They are:

1. 'Directors' duties and company's interest are interpreted narrowly and tend to favour the short-term maximisation of shareholder value

2. Growing pressures from investors with a short-term horizon contribute to increasing the boards' focus on short-term financial returns to shareholders at the expense of long-term value creation
3. Companies lack a strategic perspective over sustainability and current practices fail to effectively identify and manage relevant sustainability risks and impacts
4. Board remuneration structures incentivise the focus on short-term shareholder value rather than long-term value creation for the company
5. The current board composition does not fully support a shift towards sustainability
6. Current corporate governance frameworks and practices do not sufficiently voice the long-term interests of stakeholders
7. Enforcement of the directors' duty to act in the long-term interest of company is limited'.

How to fix it? Possible actions to tackle the root causes of short-termism

The report states that broadly, any future EU intervention should be underpinned by the following objectives:

- Strengthening the role of directors in pursuing their company's long-term interests by 'dispel[ling] current misconceptions and errors in relation to the purpose of the company and the duties of directors, which lead directors to prioritise short-term financial performance over the long-term interest of the company'; and
- Strengthening director accountability: EU intervention should 'bring about a higher level of responsibility for sustainable value creation by making directors more accountable for the sustainability of their business conduct' and
- Removing barriers to the integration of sustainability into company decision making for example in the area of corporate reporting, board remuneration, board composition, stakeholder involvement.

The Commission's preferred options to address the seven drivers of short-termism

The report includes a list of potential options to address each of the seven root causes identified escalating from non-legislative/soft measures (eg awareness raising) to legislative/hard measures (EU legislative intervention). The report also provides an assessment of the likely effectiveness of the suggested options. The table on p vii of the report summarises the potential options.

Below is a high level overview of the Commission's preferred options to strengthen directors' duties; strengthen enforcement and to realign executive remuneration frameworks.

Strengthening director duties: The report suggests that a new EU directive providing an EU-wide formulation of directors' duties and company's interest should be considered

The report suggests that the most effective way to strengthen director duties would be for the European Commission to issue a directive 'providing an EU-wide formulation of directors' duties and company's interest'. The proposed new directive would require directors to:

- 'properly balance' the interests of 'employees; interest of customers; interest of local and global environment; interest of society at large' in addition to the interests of shareholders when acting in the long-term interests of the company (beyond 5-10 years)
- 'identify and mitigate sustainability risks and impacts, both internal and external, connected to the company's business operations and value chain'.

The report argues that 'an EU intervention in the area of director's duties, at the core of corporate governance, would have a remarkable impact in improving sustainability. An EU-wide formulation of directors' duties and company interest would impact all ESG dimensions positively'. Having said this the report concedes that this option 'could create some difficulties for companies to adapt to the new concepts and review their governance in the short term'.

Integrating sustainability considerations into company decision making: new rules should be considered

The Commission's considers that the most effective approach to ensure boards build sustainability considerations into their decision making is for the Commission to propose a new EU directive requiring them to do so. The directive would require boards to:

- integrate sustainability aspects (risks, opportunities, impacts) into business strategy;
- identify and set as part of the business strategy 'measurable, specific, time-bound, and science-based sustainability targets aligned with overarching goals (such as the SDGs and the goals of the Paris Agreement on climate change)'; and
- to disclose 'appropriate information'.

This report states that this option would also increase director accountability for implementing long-term and sustainable business strategy. The Commission comments that this option has the support of 'most NGOs and trade unions' and that the effectiveness of the measure is acknowledged by not only trade unions and NGOs but by companies.

Strengthening enforcement of directors' duties: again new rules should be considered

The Commission considers that either issuing a recommendation for EU member states to consider measures to strengthen enforcement of directors' duty to act in the interests of the company in their respective national frameworks, or in the alternative for the Commission to propose binding rules to strengthen the enforcement of directors' duty to do so are likely to be the most effective options in terms of increasing director accountability.

These options would also provide an enforcement mechanism to ensure accountability for complying with the proposals outlined above.

Incentivising boards to make decisions in the long term interests of the company: a range of responses should be considered

The report puts forward a range of options to align board remuneration with long-term value creation all of which are considered, by the Commission to be likely to be valuable/effective in driving positive change.

These options include:

1. Launching a Commission led and funded campaign encouraging companies to tie board remuneration to long-term, sustainable value creation for the company
2. Issuing a recommendation for EU states to introduce in their respective national frameworks new provisions: a) restricting executives' ability to sell shares they receive as pay; and b) making the inclusion of non-financial ESG metrics linked to company sustainability targets compulsory in executive pay schemes.
3. Taking option two a step further by proposing to amend the Shareholder Rights Directive II to: a) 'regulate' executives' ability to sell shares received as pay; and b) make the inclusion of non-financial ESG metrics mandatory in executive pay schemes.

The report comments that in particular, proposing to amend the Shareholder Rights Directive II 'would have a positive impact on the society, the environment, and the economy, as executives would be incentivised to focus on sustainability' but that at the same time every option put forward will increase compliance costs for companies to some extent. .

[Source: European Commission Report: Study on directors' duties and sustainable corporate governance 29/07/2020]

Non-shareholder Stakeholders

COVID-19: Are they walking the talk? Just Capital finds signatories to the Business Roundtable's Statement on corporate purpose have responded 'comparatively well' to the challenges of COVID-19, but are still falling far short of community expectations

Key Takeouts

- A year on from the Business Roundtable's revised statement (BRT statement) on corporate purpose, (the full text of the statement is here. Our summary is here.) Just Capital has released the results of a study into both the extent to which BRT signatories lived up to community expectations around how companies should respond to the challenges of COVID-19 and the now BRT companies' response differed from that of Russell 1000 companies in general.
- Overall, the conclusion is that BRT companies have responded 'comparatively well' to the crisis, outperforming their peer organisations in terms of how well they measure up to community expectations. Having said this, BRT companies' response still falls short of what the community expects.
- Separately, Just Capital released the results of analysis into the extent to which BRT signatories' commitments to tackling racial inequality live up to community expectations. Overall, the conclusion is that 'there remains a significant gap between what the American people want companies, including BRT signatories, to prioritize and what companies are actually doing on these issues'.

Context

In August 2019, the Business Roundtable issued a revised statement (BRT statement) on the purpose of the corporation, as part of its work to ensure more 'inclusive prosperity'. The statement commits the 180+ signatory companies to not only serve their own 'corporate purpose' but to commit to delivering benefits to all stakeholders (customers, employees, suppliers, communities and shareholders). As such, the New York Times characterised it at the time as 'an explicit rebuke of the notion that the role of the corporation is to maximize profits at all costs — the philosophy that has held sway on Wall Street and in the boardroom for 50 years'. The full text of the statement is here. Our summary is here.

Has it made any difference to the way companies have responded to COVID-19? BRT statement signatories vs Russell 1000 companies

Just Capital has released the results of its comparative analysis into the way in which Russell 1000 companies and BRT statement companies have responded to the COVID-19 pandemic. The analysis is focused on six key aspects of the corporate response: 1) response to disruption of usual dependent care arrangements; 2) provision of free personal protective equipment (PPE) to frontline workers; 3) provision of paid sick leave; 4) provision of financial assistance to frontline workers (eg hazard pay); 5) the extent to which companies changed policies to accommodate customers impacted by the pandemic (customer accommodations); and 6) financial donations to support COVID-19 community relief efforts.

The purpose of the study was to 'better understand how the companies pushing for stakeholder capitalism are actually serving their stakeholders this year'.

The headline finding is that BRT signatories 'significantly outperform their peers on all six issues' but nevertheless do not measure up to community expectations around how companies should respond on any issue.

Comparison: BRT signatories' response vs peer organsiations

The table below provides a brief overview of the key findings to emerge from Just Capital's analysis.

ISSUE	BRT SIGNATORY RESPONSE	RUSSELL 1000 COMPANY RESPONSE	EXTENT TO WHICH BOTH GROUPS FALL SHORT
Response to disruption to usual care arrangements for dependents – provision of additional support	22% of BRT signatories disclosed they provided some form of support to enable workers to undertake care of dependents during the pandemic in light of the disruption to usual care arrangements (eg closure of schools/childcare centres)	7% of other companies disclosed that they provided any form of support.	Though BRT companies are three times more likely than their peers to disclose measures to support workers on this issue, the report concludes that 'the overwhelming majority of companies' have failed to provide any form of support 'most likely leaving working parents in the US without a solution to the ongoing disruptions to their typical care arrangements' as a result of the pandemic.
Provision of free personal protective equipment (PPE) to frontline workers	40% of BRT signatories disclosed that they are providing frontline workers with free PPE (eg gloves/masks)	22% of Russell 1000 companies disclosed that they are providing free PPE to frontline workers	Though BRT companies are almost twice as likely as non-signatory companies to disclose that they are providing free PPE to frontline workers this falls well short of community expectations. 90% of the community want companies to prioritise the health of frontline workers by providing free PPE.
Paid sick leave for workers	36% of BRT signatories have announced expanded or new sick leave policies (including paid sick leave)	18% of Russell 1000 companies disclosed that they have revised/put into place new sick leave policies.	Though BRT companies are twice as likely as their peers to disclose changes to sick leave in response to the pandemic, the proportion of companies offering paid sick leave falls well short of community expectations. 74% of the community expects companies to offer 14 days of paid sick leave, and most (70%) want this to continue into 2021.
Financial assistance to frontline workers	29% of BRT signatories disclosed that they are providing some form of financial assistance (eg grants, bonuses, wage increases, additional incentive pay) to frontline workers.	16% of Russell 1000 companies disclosed that they are providing some form of financial assistance to frontline workers.	Though BRT signatories are almost twice as likely than their peers to provide some form of financial assistance this still falls well short of community expectations. 77% of the community want companies to provide 'hazard pay' to frontline workers, yet not only is the proportion of companies providing additional financial assistance well short of this, some BRT signatory companies have actually allowed their hazard pay policies to expire during the pandemic.

ISSUE	BRT SIGNATORY RESPONSE	RUSSELL 1000 COMPANY RESPONSE	EXTENT TO WHICH BOTH GROUPS FALL SHORT
Customer accommodations (measures to support customers impacted by COVID-19)	54% of BRT signatories disclosed that they provided some form of customer accommodations.	45% provided some form of customer accommodation.	Though BRT signatories were more likely than other organisations to provide some form of customer accommodation, the proportion falls well short of community expectations. 74% of the community expects companies to offer some form of 'customer accommodation'.
Cash donations to support community relief efforts	71% signatories disclosed financial donations to support community relief efforts	42% of Russell 1000 companies disclosed financial donations to support community relief efforts.	The proportion of BRT companies who disclosed financial donations is significantly higher than peer organisations. However, this again falls well short of community expectations. 90% of the community expects companies to provide financial donations to support COVID-19 community relief efforts.

[Source: Just Capital Report: How Business Roundtable Companies Have Responded to Six Critical Stakeholder Issues During the COVID-19 Pandemic]

Racial equality: How do BRT signatories measure up to community expectations

Just Capital's analysis of the extent to which BRT signatories' publicly disclosed commitments align with community expectations

On 5 June 2020, the BRT announced the creation of a Special Committee to advance racial equity in four areas: education, health, finance and criminal justice.

Just Capital conducted a review into how BRT signatories' commitments in four areas: a) conducting a pay equity analysis: b) disclosing workforce demographic data; c) funding local education programs; and d) instituting a diverse supplier policy align with community expectations

Overall, Just Capital concluded that 'there remains a significant gap between what the American people want companies, including BRT signatories, to prioritize and what companies are actually doing on these issues'. Despite the fact that a majority of BRT signatories lead the way on transparency around their actions on these issues, more than transparency is required.

Some Key Findings

- Conducting pay equity or wage gap analysis: Though 75% of respondents overall, and 81% of Black respondents, believe that companies should conduct wage gap analysis (by race, ethnicity, and gender) in order to identify and address any discrepancies, only 51% of BRT signatories disclose that they have done so.
- Disclosing workplace demographic data: Though 62% of respondents overall, and 77% of Black respondents consider it important that companies should publicly disclose the ethnic/racial makeup of their workforce 38% of BRT signatories do not disclose any information on the issue and only 25% disclose general data on the proportion of employees who identify as a non-White minority.
- Funding of local educational initiatives: Though 74% of respondents overall and 88% of Black respondents consider it to be important that companies fund local education and create apprenticeship and scholarship programs to support more diverse hiring, 27% of BRT signatories have not disclosed they do so.

- **Supplier diversity:** 71% of all respondents, and 89% of Black respondents considered it to be important that companies increase business with Black-owned suppliers. To date, 19% of BRT signatories are yet to disclose their supplier diversity policy.

  [Source: Just Capital Report: Roundtable Companies Have Responded to Four Critical Issues Advancing Racial Equity in the Workplace]

Open letter calls on the Business Roundtable to commit to concrete steps to implement its commitment to stakeholders

A year on from the release of the Business Roundtable's (BRT) revised statement of Corporate purpose, Oren Cass (Executive Director American Compass), Sarah Miller (Executive Director American Economic Liberties Project) and Terry Schilling (Executive Director American Principles Project) have released an open letter calling on the BRT to take concrete steps to implement their commitment to stakeholders.

> 'We and our organizations were intrigued by the vision of corporate actual responsibility that this statement seemed to contemplate, but we have also noticed the lack of concrete follow on action. As the chief executives who signed the BRT statement would surely attest, a serious strategic commitment is not something merely announced. It requires a timeline, milestones, resources, and—most importantly—tangible targets and ongoing measurement. No such steps appear to have been taken' they write.

Suggested actions

The letter calls on the BRT to consider implementing the following three actions to push signatories to look beyond short term profitability and the interests of shareholders.

- **Get more specific:** 'Declaring everyone a stakeholder and everything a priority is a sure fire recipe for avoiding meaningful action or accountability' the letter states. Instead, the writers call on the BRT to 'establish clear priorities' based on the corporations stated role, which is to 'promote an economy that serves all Americans'. The writers suggest this could include commitments to: a) creating good jobs for workers; b) maintaining a workplace compatible with family life; c) 'providing the economic foundation and supporting the public institutions vital for strong communities', and d) 'advancing the long-term prosperity of the nation'.
- **Measure and publicly disclose progress against commitments:** The letter calls on the BRT to 'establish and report standardized metrics that would allow the public to evaluate the performance of their firms' against their commitments. The letter includes suggested metrics for measuring performance. For example, suggested metrics to measure progress towards 'advancing the long term prosperity of the nation' include: a) the ratio of capital expenditure to shareholder distribution; b) the ratio of domestic to foreign operating expenditures; and c) the ratio of political and lobbying expenditures to tax payments.
- **Support legislative reforms that would 'require all of them to behave as they believe they should'.** The writers argue that the BRT has since its inception opposed tighter regulation of firms and that this approach is contrary to the BRT's commitment to redefining the purpose of a corporation. They argue that 'if BRT were serious about its obligations to stakeholders other than shareholders, it could for example lead a push for nationwide action to restrict anticompetitive practices like non-compete and no-poach agreements, afford workers representation on corporate boards, and prevent abuse of the H-1B visa system. BRT members could likewise pledge to invest in rebuilding public institutions capable of combatting corruption'.

The letter concludes with the observation that in the absence of action it is 'difficult to avoid the conclusion that executives of large corporations are incapable of acting as even they say they should, without being compelled by significant public policy changes', and calls on the BRT to provide an update on the actions taken to date and its planned next steps.

[Source: Open Letter: The Business Roundtable's Commitment to Corporate Actual Responsibility 12/08/2020]

Financial Services

Top Story | Expert insights into the challenges facing the managed accounts industry

MinterEllison Partners Richard Batten and Andrew Bradley discussed some of the key regulatory challenges facing the managed accounts industry with Head of Managed Accounts at Macquarie Group, Eylem Kamerakkas. The discussion touched, among other things, on upcoming design and distribution obligations as well as changes in the regulator's policy settings.

You can access a recording of the discussion here.

FFNS bill tops $1.05 billion: ASIC has issued an update on compensation paid by financial institutions

The Australian Securities and Investments Commission (ASIC) has issued an update on amount of compensation paid by Australia's largest banking and financial services institutions for 'financial advice related misconduct'.

- As at 30 June 2020, six of Australia's largest banking and financial services institutions have paid/offered a total of $1.05bn in compensation to customers for fee for no service (FFNS) conduct or 'non-compliant' financial advice.
- During the period 1 January to 30 June 2020, financial institutions paid a further $295.9m in compensation payments/offers of compensation.

[Source: ASIC media release 24/08/2020]

Hayne FFNS case studies: ASIC commences proceedings

The Australian Securities and Investments Commission (ASIC) has commenced civil penalty proceedings in the Federal Court against State Super Financial Services Australia Limited (StatePlus), Asgard Capital Management Ltd (Asgard) and BT Funds Management Limited (BT) in connection with (alleged) fee for no service (FFNS) issues which were each the subject of case studies considered by the Hayne Royal Commission.

ASIC comments that it has now commenced a total of four enforcement actions concerning (alleged) FFNS activity.

Details

ASIC's case against StatePlus

Broadly ASIC alleges that between 1 April 2013 and 30 June 2018 StatePlus:

- did not provide promised financial advice (in the form of annual financial planning reviews through StatePlus financial planners) to 36,592 members;
- 'issued defective disclosure documents or statements that included promises to provide annual financial advice to members in circumstances that StatePlus did not have reasonable grounds for believing it could provide'; and
- did not have appropriate systems, controls and processes in place to 'ensure that, as far as reasonably practicable, it provided or would be able to provide Annual Review Services to all Advice Clients'.

ASIC alleges that by failing to have in place systems/controls 'adequate to prevent the FFNS conduct' StatePlus 'breached its obligation to do all things necessary to ensure that the financial services covered by its AFSL were provided efficiently, honestly and fairly' (as required under ss912A(1)(a),(b) and (c) of the Corporations Act).

ASIC also alleges that between 21 August 2014 and 30 June 2018 the acceptance of monthly payments for financial advice services amounted to a contravention of s12DI(3) of the ASIC Act (accepting payment without being able to supply as ordered).

The originating process sets out ASIC's allegations in further detail. The concise statement provides details of the relief being sought.

Response to the proceedings

In a brief statement acknowledging the proceedings, First State said,

> 'While the period under review largely pre-dates our ownership of StatePlus, as the new owner we have recognised the issue, promptly rectified it and ensured all affected clients were refunded. We have also put in process improvements to ensure that this issue does not happen again. From the time we acquired the business we have strived to do the right thing by our advice clients, and we remain committed to the importance of financial advice. Our recent experience through the COVID-19 pandemic has demonstrated that having access to the right advice at the right time meant that clients had greater peace of mind'.

The statement makes no reference to whether the proceedings will be defended.

ASIC's case against BT Funds Management and Asgard

Broadly ASIC alleges that:

- Between September 2014 and August 2017, Asgard incorrectly charged 404 customers a total of $130,006 in financial advice fees for services that were not provided. ASIC also alleges that Asgard did not have in place effective processes, systems and controls to ensure adviser fees were not charged to customers who had requested that their financial adviser was removed and that Asgard retained fees to which it was not entitled until December 2017.
- ASIC alleges that both Asgard and BT Funds Management Limited (BT) made misleading representations in customer communications regarding the charging of the adviser fees.

ASIC argues that BT Funds Management and Asgard each:

- made a false or misleading representation in contravention of s 12DB(1)(g) of the ASIC Act
- engaged in misleading or deceptive conduct or conduct that was likely to mislead or deceive, in contravention of s 12DA(1) of the ASIC Act and s 1041H of the Corporations Act.

ASIC also alleges that Asgard 'breached its obligation to do all things necessary to ensure the financial services covered by its financial services license, being the custodial services provided in respect of each Affected Product, were provided efficiently, honestly and fairly, and thereby contravened s 912A(1)(a) of the Corporations Act'.

The originating process and concise statement provide further detail on ASIC's allegations and the relief being sought.

Westpac's response to the allegations

In a short statement acknowledging the proceedings, Westpac confirmed that BT Funds Management Limited (BTFM) and Asgard Capital Management Limited (ACML) 'accept the allegations made and do not intend to defend the proceedings. BTFM and ACML will make submissions on the appropriate penalty in due course. BTFM and ACML apologise that these errors occurred and will work with ASIC to resolve the proceedings as quickly as possible'.

[Sources: ASIC media releases 20/08/2020; 20/08/2020; Westpac media release 20/08/2020; First State Super media release 20/08/2020]

Failure to have adequate cybersecurity arrangements in place: ASIC commences civil penalty proceedings

The Australian Securities and Investments Commission (ASIC) has commenced civil penalty proceedings in the Federal Court against Australian Financial Services (AFS) licence holder, RI Advice Group Pty Ltd (RI), for (alleged) failure to have in place 'adequate' cybersecurity systems.

Broadly, ASIC alleges that:

- 'RI failed to have implemented (including by its ARs [ie authorised representatives]) adequate policies, systems and resources which were reasonably appropriate to manage risk in respect of cybersecurity and cyber resilience'.
- Following cyber incidents, RI did not 'properly review the effectiveness of, and remediate where necessary in a timely manner, its cybersecurity controls (including those of its authorised representatives)'.

ASIC alleges that RI's failure to have adequate cybersecurity systems in place, and to ensure that effective controls were in place, amounted to failing to do all things necessary to ensure that the financial services covered by its licence were provided efficiently, honestly and fairly (in contravention of s912A(1)(a) of the Corporations Act). ASIC also alleges that RI's conduct contravened sections 912A(1)(b), (c),(d),(h) and (5A) of the Act.

ASIC is seeking civil penalties and compliance orders requiring that RI implement 'systems that are reasonably appropriate to adequately manage risk in respect of cybersecurity and cyber resilience and provide a report from a suitably qualified independent expert confirming that such systems have been implemented'.

The concise statement and originating process provide further detail around ASIC's allegations and the relief being sought.

[Sources: ASIC media release 21/08/2020]

FSRC financial advice case study: Update on ASIC's enforcement action against a financial adviser

Background

Financial advice firm Henderson Maxwell Pty Ltd and Sam Henderson (the responsible manager, director and CEO Henderson Maxwell) were the subjects of a financial advice case study considered by the Financial Services Royal Commission. Mr Henderson announced his retirement from the financial planning industry in June 2018 and is listed as 'Ceased' on the Financial Advisers Register. In July 2019, following an 'ASIC surveillance', ASIC banned Mr Henderson from providing financial services for a period of three years.

Proceedings against Mr Henderson

On 25 August, ASIC announced that Mr Henderson pleaded guilty to one 'rolled up' offence under s1041G of the Corporations Act 2001 (Cth) (engaging in dishonest conduct in relation to a financial product or financial service) and two counts of making a disclosure document available to a person knowing it to be defective (in breach of s952D(2)(a)(ii) of the Corporations Act) by giving two clients a Financial Services Guide, containing the false representation that he held a Master of Commerce (Financial Planning).

A dishonest conduct offence under s1041G of the Corporations Act 2001 (Cth) carries a maximum penalty in the local court of two years' imprisonment or a fine not exceeding 120 penalty units, or both.

A defective disclosure offence under s952D(2)(a)(ii) Corporations Act carries a maximum of 12 months' imprisonment or a fine not exceeding 60 penalty units, or both.

[Note: Section 4AA of the Crime Act 1914 (Cth) states that one penalty unit is $210. Though the penalty unit amount was recently increased to $222 (effective 1 July 2020), the new penalty unit value will only apply to offences committed on or after 1 July 2020.]

The sentencing hearing is set for 13 October 2020.

[Source: ASIC media release 25/08/2020]

How can regulators be blamed for red-tape? In his opening address to the regtech responsible lending demonstration, ASIC Commissioner Sean Hughes said that investing in technology holds the key to better stakeholder outcomes, not reduction in 'red tape'

Key Takeouts

- ASIC Commissioner Sean Hughes said that regtech has potential to deliver a range of benefits including in the context of responsible lending. For example, technology can shorten time taken to approve a loan from 64 days to 58 minutes.
- A question of investment: How can regulators be blamed for red tape? Mr Hughes observed that 'it is remarkable to think that regulators are often blamed for red tape blockages, when in fact the capability to harness and tap into technology to accelerate positive customer outcomes lies within entities, if they choose to invest in and develop it'.

In his opening address to the ASIC Regtech Responsible Lending Demonstration, Australian Securities and Investments Commission (ASIC) Commissioner Sean Hughes emphasised the valuable role technology can play in delivering benefits to stakeholders, including in the context of responsible lending.

Some Key Points

- ASIC's approach to regtech: Mr Hughes said that ASIC's approach to regtech has always been governed by three principles: 1) ensuring regtech outcomes are in alignment with ASIC's strategic priorities to protect consumers and ensure economic stability; 2) working to 'better understand innovation without advocating or endorsing any one solution, technology, or business model; and 3) ongoing learning through engagement 'through industry inputs, good domestic and international case studies, as well as our own experiences from engaging with the regtech sector'.
- COVID-19 has heightened expectations of lenders: Mr Hughes said that technology could streamline compliance, making it both more efficient and more customer centric, as well as enhancing consumers' digital interactions with their lenders. Mr Hughes said that the pandemic has served to accelerate the pace at which change is expected to occur and underlined the importance of improving performance across the lending industry, including in the context of responsible lending.
- The role of regtech in supporting lenders in meeting responsible lending obligations: Mr Hughes said that ASIC's recently revised responsible lending guidance (RG 209 Credit licensing: responsible lending conduct) included updates to 'better reflect and anticipate technological developments' in light of the capacity for technology to support compliance and to deliver stronger outcomes for stakeholders. As part of the consultation ASIC conducted prior to the release of the guidance, Mr Hughes said that he was 'impressed' by how existing technology solutions are 'rapidly transforming the sector' and gave a number of examples of how technology could enhance and streamline processes. Mr Hughes said that one entity had integrated 'responsible practices into the design of their user experience' from inception', with the result that 'scaling was easier to manage; processes and procedures were easier to replicate; and any need for adaptation or change manifested themselves as adjustments, rather than root and branch system overhauls'. In another exmple, Mr Hughes said that aggregation tools could substantially decrease (by 89-90%) the time taken to analyse consumer household expenditure as compared with manual processes which in term enabled much faster decisions on granting loans. Use of technology in this example he said enabled the lender to approve customer loans within 58 minutes as compared with 64 days for 'traditional institutions to approve similar loans'.
- Open banking should provide a 'springboard' for regtechs: Mr Hughes said that technology has an important role to play in the context of realising the many benefits – improved comparability of services, improved transparency, improved accessibility, stronger competition, more streamlined and efficient processes - of open banking. Mr Hughes said that ASIC hopes that open banking 'provide a springboard for regtechs in bringing their ideas to life'.
- How can regulators be blamed for red tape? Mr Hughes observed that 'it is remarkable to think that regulators are often blamed for red tape blockages, when in fact the capability to harness and tap into technology to accelerate positive customer outcomes lies within entities, if they choose to invest in and develop it'.

[Source: Opening address by Sean Hughes, ASIC Commissioner, at the ASIC Regtech Responsible Lending Demonstration Webinar 20/08/2020]

COVID-19: So far funds have paid out $31.1bn under the government's early release of superannuation scheme, the data indicates that the number of applications coming through continues to slow

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 16 August.

- Total payments made since the inception of the scheme have taken an average of 3.3 business days to process, with 95% of payments made within five business days.
- The volume of applications received is declining: Over the week to 16 August, superannuation funds received 70,000 applications, down from 88,000 applications received in the week to 9 August.
- Of the applications received in the week to 16 August, 33 000 were repeat applications bringing the total number of repeat applications received to date to 1.2 million since inception of the scheme.
- 40 000 were initial applications bringing the total number of initial applications to 3.1 million since inception of the scheme.
- Over the week to 16 August, superannuation funds made payments to 80,000 members worth $0.6 billion (down from $0.71 billion in the week to 9 August).
- Funds have made approximately 4.1 million payments since the inception of the scheme worth a total of $31.7 billion. This figure represents 97% of applications received since inception of the scheme.

[Source: APRA media release 24/08/2020]

Updated MySuper Heatmap to be released December 2020

The Australian Prudential Regulation Authority (APRA) has published updated frequently asked questions on the MySuper Product Heatmap.

Some key points to note:

- APRA will release updates to all components of the MySuper Heatmap - investment performance, fees and costs and sustainability - in December 2020.
- The updated investment performance and sustainability of member outcomes metrics will be based on data as at 30 June 2020. The fees and costs data will be based on product disclosure statements as at 1 October 2020.
- APRA says that the 2020 heatmap data will be 'locked down' after 5pm on 29 October 2020. This means that any data submitted after that date will be included in the 2021 MySuper Product Heatmap, planned for release in December 2021.

[Source: APRA media release 21/08/2020]

Choice of Super Bill passes both Houses with amendments

Having passed the House on 12 February, Treasury Laws Amendment (Your Superannuation, Your Choice) Bill 2019 finally passed both houses on 25 August (having been amended in the senate).

Amendments

- The super choice of fund regime will apply to employees covered by workplace determinations and enterprise agreements made on or after 1 January 2021 (rather than 1 July 2020).
- That the Australian Prudential Regulation Authority (APRA) conduct a review into the operation of the reforms within 30 months of their commencement to identify any unintended consequences, including the ongoing viability and profitability of defined benefits schemes.

[The full text of the schedule of amendments is here.]

In a joint statement announcing the passage of the legislation through the senate, Treasurer Josh Frydenberg and Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume said that the legislation (once passed) will enable approximately 800,000 workers of 40% of all employees covered by a current enterprise agreement the freedom to select their own superannuation fund.

[Sources: Treasury Laws Amendment (Your Superannuation, Your Choice) Bill 2019; Schedule of amendments; Joint statement, Treasurer Josh Frydenberg and Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume 25/08/2020]

In Brief | Shrinking asset pool: APRA's quarterly superannuation statistics show that over the 12 months to June 2020 there was a 0.6% decrease in the value of total superannuation assets. Quarterly benefit payments were $37.4 billion, up from $21.1 billion in the March 2020 quarter due to payments made under the Early Release of Superannuation Scheme.

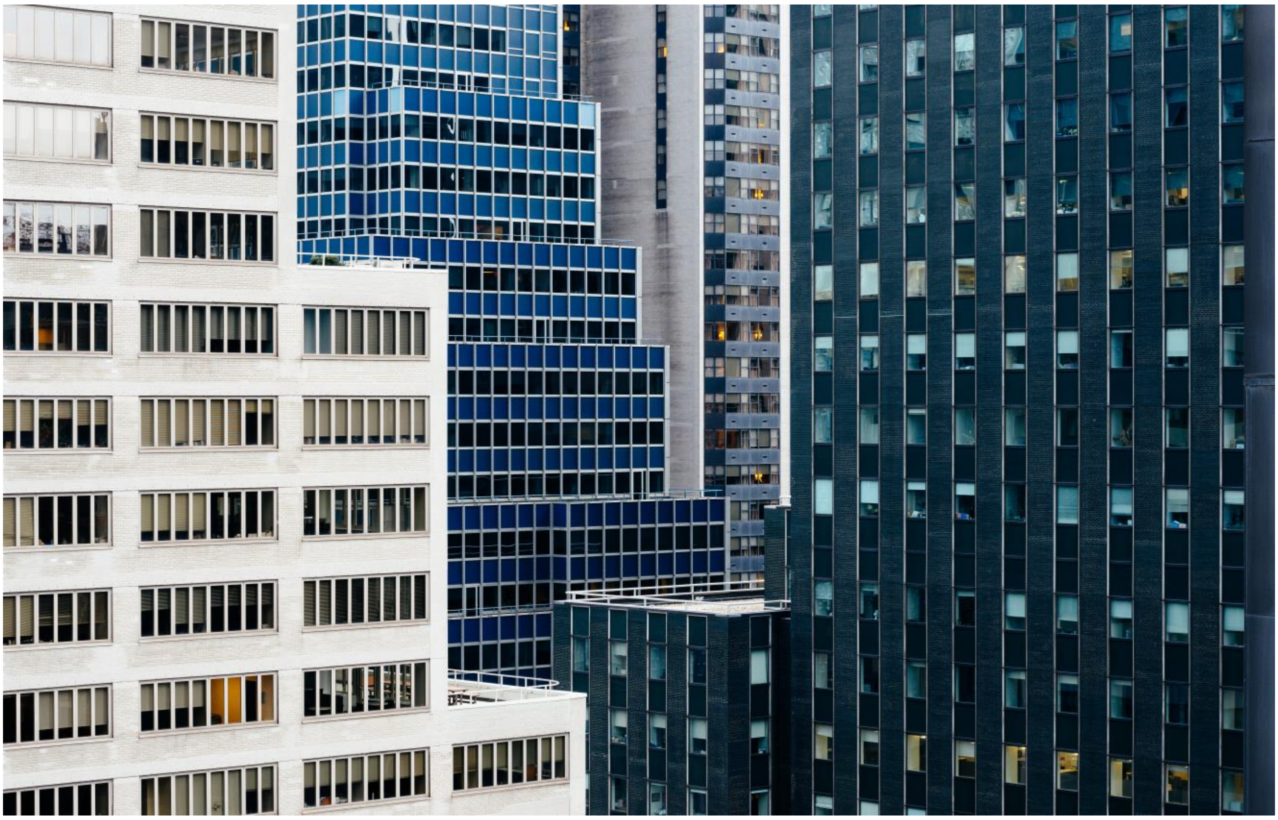
[Source: APRA media release 25/08/2020]

In Brief | ASIC has released guidance (Information Sheet 248 Enhanced regulatory sandbox) to assist financial businesses to test their products and services under the government's enhanced regulatory sandbox scheduled to commence on 1 September 2020

[Source: ASIC media release 25/08/2020]

In Brief | ANZ announced that it is the first bank to issue a Sustainable Development Goal Bond in in Australia's domestic bond market. The bond is ANZ's third issuance under its SDG Bond Framework which has been in place since February 2018

[Source: ANZ media release 20/08/2020]



Risk Management__

Norway's largest asset manager commits to using its 'significant influence' to help 'accelerate decarbonisation in the global economy'

Key Takeouts

- Norway's larges asset manager Storebrand has released a new climate strategy which 'entails a strengthened focus on active ownership, not only vis-à-vis fossil energy producers, but also vis-à-vis large consumers of energy, such as industrial companies with large emissions'.
- The new strategy commits Storeband to exerting its 'significant influence' to accelerate the pace of global emissions reductions
- One consequence of tighter investment requirements is the exclusion of 27 companies, including Exxon Mobil, Chevron, Basf, Rio Tinto and Southern Company from Storebrand's portfolio.

Storebrand has released a new climate strategy which broadly, outlines how Storebrand will contribute to accelerating the pace of reductions in global emissions.

Long-term focus

Announcing the new strategy Storebrand states that,

> 'As one of the Nordic region's largest asset managers, we are concerned about the effect of climate change on ecosystems, societies and economies, and thus our own portfolio companies. Fortunately, we also have significant influence, and can help accelerate decarbonisation in the global economy. Storebrand has worked with sustainable investments for 25 years, and with our new climate strategy we are stepping up our work and taking it two steps further. These measures are necessary to secure customers' investments for the future'.

New climate strategy

Commitments under the strategy include (among other things) commitments to:

- **make investment decisions in line with scientific consensus** (based on United Nations Intergovernmental Panel on Climate Change data) and in line with the goals of the Paris Agreement. Storebrand will have a net zero in greenhouse gas emissions from its investment portfolios by 2050 'at the latest'.
- **exclude companies** from its portfolio that:
  - 'actively lobby against the Paris Agreement and climate regulations'; or
  - generate revenue of more than 5% from coal and sands.
  - one consequence of this strategy is that 27 companies have been excluded from Storebrand's portfolio including Exxon Mobil, Chevron, Basf, Rio Tinto and Southern Company. The statement announcing the new climate strategy includes a full list of the companies that have been excluded and the reason for their exclusion. The statement is here.
- **exert its 'significant influence'** through 'active ownership and dialogue' directly with companies to:
  - push oil and gas companies and high-emission industries' to adopt more ambitious transition targets and improve climate practices
  - engage with companies involved in deforestation (directly or through their supply chain)
- **increase investment in companies that can contribution to 'solutions to the climate crisis'**
- **further develop climate risk analyses** of the portfolios and report annually.

[Source: Storebrand media release 24/08/2020; Climate Strategy]

Suncorp has announced plans to phase out direct investment in, and underwriting/financing of oil and gas projects, Market Forces has welcomed the announcement

Market Forces has welcomed the release of Suncorp's updated Fossil Fuels Sensitive Sector Guideline (in Suncorp's Responsible Business Report) which commits it to:

> 'cease underwriting, financing or directly investing in new oil and gas projects, phase out underwriting and financing oil and gas by 2025, and directly investing by 2040. This builds on our commitment to phase out of existing thermal coal by 2025'.

Market Forces campaigner Pablo Brait said that the commitment is a step in the right direction that puts Suncorp ahead of other insurers, but suggests that it could go further.

> 'While this new guideline has significant gaps, that is, it doesn't address oil and gas pipelines nor gas-fired power stations, it is a great step forward for Suncorp which puts it ahead of many other insurance companies worldwide. Suncorp has recognised that an expansion in oil and gas production will undermine the Paris Agreement on climate change and worsen the floods, bushfires, droughts and storms which are hitting its profits. With this new policy Suncorp has sent a clear message to its customers, shareholders and the Federal Government, that it will not be a part of any expansion of dirty gas production'.
>
> [Sources: Suncorp FY 20 Responsible Business Report 21/08/2020; Market Forces media release 21/08/2020]

Rio Tinto has released the board's review of cultural heritage management

Rio Tinto has released the board review of cultural heritage management following the destruction of the Juukan Gorge rock shelters. The full text of the report is here.

Broadly, the review found that:

> 'no single individual or error was responsible for the destruction of the Juukan rock shelters, but there were numerous missed opportunities over almost a decade and the company failed to uphold one of Rio Tinto's core values – respect for local communities and for their heritage'.

Executive pay consequences

The company announced that in light of the review findings, performance related bonuses under the Short Term Incentive Plan would be reduced to zero for CEO JS Jacques, CEO of Iron Ore Chris Salisbury and Group Executive, Corporate Relations Simone Niven.

In addition, the Chief Executive Officer's 2016 Long-Term Incentive Plan (LTIP) award that is due to vest in the first half of 2021 will be reduced by £1,000,000 (subject to vesting).

The report states that each of Rio's non-executive directors have agreed to donate the equivalent of 10% of their 2020 non-executive director fees to the Clontarf Foundation, which supports education, training and employment for Indigenous Australians. Rio Tinto CFO and executive director Jakob Stausholm, will also make an equivalent donation.

Pay reductions for non-executives 'where appropriate'

The report states that variable pay arrangements for individuals below the executive committee will also be reviewed and, reduced 'where appropriate'.

[Source: Rio Tinto media release 24/08/2020; Rio Tinto board review]

The Basel Committee is consulting on proposed new principles for operational resilience and separately on changes to its existing principles for the sound management of operational risk

Proposed new principles for operational resilience

The Basel Committee is consulting on proposed new principles for operational resilience 'that aim to mitigate the impact of potentially severe adverse events by enhancing banks' ability to withstand, adapt to and recover from them'.

The proposed new principles focus on: 'governance; operational risk management; business continuity planning and testing; mapping interconnections and interdependencies; third-party dependency management; incident management; and resilient cyber security and ICT' (information and communication technologies).

Among other things, the Committee is seeking feedback on how banks' operational resilience should be measured and specifically, the kinds of metrics already in use by organisations to measure it.

The Committee observes that:

> 'measuring a bank's operational resilience is in a nascent stage and further work is required to develop a reliable set of metrics that both banks and supervisors can use to assess whether resilience expectations are being met.'

Updates to existing principles for the sound management of operational risk

The Committee is also consulting on proposed updates to its existing principles for the sound management of operational risk (PSMOR) which were last updated in 2011 Following the 2014 implementation review, the Committee is proposing a limited number of updates to: a) align them with the recently finalised Basel III operational risk framework; b) update the guidance on change management and information and communication technologies (ICT) as needed; and d) 'enhance the overall clarity of the principles document'.

Separate but concurrent consultations

The Committee explains that the consultations are being undertaken concurrently but separately in light of the 'natural relationship' between operational resilience and operational risk.

> 'The proposed principles for operational resilience…not only build upon the proposed updates to the PSMOR, they are largely derived and adapted from existing guidance on outsourcing, business continuity and risk management-related guidance issued by the Committee or national supervisors over a number of years. By building upon existing guidance and current practices, the Committee is seeking to develop a coherent framework and avoid duplication'.

Timeline

The deadline for submissions is 6 November 2020

[Sources: Basel Committee media release 06/08/2020; Principles for operational resilience; Principles for the sound management of operational risk]

In Brief | Link between WFH and increased cyber risk? The level of cybercrime has 'vastly increased' since COVID-19 hit, primarily as a result of the rapid shift in work practices according to Deloitte. Deloitte nominates staff education as a key step in protecting against the risk

[Source: Gateway Network Governance Body Cyber Roundtable 12/08/2020]

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