Governance News

COVID-19 Special Edition

11 November 2020

Contents

Boards and Directors

Trends in board composition and governance on FTSE 150 boards: Key takeaways from the annual Spencer Stuart Board Index

Key Takeouts

- The annual Spencer Stuart Board Index tracks trends in board governance practices, director workload and board at FTSE 150 companies.
- Among other things, the latest index found that:
  - the appointment of a designated non-executive director to the board is the most popular approach to meeting the Governance Code recommendation around workforce engagement. So far zero boards have opted to appoint a worker director.
  - Chairs are taking on fewer outside commitments than has been the case in the past, primarily due to the increased workload/demands of the role. The number of senior executives sitting on outside boards has also dropped:
  - most boards comply with the UK Corporate Governance Code recommendation that they conduct an annual board evaluation and use an external facilitator at least one every three years.
  - efforts to increase board diversity (especially gender diversity) are having an impact with women now accounting for 34% of FTSE 150 director roles overall. Progress towards increased racial diversity on boards is slower.

The latest annual Spencer Stuart Board Index tracks trends in board governance practices, director workload and board at FTSE 150 companies.

Some interseting findings

Workforce engagement

The 2018 Corporate Governance Code recommends that, in line with directors' obligations under s172 of the Companies Act 2006 (UK), boards should engage with their workforce using one or more of the following methods: 1) appointing a worker director; 2) establishing a formal workforce advisory panel; and/or 3) appointing a designated non-executive director.

Where boards opt not to use one or more of these methods, the Code enjoins them to explain what alternative arrangements are in place and why the board considers them to be effective.

The report found that:

- 56% of companies have adopted one of the three options in the Code to increase workforce engagement with the most popular approach being the appointment of a designated non-executive director to the board. This was the approach taken by 49% of companies.
- Interestingly, not a single board has appointed a worker director and 36% of boards have elected to rely on existing methods of engagement.

Director workload

Number of scheduled meetings

- The number of scheduled meetings varied within a fairly wide range: between four and sixteen.
- The average number of (scheduled) board meetings has slightly decreased from an average of eight meetings in 2010 to an average of 7.7 meetings in 2020. The number of scheduled meetings ranged fairly widely four to 16 meetings.
- 31 companies disclosed holding additional ad-hoc meetings.
- 86.5% of companies reported their meeting attendance rate at 95% or higher.

Committees

The proportion of boards with more than three committees has increased from 43% in 2010 to 55% in 2020.

Overboarding

The report found the Chairs are taking on fewer outside commitments than has been the case in the past, primarily due to the increased workload/demands of the role. For example:

- The number of Chairs with no other listed company directorships has increased from 17% in 2008 to 39% now.
- There has been a steep drop in the number of Chairs who Chair more than one FTSE 350 Board over the past two years. In 2019, 60% of Chairs led more than one FTSE 350 board, in 2020 this had dropped to 28%.

The number of senior executives sitting on outside boards has also dropped:

- The proportion of CEOs with an outside directorship is now 30% (down from 41% in 2010)
- The proportion of CFOs sitting on an outside board has fallen from 41% in 2010 to 28% in 2020.

Board evaluation

Most boards comply with the UK Corporate Governance Code recommendation that they conduct an annual board evaluation and use an external facilitator at least one every three years.

In 2020:

- 52% of boards undertook an internal evaluation process and 46% of companies conducted an externally facilitated review.
- Only 2% on boards did not undertake any form of evaluation.

Board Composition

The proportion of independent vs executive directors and the size of boards has remained more or less stable over the last ten years.

- The average size of FTSE 150 boards has remained constant over the past 10 years at around ten members
- The proportion of boards that include independent directors is unchanged at 94%
- The number of boards with a full time chair has barely shifted at 7% (up from 6% in 2010).
- The number of boards with a combined CEO/Chair is now nil (down from only 1% in 2010)

Age

Directors are getting (slightly) older::

- The average age of non-executive directors in 2010 was 59 years. It is now 60.3 years
- The average age of executive directors in 2020 is 54.1 years (up from 51 in 2010)

Tenure

Non-executive directors serve an average of 4.3 years on a board (down from 5.6 years in 2010).

Board Diversity

Boards overall remain predominantly white and male, but efforts to increase board diversity (especially gender diversity) are having an impact with women now accounting for 34% of FTSE 150 director roles overall. Progress towards increased racial diversity on boards is slower.

Gender diversity

- The report found that FTSE 150 boards are becoming more gender diverse with the number of female directors now standing at 34% overall (up from 12% in 2010).

- 100% of boards now include at least one female director and13% boards have achieved gender parity.
- For the second consecutive year, more women are being appointed to FTSE 150 boards than men: 51% of directors appointed to FTSE 150 boards this year are women.
- However, there are no more female CEOs now than in 2010 (women account for only 5% of CEO roles) and the number of female Chairs also stands at only 5%.

Racial Diversity

There has been less progress on increasing Black, Asian and minority ethnic (BAME) board representation:

- only 8% of serving directors have BAME backgrounds
- 17% of first time directors have BAME backgrounds

Foreign Directors

Overall, the proportion of foreign directors sitting on FTSE 150 boards has increased over the past ten years. In 2010 foreign directors accounted for 24% of board seats, in 2020 this had increased to 30% with most boards (79%) including at least one foreign director.

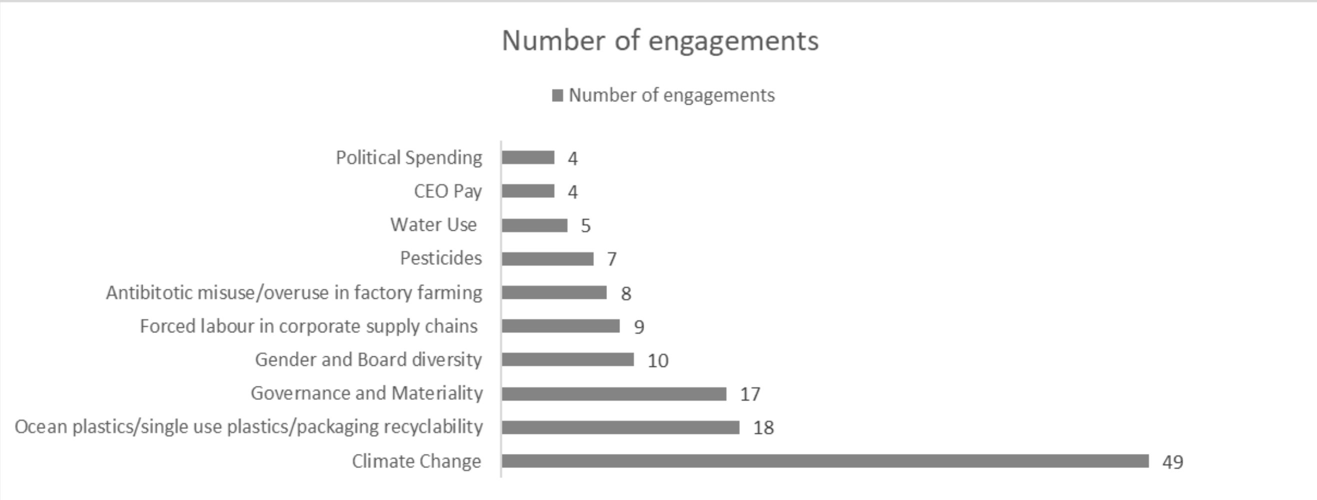
[Source: Spencer Stuart 2020 Board Index]

Shareholder Activism

As You Sow reports on the outcomes of engagement efforts over the 2020 proxy season

As You Sow has released a report on the outcomes of its engagement efforts over the 2020 proxy season.

In total, As You Sow conducted 131 engagements with 111 companies across 10 program areas (see table below). As you Sow's top three focus areas were: 1) climate change (37% of engagements); 2) plastic waste (14% of engagements); and 3) governance.



Outcomes of engagement efforts

Twenty two As You Sow resolutions filed on behalf of shareholders went to a vote. On average, the resolutions received 30% support.

Four resolutions received majority support (the details are set out in the table below).

COMPANY	SUBJECT OF RESOLUTION	VOTING OUTCOME
Fastenal	The resolution called on the board to report to shareholders on the diversity of the company's workforce using Sustainable Accounting Standards Board (SASB) Materiality guidelines.	▪ 61.1% support As you Sow comments that a similar resolution received 20% less support at the 2019 meeting.
Genuine Parts	In both cases the resolution called on the board to report to shareholders on the company's workforce diversity and inclusion practices, diversity targets, human capital risks/opportunities using the SASB guidelines.	▪ 79.1% support
O'Reilly Automotive		▪ 66% support
Phillips 66	The resolution called on the company to publish a report on the public health risks of expanding petrochemical operations and investments in areas increasingly prone to climate change induced storms, flooding and sea level rise.	▪ 54.7% support

Resolutions withdrawn following successful engagement

A further 45 resolutions withdrawn prior to the meeting, as the result of successful negotiations with the companies being targeted.

One example highlighted in the report, is the agreement reached with BP to cooperate on preparing a shareholder resolution, for consideration at the 2021 AGM, calling on the company to 'set a net zero ambition including for scope 1 2 and 3 emissions and increase the proportion of its investment that goes into non-oil and gas business in support of the goals of the Paris Climate Agreement'.

Ongoing dialogue

Page 14 of the report names the companies where engagement is continuing (and may be resolved or develop into future resolutions) and the topics of engagement efforts. Climate change reporting remains the primary focus.

[Sources: As You Sow report: 2020 Shareholder Impact Review: Changing Corporations For Good]

Meetings and Proxy Advisers

BCA backs virtual AGMs and other proposed changes to permanently modernise the Corporations Act

Context

Following what it considers to be a successful test run of changes to meeting and execution requirements introduced in response to the COVID-19 pandemic, the government recently released draft legislation for a short consultation period proposing to make them permanent. Our summary of key proposed changes is here.

> [Note: For further background on the proposed changes, concerns that have been raised and other submissions to the consultation see: Governance News 04/11/2020 from p20.]

BCA supports the proposed changes overall, but has raised some concerns

The Business Council of Australia's (BCA's) submission to the consultation is broadly supportive of the proposed changes on the basis that they are expected to deliver welcome flexibility for business, as well as cost savings. The submission states,

> 'Making the changes to virtual meetings and electronic document execution permanent will be a significant deregulation initiative that will allow businesses to use technology to fulfil their regulatory obligations. They will deliver ongoing cost savings and make it easier to do business in Australia which in turn will support Australia's economic recovery and job creation.'

The submission also argues that the proposed changes are an important step towards modernising the economy.

> 'Most importantly, these changes are another major step forward in the shift to a digital economy. Australia needs to adapt and embrace change if we are to unlock the significant productivity and participation benefits that will flow from the use of digital technology. Accelerating this shift is even more important if we're going to achieve the ambition of being a leading digital economy by 2030'.

Suggested improvements

The submission includes several recommendations which the BCA considers will clarify and/or improve the government's proposals.

Virtual meetings

The submission is supportive of the proposal to permanently enable companies the option to determine their preferred meeting format. However, it also raises several concerns/makes several suggestions as to how the proposed legislation could be improved.

These include the following.

- **Existing shareholder participation requirements should remain unaltered:** The submission expresses concern about what the BCA considers to be an extension of existing requirements to ensure that shareholders have a reasonable opportunity to participate in meetings. Specifically, the BCA questions whether the proposed requirement that 'all persons entitled to attend the meeting' have a 'reasonable opportunity to participate' is appropriate given that the wording departs from the current requirement that 'members as a whole' have reasonable opportunity to participate. The BCA 'submits that the existing standard should be maintained and expects that a clearly higher and judicially uncertain standard would mean companies may be unwilling to utilise virtual meeting technology going forward, and revert to entirely physical meetings'.
- **Imposing new minutes-related requirements for virtual meetings is unnecessary:** The BCA argues that there is no need to require member questions/comments submitted before or at a virtual meeting to be recorded in the minutes because sufficient shareholder protections are already in place. The BCA argues the proposal is a,

> …'disproportionate response to the perceived risk of a member's contributions to a meeting via technology being moderated in a selective manner. It would oblige, without the ability to apply discretion, companies to make public information which, in some instances, may be irrelevant, misleading or defamatory. There are already protections available to members to seek relief under section 1322 and for regulatory intervention by ASIC.

Instead, the BCA suggests that these concerns would be better addressed through strengthening the role of the Australian Securities and Investments Commission (ASIC) by enabling the regulator to: a) conduct inquiries where they consider there are grounds to do so; and b) 'potentially' imposing a new requirement on companies to keep records of questions/comments made at or before a meeting which ASIC could examine should it determine that there was need to do so.

- **Tabling documents should occur prior to a meeting:** The submission argues that the proposal to allow documents to be tabled at a meeting by giving it 'to the persons entitled to attend the meeting before or at the meeting' unnecessarily departs from existing practice. The submission argues that documents should be tabled before meetings (whatever the format) to enable sufficient time for consideration ahead of the meeting.

Electronic signatures

The BCA is also supportive of the proposed changes to execution requirements, but again makes several suggestions as to how the proposed legislation could be improved.

Among other things, the submission argues that proposed electronic execution requirements could be somewhat streamlined. For example, the submission argues that,

> 'The requirement in subsection (3B)(a)(ii) – that a signer receive a document by electronic communication – should be removed. It is not clear as a policy matter why this requirement exists. If a person is signing a document it should not matter how the signer has received the document.
>
> Similarly, the requirement in subsection (3B)(c) for a signer separately to indicate that the signer signed the document is significantly restrictive, and makes reliance by outside parties under section 129(5) difficult. Signing of the document itself should be sufficient'.

Likewise, the submission welcomes proposals to expressly allow 'split execution' of documents but questions whether it is necessary that the document being signed include the entire contents of the document. The submission argues,

> 'Documents can run to hundreds of pages, and in some cases, in relation to construction and infrastructure, they can be over one thousand pages. Where an agreement is being signed (as opposed to a deed), it is common practice, both internationally and in Australia, for the signers to print out and sign just the signature pages, and not to print out the entire document'.

The submission also argues that the proposed reforms should extend the ability to execute deeds electronically to foreign corporations and statutory corporations.

Finally, the submission argues that it 'would be useful to take the opportunity to fix up one common practical problem that occurs in relation to section 127(1). Many small companies have a sole director who is not also secretary. The subsection and subsection (2) should extend to the sole director'.

[Source: Business Council of Australia submission 02/11/2020]

Institutional Investors and Stewardship

ASFA commissioned research finds most super fund members support the idea of funds being more active on ESG issues including climate change

The Association of Superannuation Funds of Australia (ASFA) has released the results of a survey of 1375 superannuation account holders, exploring their views on the superannuation guarantee and their retirement lifestyle expectations as well as their views on superannuation fund action on ESG.

Some Key Takeaways

Support for action on ESG

According to ASFA data, the majority of superannuation fund members approve of funds being active on ESG issues.

- Climate change: 64% of respondents across all age and gender groups supported the idea of superannuation funds being more active on climate change. Support for climate action was highest among young people (18-34 age group) at 73% and lowest among the 50-64 age group at 56%. 20% of respondents overall disagreed that funds should be more active on this issue.
- Governance: 64% of respondents across all age and gender groups supported the idea of superannuation funds being more 'open on corporate governance'. Only 16% of respondents disagreed.
- Gender diversity: 58% of all respondents agreed that funds should be more active in increasing gender diversity. Support was highest among the 18-34 age group (66%) and lowest in the 50-64 age group (50%). Over a quarter (26%) of respondents overall disagreed that funds should be more active on this issue.

The majority of people support the scheduled SG increase

- There was strong support across all gender and age groups (75% of respondents) for the scheduled increase in the superannuation guarantee to 12%. Only 12% of respondents opposed the increase and 13% of respondents indicated that they were unsure.
- 43% of respondents overall said that they were not confident they would have enough super and savings to achieve a comfortable lifestyle during retirement. In the 50-64 age group, 54% of respondents said that they were not confident.
- 52% of respondents overall said that they expect to live on a mix of superannuation, savings and the Age Pension. 43% stated they would prefer to live on their superannuation and savings alone, and 42% advised they would prefer to live on a mix of their super, savings and Age Pension.
- 75% of respondents stated they would struggle to live comfortably on the Age Pension alone, 11% of respondents indicated that they were unsure, and 14% said that they could live comfortably.

[Sources: ASFA media release 09/11/2020; ASFA full text report: Superannuation and Australians' expectations]

Market Forces calls on super fund members to push their own funds to match 'the minimum standard of climate action' that the landmark climate settlement established

Context

On 2 November, The Retail Employees Superannuation Trust (REST) issued a statement announcing that it had reached agreement with fund Mark McVeigh, to settle legal proceedings brought by him in connection with the fund's handling of climate related financial risk. As part of the settlement, REST acknowledged that

> 'Climate change is a material, direct and current financial risk to the superannuation fund across many risk categories, including investment, market, reputational, strategic, governance and third-party risks'

REST also committed to implement a number of actions including: a) setting a net-zero by 2050 target for portfolio emissions; b)disclosing all investments; c) identifying, quantifying and managing climate-related financial risks having regard to the goals of the Paris Agreement and other international efforts to limit climate change; and) factoring climate risk into its investment strategy.

You can access our summary in Governance News 04/11/2020 at p30.

Call for members to pressure their funds to make the same commitments

Market Forces has issued a statement calling on members to write to their funds to push them to match REST's climate commitments. Market Forces states,

> 'The case now sets the minimum standard of climate action that every other super fund in Australia should meet. Market Forces intends to keep pushing super funds further, seeking, most importantly, funds take immediate steps to reduce climate risk by divesting your retirement savings from the coal, oil and gas companies that are undermining the Paris climate goals. Tell your super fund to take climate action, or risk losing you as a member. We've seen some movement from super funds in recent months, with hundreds of millions of dollars being withdrawn from some of Australia's dirtiest companies. However, it's still a matter of not enough super funds, and not enough divestment'.
>
> [Source: Market Forces media release 05/11/2020]

Proposed model law for responsible investment: ShareAction calls on UK parliamentarians to enact legislation to strength the legal duties of fiduciary investors

UK based group ShareAction has drafted a proposed 'model law' – The Responsible Investment Bill –with the aim of strengthening 'the legal duties of fiduciary investors (primarily pension trustees and their asset managers) to act in the best interests of their beneficiaries, by stipulating in law that 'best interests' include environmental and social considerations'.

Some Key Points

- 'Double materiality': Among other things, the Bill proposes to introduce the concept of 'double materiality' through expanding the 'best interests duty'.

  Under the proposes changes, in order for investors to fulfil their fiduciary duty to act in the best interests of their beneficiaries, they would need to consider not only ESG factors in decision making but also the consequences of their investment activities on the financial system, the economy, communities and the environment.
- Default funds and funds marketed as 'sustainable' would be required to align their activities with the goals of the Paris Agreement. The Financial Conduct Authority and The Pensions Regulator would supervise compliance with this requirement.
- Establish a UK Council for Investor Due Diligence regarding human rights and the environment. The Council would research company practices and issue alerts and recommendations to investors. Investors would be required to provide an explanation to the Council within 60 days as to how their intend to mitigate the risk.
- Enforcement: The Bill would also provide enforcement powers through judicial redress for beneficiaries.

Aim for the Bill to be introduced 'before the end of the current parliament'

ShareAction has said it will work with parliamentarians of all parties and other stakeholders to 'build widespread backing for the introduction of such a Bill before the end of the current parliament'.

Support from the leader of the Liberal Democrats

ShareAction quotes Sir Ed Davey leader of the Liberal Democrats as welcoming the Bill, stating that the

> 'government and regulatory action are needed to help us achieve our international climate commitments and to place the financial services sector on a more sustainable footing. This Bill represents a clear pathway to achieving that aim and I look forward to supporting it over the coming months and years.'

[Sources: ShareAction media release 05/11/2020; The Responsible Investment Bill]

Global investor groups have urged the US to re-sign the Paris Agreement, US President Elect Joe Biden has confirmed his intention to do so

Following the formal withdrawal of the US from the Paris Agreement, the founding partners of the Investor Agenda – Asia Investment Group on Climate Change; CDP; Ceres; Investor Group on Climate Change; Institutional Investors Group on Climate Change; and Principles for Responsible Investment – have issued a statement calling for:

- The US to immediately rejoin the Paris Agreement
- All signatories to the Paris Agreement 'step up their climate ambition in order to secure a sustainable global economic recovery and net-zero emissions future'.

President Elect Joe Biden has Tweeted that he intends to re-join the agreement.

> 'Today, the Trump Administration officially left the Paris Climate Agreement. And in exactly 77 days, a Biden Administration will re-join it'.

[Sources: IGCC media release 04/11/2020; Statement]

Disclosure and Reporting

Top Story | UK to mandate TCFD reporting

The UK government has announced plans for the roll out of mandatory TCFD reporting for large companies and financial institutions by 2025

Key Takeouts

- UK Chancellor Rishi Sunak has announced the government's ambition to progressively roll out mandatory TCFD reporting to large companies and financial institutions by 2025.
- The UK joint regulator and government TCFD Taskforce's interim report and implementation roadmap, map out the planned strategy and provide indicative timelines for achieving this goal, with most of the change set to occur by 2023.
- The Taskforce suggests that organisations use the indicative timelines to guide their preparations – organisations are encouraged to consider taking 'the necessary steps now to build their capabilities and iteratively refine their climate data and the resulting disclosures'.
- The Taskforce also expresses support for the IFRS Foundation's proposal to create a new, global Sustainability Standards Board, and the work being undertaken to develop international sustainability standards. The Taskforce states that the it will 'consider an appropriate process for possible endorsement and implementation of international standards in due course'.

In a speech outlining the government's 'vision' for the future of the UK financial services sector, UK Chancellor Rishi Sunak identified the need to address climate risk as a key priority.

Among other measures, Mr Sunak announced the UK's intention to become the first G20 country to 'mandate climate disclosures by large companies and financial institutions across the economy', by 2025.

The announcement was accompanied by a report and accompanying roadmap from the UK joint regulator and government TCFD Taskforce, outlining an 'indicative pathway' to achieving this goal over the next five years, with most of the change set to occur by 2023.

Roadmap for mandating TCFD disclosure: indicative timeframes

The Roadmap outlines a strategy with indicative timeframes/milestones, for the progressive roll out of mandatory TCFD reporting across seven categories of organisation - listed commercial companies; UK-registered companies; banks and building societies; insurance companies; asset managers; life insurers and FCA-regulated pension schemes; and occupational pension schemes – over the next five years.

Annex A at page 22 of the accompanying report provides a summary of the planned roll out of regulatory changes, including indicative timeframes for each category of organisation.

Figure 1 at page 5 of the roadmap provides a consolidated overview of the information.

It's suggested that organisations in every category use the roadmap to plan for the changes. The roadmap suggests that organisations should 'consider taking the necessary steps now to build their capabilities and iteratively refine their climate data and the resulting disclosures'.

Support for global sustainability standards with a view to 'endorsement and implementation in due course'

The Taskforce also expressed support for the development of global standards as put forward in the IFRS Foundation's consultation, as the best path to achieving improved comparability of reporting within the UK and internationally. The Taskforce states,

> 'To achieve a high level of comparability across jurisdictions, consistent disclosures are required. The UK Taskforce considers that, if arrived at sufficiently quickly, this would optimally be achieved through international standards for climate-related and other sustainability disclosures. To this end, the UK Taskforce strongly supports the International Financial Reporting Standards (IFRS) Foundation's proposal to create a new, global

Sustainability Standards Board, as well as complementary work underway on harmonisation by an alliance of voluntary standard-setting organisations.'

The Taskforce adds that it will monitor developments on the issue and 'consider an appropriate process for possible endorsement and implementation of international standards in due course'.

[Sources: Chancellor Rishi Sunak, statement to the House – Financial Services 09/11/2020; A Roadmap towards mandatory climate related disclosures; Interim Report of the UK's Joint Government Regulator TCFD Taskforce]

UK regulator throws its weight behind the development of global sustainability standards

Key Takeouts

- The UK Financial Reporting Counsel (FRC) has issued a statement expressing support for the recent IFRS Foundation consultation on the development of global sustainability standards.
- The FRC considers however, that until global sustainability standards are developed, companies should voluntarily report against the Task Force on Climate-related Financial Disclosures (TCFD) recommendations and the Sustainability Accounting Standards Board (SASB) metrics. The regulator suggests that this should occur where possible, 'within their next reporting cycle'.
- BlackRock has also recently expressed support for the development of global standards as put forward in the IFRS Foundation's consultation. Like the FRC, BlackRock considers that until global sustainability standards are developed, companies should continue to work towards improving the quality of their reporting under existing standards/frameworks. You can find a more detailed summary of BlackRock's approach in Governance News 04/11/2020 at p16.
- Separately the FRC has released the findings of a thematic review into how climate related issues are impacting governance, reporting and audit, and the roles of boards, companies, auditors and professional bodies. The regulator has also released standalone reports presenting detailed findings on certain issues. One headline finding is that corporate reporting needs to improve to meet the expectations of investors and other users - 'users of corporate reporting expect more from companies, auditors, regulators and standard setters' the FRC states.

Context

On 30 September, the International Financial Reporting Standards (IFRS) Foundation released a consultation paper seeking feedback on the strength of demand for global sustainability standards and also on whether the IFRS Foundation should play a role in developing them.

Among other proposals, the Foundation is seeking feedback on a proposal that it establish a new sustainability standards board which would operate alongside the International Accounting Standards Board (IASB) and 'build on existing developments and collaborate with other bodies and initiatives in sustainability, focusing initially on climate related matters'. The deadline for submissions is 31 December 2020.

The FRC supports the development of global sustainability standards in the long term

The UK Financial Reporting Council (FRC) has released a statement expressing support for the long term goal of developing global standards for non-financial reporting and welcoming the IFRS Foundation consultation.

Progress toward improving sustainability reporting should continue in the interim

The FRC considers that until global standards are developed, which is likely to be a time-consuming process, companies should voluntarily report against the Task Force on Climate-related Financial Disclosures' (TCFD) recommendations and, use the Sustainability Accounting Standards Board (SASB) metrics for their sector. This approach is expected to assist them to improve 'the quantity and quality of climate-related and wider environmental, social and governance reporting' in line with the needs of investors.

The FRC has encouraged companies to implement TCFD/SASB aligned reporting in their next reporting cycle, 'where possible'.

Increased focus on climate risk

The FRC states that in the short to medium term it will consider how best to 'help companies to achieve reporting under TCFD and SASB that meets the needs of investors'.

The statement suggests that this work could include the following measures.

- 'Increasing the focus on climate change considerations as part of Corporate Reporting Review, and Audit Quality Review monitoring work where relevant.
- Undertaking a review of reporting under the Streamlined Energy and Carbon Reporting regulations in 2021.
- Assessing professional associations' approaches to climate change, including in their regulatory and curriculum-setting functions.
- Incorporating monitoring of climate-related reporting into our annual UK Stewardship Code and UK Corporate Governance Code monitoring and consider whether climate-related amendments are appropriate within future revisions of these Codes, the Guidance on the Strategic Report and associated guidance.
- Investigating developing investor expectations and better practice reporting under TCFD and SASB, plus engage internationally on the developing approach to reporting frameworks and standards.
- Highlighting areas of the financial statements of UK GAAP reporters where climate change could be a consideration.
- Undertaking a project considering the role of assurance, and responsibilities of audit committees in this area'.

Some key takeaways from the FRC's thematic review

Separately the FRC has released the findings of a thematic review into how climate related issues are impacting the governance and reporting practices of boards, companies, auditors, industry bodies, investors and regulators.

The report outlines the regulator's view on current market practice, sets out the FRC's expectations and provides examples of better practice, and identifies areas of focus for the regulator going forward.

A headline finding is that every group needs to do more to meet the climate challenge. Financial Reporting Council CEO Jonathan Thompson states:

> 'Climate change will affect companies and societies across the globe, and while for some companies these challenges may be further on the horizon, climate change must be integrated into decision making now if we hope to tackle it in an orderly way. Users of corporate reporting expect more from companies, auditors, regulators and standard setters. While this review of corporate reporting and audit highlights some bright spots of better practice, we also found that more needs to be done. We must do better – all of us'.

The FRC has also released standalone reports presenting detailed findings on: Governance; Corporate reporting; Audit; Professional Oversight; and Investor reporting and TCFD disclosure.

Corporate reporting

On the issue of Corporate Reporting, the FRC found that though companies are increasingly addressing climate risks in their narrative reporting, and a growing number of companies are reporting in line with the TCFD recommendations/intend to do so, the standard of reporting needs to improve.

For example, though the impacts of climate change on the business model, including risks and opportunities were often touched on, a number of reports either 'lacked substance' or placed undue emphasis on the opportunities as opposed to the risks. The FRC observes that 'Investors seek to understand the risks and opportunities presented by climate change including their prioritisation, likelihood and impact, and the timeframes over which they might crystallise; they would like this to be presented in a more balanced way'.

Summing up what companies need to do to lift standards, Mr Thompson said that companies need to provide more detailed, specific information:

> 'In particular, corporate reporting should address the company's impact on the environment, the resilience of its business model and the impact of climate change on its financial statements. For UK companies, the Government has pledged to reach 'net zero' by 2050, and in the Green Finance Strategy outlined its

expectation that listed companies and large asset owners should be reporting using a framework established by the Taskforce on Climate related Financial Disclosures by 2022. The challenge is clear.'

The future of corporate reporting

The FRC observes that though TCFD/SASB aligned reporting should help meet the needs of investors, investors are not he only users of corporate reports. Referencing its recent discussion paper - the Future of Corporate Reporting – the FRC emphasises the importance of ensuring reports meet the needs of a broader range of stakeholders and welcomed the work being undertaken to assess how existing frameworks could come together to achieve this aim.

[Sources: FRC Statement on Non-Financial Reporting Frameworks 10/11/2020; FRC media release 10/11/2020; FRC Report: Climate Thematic November 2020]

Regulators

In Brief | AUSTRAC and the United Arab Emirates Financial Intelligence Unit have signed a financial intelligence MOU to facilitate cooperation in the 'development, exchange and analysis of financial intelligence related to suspected money laundering, terror financing and/or other serious crimes'

[Source: AUSTRAC media release 02/11/2020]

In Brief | US firms should be prepared for increased regulatory focus on climate risk: In a recent speech, SEC Commissioner Allison Herron-Lee spoke about how climate risk fits into SEC's mandate. Commissioner Lee said that climate risk is a systemic risk to financial markets and emphasised the importance of having access to accurate and reliable information about climate-related risks from both a regulatory and investor perspective. In addition, she flagged other areas where SEC could step up its oversight including: oversight of funds and their advisers, credit rating agencies, and accounting standards

[Source: Speech by SEC Commissioner Allison Herren Lee Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation 05/11/2020]

Financial Services

Top Story | Proposed overhaul of responsible lending obligations: Draft legislation released for consultation

Key Takeouts

- On the 25 September, the government announced plans for the proposed overhaul of consumer credit laws, including plans to roll back what it considers to be overly prescriptive responsible lending obligations. The object of the proposed changes is to improve the flow of credit and support the nation's economic recovery. You can find our summary here.
- On 4 November, the government released a package of draft legislation for consultation, proposing to implement these changes.
- Broadly (if enacted) the proposed changes will mean that from 1 March 2021:
  - Responsible lending obligations in Chapter 3 of the National Consumer Credit Protection Act 2009 (Cth) (NCCP Act) will only apply to: a) small amount credit contracts (SACCs); b) 'SACC-equivalent loans' (low limit credit contracts) provided by ADIs; and c) consumer leases.
  - This means that ADIs will no longer be required to comply with the responsible lending obligations NCCP Act (except 'SACC-equivalent loans). ADIs will continue be required to comply with the prudential standards set and enforced by the Australian Prudential Regulation Authority.
  - Non-ADI credit providers will need to comply with new non-ADI lending standards, modelled on 'key elements' of APRA's prudential standards applying to ADIs.
  - All credit assistance providers will need to comply with the 'best interests' obligations legislated for mortgage brokers.
- The deadline for submissions to the consultation is 20 November 2020. The proposed commencement date for the changes is March 2021.

Overview

Treasury has released for consultation a package of draft legislation – [Exposure draft] NCCP (Supporting Economic Recovery) Bill 2020 (updated); [Exposure draft] NCCP (A new regulatory framework for the provision of consumer credit) Regulations 2020; [Exposure draft] Non-ADI Credit Standards and accompanying explanatory materials - proposing to legislate changes to consumer credit requirements previously announced by the government, and outlined in a fact sheet, on 25 September. You can access our summary here.

The deadline for submissions on the draft legislation is 20 November 2020.

The proposed commencement date for the changes is 1 March 2021.

Key changes

Rolling back responsible lending requirements

To remove unnecessary regulatory duplication and to move away from what the government considers to be an overly prescriptive, 'one size fits all' approach to lending, it's proposed that from 1 March 2021:

- Responsible lending obligations in Chapter 3 of the National Consumer Credit Protection Act 2009 (Cth) (NCCP Act) will only apply to: a) small amount credit contracts (SACCs); b) 'SACC-equivalent loans' (low limit credit contracts) provided by ADIs; and c) consumer leases.
- ADIs will continue be required to comply with the prudential standards set and enforced by the Australian Prudential Regulation Authority. The draft explanatory materials comment that,

> 'APRA's prudential standards for ADIs ensure lenders have appropriate settings for managing risk to financial soundness throughout the life of loans. The credit risk management standards that ADIs are expected to meet include expectations of sound lending practices similar to the requirements under the RLOs [responsible lending obligations]. As part of these sound lending practices, APRA imposes serviceability requirements to ensure consumers can meet their obligations without substantial hardship'.

New non-ADI lending standards: applying 'key elements' of APRA's prudential lending standards to non-ADI credit providers

If enacted, Schedule 1 of the draft Bill will enable the Minister to determine standards, by legislative instrument, specifying requirements for a credit licensee's systems, policies and processes in relation to certain 'non-ADI credit conduct' such as entering into a credit contract, increasing the credit limit under a credit contract, 'or making an unconditional representation to a consumer that the licensee will do either of those things'.

According to the draft explanatory memorandum, the aim of the draft National Consumer Credit Protection (Non-ADI Credit Standards) Determination 2020 (the Standard) is to:

> 'ensure non-ADI credit providers establish, maintain and implement systems, policies and processes directed toward credit being provided where the licensee has assessed that a borrower will have the capacity to repay any credit provided without substantial hardship'.

This will be achieved through 'appropriately adopting key elements of APRA's prudential lending standards for ADIs', and in particular certain provisions in APRA's forthcoming prudential standard APS 220 Credit Risk Management (APS 220), and applying them to non ADI credit providers.

The draft explanatory materials state that the proposed Standard is similar to provisions in APRA's forthcoming APS 220 relating to an institution's lending standards and ensuring borrowers' capacity to repay in APS 220 Credit Risk Management. The draft explanatory materials flag that APRA will consult 'over the coming month' on a further amendment to APS 220 which will require an ADI to assess an individual's capacity to repay credit without substantial hardship.

The draft standard

Broadly it's proposed that the draft Standard will:

- Impose obligations on credit licensees to: a) implement and maintain 'systems, policies and processes' to assess that a borrower will have the capacity to repay any credit provided without substantial hardship'; and b) formally document these processes/systems in a written plan, before engaging in 'non-ADI credit conduct'.
- Require licencees to retain a record of this written plan for seven years after the time it 'ceases to set out the current systems, policies and processes the licensee utilises'.
- Require licensees, at the request of a consumer, to provide the consumer with a copy of an assessment for up to seven years after the credit contract was entered into or the credit limit was increased.
- Breach of these requirements could attract a maximum civil penalty of 5000 penalty units.

A risk based approach

The draft explanatory materials emphasise that this approach reflects the government's decision to move away from what it considers to be an overly prescriptive approach to lending.

> 'These standards will require licensees to implement adequate systems, policies and processes relating to non ADI credit conduct rather than impose individual conduct level obligations. This enables credit assessment to move away from a prescriptive framework for lenders and borrowers and will support risk-based lending that is attuned to the needs and circumstances of the borrower and credit product. These standards are appropriately adopted from the APRA standards to maximise alignment between the ADI and non-ADI regimes'.

The draft explanatory materials also emphaise that the standard will not apply in relation to credit provided 'genuinely for a small business purpose, where that purpose is not minor or incidental to the overall purpose of the credit'.

> 'Clarifying that the Standard does not apply to lending for a small business purpose will ensure that the obligations being imposed do not impede the timely flow of credit to small business. Licensees will still be required to determine the purpose of credit for compliance with other provisions of the Act and the National Credit Code'.

The proposed commencement date for the draft standard is immediately after the commencement of the draft Bill (1 March 2021).

Extension of best interests obligations to all credit assistance providers

If enacted, from 1 March 2021 the 'best interests' obligations legislated for mortgage brokers will be extended to all credit assistance providers.

This means that licensees and their credit representatives will be required to:

- act in the best interests of consumers when providing credit assistance in relation to credit contracts;
- resolve any conflicts of interest (should they arise) in the consumers' favour

Licensees that authorise credit representatives will also be required to take 'reasonable steps' to ensure that those representatives comply with best interests obligations.

A maximum civil penalty of 5,000 penalty units will apply for a breach of these obligations.

The object of the proposed change is to 'improve outcomes for consumers by legally requiring that credit assistance providers act in the consumer's best interests and place their consumer's interests before their own'.

Principles based standard

The draft explanatory materials state that

> 'The duty to act in the best interests of the consumer in relation to credit assistance is a principles-based standard of conduct that applies across a range of activities that licensees and representatives engage in. As such, what conduct satisfies the duty will depend on the individual circumstances in which credit assistance is provided to a consumer in relation to a credit contract. The duty does not prescribe conduct that will be taken to satisfy the duty in specific circumstances. It is the responsibility of credit assistance providers to ensure that their conduct meets the standard of 'acting in the best interests of consumers' in the relevant circumstances'.

The draft explanatory memorandum expressly states that the 'obligations do not apply to credit assistance provided in relation to credit for predominantly business purposes'.

> [Sources: Treasury media release 04/11/2020; [Exposure draft] NCCP (Supporting Economic Recovery) Bill 2020; [Exposure draft] NCCP (A new regulatory framework for the provision of consumer credit) Regulations 2020; [Exposure draft] Non-ADI Credit Standards; [Exposure draft] Explanatory Materials for Bill; Explanatory Materials for Regulations; Exposure draft] Explanatory Materials for Non-ADI Credit Standards]

Treasury has been tasked with developing draft legislation to strengthen unfair contract terms protections

Context

In November 2016 unfair contract terms (UCT) protections were extended to small business contracts.

In 2018 a review of the effectiveness of the changes was conducted, and in December 2019, Treasury released for consultation a Regulation Impact Statement seeking feedback on a range of policy options to address the issues identified by the 2018 Review. The consultation period was open until 27 March 2020. Treasury also held consultation roundtables in March 2020 with a broad range of stakeholders.

Consultation update

Submissions identified a need to strengthen existing protections: According to Treasury, feedback to the consultation flagged two issues: 1) that unfair contract terms remain prevalent in standard form contracts; and 2) that there continues to be uncertainty around the scope of existing protections. Submissions to the consultation have been released and can be viewed here.

Agreement that change is needed: On 6 November 2020, Commonwealth and state and territory consumer affairs ministers agreed that action is required to strengthen existing unfair contract term protections for consumers and to reduce the prevalence of UCTs in standard form contracts.

The group agreed that changes to existing requirements should include:

- making unfair contract terms unlawful and giving courts the power to impose a civil penalty

- lifting the eligibility threshold for the protections from less than 20 employees to less than 100 employees, and introducing an annual turnover threshold of less than $10 million as an alternative threshold for determining eligibility
- removing the requirement for the upfront price payable under a contract to be below a certain threshold in order for the contract to be covered by the UCT protections;
- improving the clarity around the definition of a standard-form contract, for example, by providing 'further certainty on factors such as repeat usage of a contract template, and whether the small business had an effective opportunity to negotiate the contract'.

The Decision Regulation Impact Statement provides further detail on the preferred options for reform and insights into feedback received in response to the consultation.

Estimated implementation costs

The estimated cost to business of implementation of the 'preferred options' included in the Decision Regulation Impact Statement is $7.5 million in the first year, with no ongoing compliance costs.

Next steps: Treasury to develop draft legislation

Treasury has been tasked with developing exposure draft legislation for consultation. No timeframe has been given for the release of the draft legislation.

[Sources: Treasury Consultation: Enhancements to Unfair Contract Term Protections - Regulation Impact Statement for Decision; Regulation Impact Statement for Decision; Consumer Affairs (CAF) meeting communique]

Further consultation: ASIC is consulting on further amendments to the draft product intervention order targeting continuing credit contracts

Context

In July, the Australian Securities and Investments Commission (ASIC) consulted (CP 330) on a proposal to use its product intervention power to target certain continuing credit contracts that it considers cause 'significant consumer detriment' to vulnerable customers.

ASIC proposed to impose an industry wide product intervention order (order) that would impose a cost cap on the total fees that could be charged under continuing credit contracts targeted at low income/unemployed retail clients. You can find our summary here.

Feedback to the initial consultation raised concerns that the proposed product intervention order was too broad

ASIC states that several of the 900 submissions received in response to CP 330 raised concerns that as drafted, the proposed order would inadvertently capture 'certain sub-classes of continuing credit contracts' – buy now pay later arrangements and fees charged for the option to pay off continuing credit contracts using a non-cash payment facility (eg direct debit card) - that do not cause the significant consumer detriment described in CP 330.

Consultation on proposed changes to address 'potential unintended consequences'

To address these concerns, ASIC has released an amended draft product intervention order and issued an addendum to CP330 outlining the proposed changes. In essence, ASIC proposes to narrow the application of the order to exclude both:

- buy now pay later arrangements because ASIC considers that 'the significant detriment described in CP 330, does not, on the evidence currently available, arise from buy now pay later arrangements'.
- fees charged to retail clients for using a non-cash payment facility to make payments towards a continuing credit contract, where the issuer of the facility holds an Australian Financial Services (AFS) Licence. ASIC considers that the consumer protections already in place, in these circumstances eg access to external dispute resolution if the issuer of the facility holds an AFS licence, to be sufficient.

The proposed changes to the draft order are summarised in table 1 of the addendum to CP 330 at p2.

Timing

The deadline for submissions is 24 November 2020.

[Source: ASIC media release 10/11/2020]

Payment services reform: Treasury, APRA and ASIC will work to develop a reform package to implement the CFR's recommended changes to the regulation of stored value facilities (eg international money transfers, gift cards, pre-paid cards and digital wallets)

The Council of Financial Regulators' (CFR) report into the regulation of stored-value facilities (SVFs) (eg international money transfers, gift cards, pre-paid cards and digital wallets) makes eleven recommendations to modernise and simplify the SVF regulatory framework in light of the changes that have occurred since it was first implemented and in light of the possible increased uptake of SVFs going forward.

The eleven recommendations are as follows.

11 RECOMMENDATIONS	
Recommendation 1	▪ ' SVFs should be introduced into the regulatory framework as a new class of regulated product, replacing 'purchased payment facilities'. ▪ 'Regulation of SVFs should be graduated and commensurate with risks to consumers'.
Recommendation 2	▪ 'Certain SVFs (and other payment products) that pose limited risk to consumers – such as small and/or limited-purpose facilities – should continue to be largely exempt from most regulatory requirements'.
Recommendation 3	▪ 'Issuers of payment products that hold client funds for only a short period of time for the purpose of facilitating a payment should be required to hold an Australian Financial Services (AFS) licence from the Australian Securities and Investments Commission (ASIC) and comply with the requirements of an updated ePayments code'.
Recommendation 4	▪ 'ASIC should be given the power to make compliance with the ePayments code mandatory, such as through a rule-making power' .
Recommendation 5	▪ 'The Australian Prudential Regulation Authority (APRA) and ASIC should be responsible for regulating and licensing SVF providers, consistent with their respective mandates for prudential supervision and consumer protection'. ▪ 'The Reserve Bank of Australia (RBA) should no longer be involved in regulating individual providers of SVFs, helping to streamline regulation in this segment of the market'.
Recommendation 6	▪ 'APRA should be responsible for prudential supervision of large SVFs that enable consumers to hold a significant amount of funds for long periods and to withdraw their funds on demand in Australian currency (eg by transferring funds to their bank account). These facilities are likely to offer similar functionality as a bank deposit and should be subject to the highest level of regulatory oversight within an updated regulatory framework for SVFs'.
Recommendation 7	▪ 'APRA should review its existing PPF prudential framework, with a view to introducing requirements for SVFs that are simpler, more targeted to the key risks posed by such entities and, where appropriate, better aligned with international approaches'.

11 RECOMMENDATIONS	
Recommendation 8	▪ 'ASIC should be responsible for regulating SVFs that do not meet the criteria for APRA prudential supervision. In addition to holding an AFS licence, providers of these products should be subject to additional requirements administered by ASIC to ensure the safety of consumers' funds. In particular, the Corporations Act 2001 (Corporations Act) should be amended to ensure that protections on client money loaded in to SVFs operate effectively and client funds cannot be used as the provider's working capital.'
Recommendation 9	▪ 'AFS licensees that are subject to the amended client money protections should be required to report to ASIC on the amount of stored value that is held and transaction flows (eg aggregate amount in and out during a period)'.
Recommendation 10	▪ 'A revised regulatory framework should incorporate a mechanism to "designate" certain facilities as being subject to APRA supervision in the public interest (eg on the basis of financial system risk considerations). The CFR should develop principles to guide such decisions, which could be vested in the Minister or exercised jointly by APRA and ASIC'.
Recommendation 11	▪ 'The CFR agencies should further consider additional measures to improve the clarity and transparency of SVF regulation for consumers and regulated entities. This could potentially include publishing a simple guide to payment regulation and providing guidance through ASIC's MoneySmart site for consumers using SVFs'.

Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume has said that implementation of the recommendations requires changes to both legislation and existing prudential standards and that Treasury has been tasked with working with APRA and ASIC to develop the reform package.

[Sources: Council of Financial Regulators media release 06/11/2020; Full text report: Regulation of Stored-value Facilities in Australia; Senator Jane Hume media release 06/11/2020]

FinTech/RegTech inquiry: Senate Committee set to focus on longer-term issues including (among others) the potential for non-bank technology companies to become accredited data recipients under the CDR regime and the roll out of the CDR to additional sectors

Context

In September the Senate Select Committee on Financial Technology and Regulatory Technology released its interim report into how competition in the financial services sector (and beyond), could be improved through supporting technological innovation and streamlining/updating existing requirements to ensure they are fit for purpose. The report included 32 recommendations which Committee Chair Senator Andrew Bragg described as a 'series of quick wins'. Our summary of the key takeaways is here.

Second issues paper released

Ahead of the government's formal response to the interim report, and ahead of the release of the final report next year, the Committee has released a second issues paper outlining the longer-term issues on which it now intends to focus. These issues include the following.

- the competitiveness of Australia's corporate tax settings
- regulatory culture and in particular, 'analysing is the ongoing role and use of ASIC's product intervention power'
- identifying research and development opportunities to assist the tech sector to drive growth in the Australian economy

- examining various issues relating to the roll out of the consumer data right (CDR) including exploring the potential for big non-bank technology companies to become accredited data recipients under the CDR regime and the roll out of the CDR to additional sectors
- exploring the issue of international data standards and facilitating data sharing with other jurisdictions
- considering the potential for blockchain based systems to streamline interactions between individuals/businesses and government
- exploring how digital identify could streamline interactions between businesses/individuals and government and be used to support new applications
- exploring approaches to cyber security in the FinTech and RegTech sectors and whether 'current industry practices and requirements in relation to data security are adequate'
- the appropriate framework to facilitate ongoing for consideration of FinTech policy issues once the Committee concludes its inquiry

Timing and next steps

The due date for submissions is 11 December 2020. The Committee's final report is due by 16 April 2021.

[Source: Senate Select Committee on Financial and Regulatory Technology Second Issues Paper]

California: Insurers prohibited from declining to renew or cancelling policies for residential properties in areas impacted by the 2020 wildfires for one year

Californian Insurance Commissioner Ricardo Lara has announced a one year moratorium on insurance companies declining to renew or cancelling residential property insurance policies for policy holders in areas within or adjacent to declared 2020 wildfire disaster zones.

This is the second consecutive year that a moratorium has been called since the 2018 law (Senate Bill 824) enabling the Commissioner to provide temporary relief from non-renewals to residents living within/adjacent to a declared wildfire disaster was enacted.

Announcing the moratorium Commissioner Lara said that avoiding a repeat in future will require all stakeholders, including insurers to work in partnership to mitigate the risk.

> 'If we don't want to be in this position every year, we have to reduce the risk to lives and homes, which means everyone plays a part - homeowners and state and local governments through home-hardening, the federal government though forest management, and the insurance industry working as a partner,' he added.

Commissioner Lara is set to hold a virtual meeting on 10 December with stakeholders - homeowners, first responders, advocates, and insurance representatives – to discuss 'potential administrative and regulatory changes to incentivise home-hardening and discuss models that are based in fire science to protect lives and property'.

The announcement of the moratorium was welcomed by the Executive Director of United Policyholders who said who said it would reassure policy holders 'as we work together to establish the state wide mitigation and reward program that will help reduce wildfire risk and restore available, affordable options for consumers.'

[Source: Insurance Commissioner Ricardo Lara, California Department of Insurance media release 05/11/2020]

The FSC will make further changes to the Life Insurance Code of Practice following consultation

In November 2018 The Financial Services Council (FSC) consulted on proposed changes to the Life Insurance Code of Practice. The FSC has now released its response to that consultation and outlined its planned next steps in light of the changes that have occurred since the consultation.

Planned changes to the Code

Planned changes to the draft Code include the following.

- **ASIC approval:** To increase consumer confidence in the Code, the revised Code will be submitted to the Australian Securities and Investments Commission (ASIC) for approval. The FSC states that the enforceability of certain provisions will also be considered following the finalisation of legislation.
- **Plain English rewrite**: To make the Code more readily understandable for consumers, a Plain English specialist will be engaged to rewrite the Code for 'language, structure and length'. The FSC notes that feedback was received calling for the Code to impose additional obligations on insurers to develop and review definitions. However, the FSC maintains that: a) the 'revised Code can provide clarity to consumers on what is covered through the clear use of plain language headings'; and b) that the release of the draft Code should not be delayed by the significant work required to standardise terms in insurance.
- **Sanctions:** The revised Code will strengthen the ability of the Life Insurance Code Committee (LCCC) to impose sanctions for significant breaches of the Code, in line with recommendation 4.10 of the Hayne Commission.
- **Extend to third party distributors:** To ensure consumers are able to rely on the Code provisions, the application of the Code will be broadened to include third-party distributors where the insurer has engaged or partnered with a third party distributor who is acting on behalf of the insurer, or under an arrangement with the insurer. This will not include independent financial advisors operating under their own AFSL.
- **Communication with customers:** The revised Code will clarify when certain communications with customers should be in writing. In addition, the revised Code will 'ensure that communication between insurer Code subscribers and their customers is consistent and done in the manner agreed with the customer where practical or except where an obligation explicitly states that it must be done in writing'.
- **Use of surveillance:** The revised Code will include changes relating to the use of interviews and surveillance of claimants including a new requirement for insurers to cease surveillance of claimants on the advice of 'any medical practitioner'.
- **Family history:** The revised Code will place limits on the information that can be sought by including a 'genetic moratorium' (as has already been implemented).
- **Funeral insurance:** To ensure customers understand how much their life insurance will cost at the outset and how the cost might change into the future, the revised Code will require this information to be clearly explained in product literature.
- **Pressure selling:** The revised Code will make clear that sales process should be driven by the customer. The Code will make clear tha pressure selling is not permitted and outline the key characteristics of a good sales process.
- **Conflicted remuneration:** The draft Code introduced an obligation to ensure that sales and claims staff were remunerated in accordance with good customer outcomes and with the core principles of the Code. The FSC states that 'the revised Code will bring these provisions forward in the Code in a separate section and apply them to those staff that interact with consumers, including sales, underwriting and claims teams'.
- **Design and distribution obligations:** At the time of the 2018 consultation of the draft Code, the design and distribution obligations (DDO) regime had not yet been finalised. Following the passage of the legislation, the sections on product design will now be reviewed to remove Code provisions which duplicate obligations under the DDO regime, and to 'focus on obligations subscribers should comply with to fill in the gaps around their existing legal obligations when designing policies'.

[Sources: FSC media release 06/11/2020; Life Insurance Code of Practice 2.0: Review of Consultation Feedback]

General insurers: APRA consults on revised data collection – cyber insurance and management liability data

The Australian Prudential Regulation Authority (APRA) has written to general insurers seeking their feedback on a proposal to start collecting cyber insurance and management liability data within the National Claims and Policies Database.

APRA is seeking feedback in particular on the proposed start date (APRA proposes to begin collecting data for the 31 December 2020 half yearly reporting period on a best endeavours basis, with full implementation from the 30 June 2021); the inclusion of three new cause of loss codes, treatment of historical data and publication of data in the NCPD data collection.

The due date for submissions is 17 December.

[Source: APRA letter to general insurers 05/11/2020]

AFCA seeks ASIC approval of unresolved SCT complaints transition arrangements

Following consultation, the Australian Financial Complaints Authority (AFCA) has sought Australian Securities and Investments Commission (ASIC) approval of proposed changes to the AFCA rules to enable any unresolved complaints from the Superannuation Complaints Tribunal (SCT) - which will cease operations at the end of the year – to be dealt with by AFCA.

Under the changes AFCA will able to:

- accept and consider complaints that are not resolved by the SCT before it ceases operations
- AFCA will consider any complaints transferred from the SCT under the AFCA Rules that apply to superannuation complaints.
- Complaints transferred from the SCT will enter AFCA's dispute resolution process at the stage most comparable to the stage the complaint had reached at the SCT
- The SCT will transfer the complaint files to ensure all information previously provided to the SCT is available to AFCA.
- AFCA will also be able to consider any matters that are before the Federal Court on appeal from the SCT that are not finalised prior to SCT ceasing operations, and that require remittal back to be determined again or finalised in accordance with the Court's decisions.

Timing

Pending approval by ASIC, AFCA anticipates the Rules will be released in January 2021.

[Source: AFCA media release 04/11/2020]

COVID-19: So far funds have paid out $34.8 billion under the government's early release of superannuation scheme, the data indicates that the number of applications coming through is slowing

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 1 November 2020.

- 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 continues to slow: Over the week to 1 November superannuation funds received 24,000 applications (the same volume as in the week to 25 October, and down on the 25,000 applications received in the down the week to 18 October).
- Of the applications received in the week to 25 October, 16,000 were initial applications bringing the total number of initial applications received to date to 3.3 million since inception of the scheme.
- 8,000 applications were repeat applications, bringing the total number of repeat applications to 1.3 million since the inception of the scheme.
- Over the week to 1 November, superannuation funds made payments to 23,000 members worth $166 million (down from $173 million worth of payments to 24,000 members in the week to 25 October).
- Funds have made approximately 4.6 million payments since the inception of the scheme worth a total of $34.8 billion paid. This figure represents 98% of applications received since inception of the scheme.

[Source: APRA media release 02/11/2020]

Related news

- Business Insider reports that the ATO indicates that up to 7% of early release withdrawals have been processed for members who were ineligible to access their savings, in most cases because members misunderstood the eligibility criteria. The ATO has reportedly asked 1600 superannuation members to provide evidence of their eligibility as part of a pilot program.
- The WSJ reports that few Americans have opted to access their retirement savings early under the US COVID-19 early release scheme, despite the considerable financial impact of the pandemic. This may reflect the fact that those most likely to do so are also least likely to have savings to access.

[Sources: [registration required] The WSJ 05/11/2020; Business Insider 06/11/2020]

Interim arrangements: APRA has advised ADIs of changes to the capital treatment of new or additional equity investments in banking and insurance subsidiaries ahead of the finalisation/implementation of APS 111

Context

In 2019, the Australian Prudential Regulation Authority (APRA) consulted on proposed changes to APS 111 Capital Adequacy: Measurement of Capital including proposed changes to the capital treatment of authorised deposit-taking institutions' (ADIs') equity investments in their banking and insurance subsidiaries.

'Interim' arrangements

Until APS 111 is finalised and implemented (the interim period), APRA considers it important that any new or additional equity investments are undertaken with the 'the proposed policy in mind' and has written to ADI's to advise of an interim change to ensure that this occurs.

APRA has advised that until APS 111 is finalised/implemented:

- APRA will require new or additional equity investments in banking and insurance subsidiaries, 'where the amount of that new or additional investments takes the aggregate value of the investment above 10 per cent of an ADI's Common Equity Tier 1 (CET1) capital, to be fully funded by equity capital at the ADI parent company level'.

- ADIs are expected to notify APRA ahead of any new or additional equity investments in banking and insurance subsidiaries, which would result in the aggregate value of any investment exceeding 10 per cent of an ADI's CET1 capital.
- APRA makes clear that during the interim period, there will be no change to the capital treatment of any existing equity investments in subsidiaries.

[Source: APRA Letter to ADIs 10/11/2020]

In Brief | ASIC IDR roundtable: The AIST is set to attend ASIC's roundtable on RG 271: Internal Dispute Resolution on 25 November The discussion will focus on what is required for internal dispute resolution systems to meet ASIC's standards/requirements

[Source: AIST policy news 05/11/2020]

In Brief | CHOICE has given a 'Shonky award' to a funeral insurer who does not display the itemised prices of its funeral services in all states/territories. CHOICE has called on the insurer to remedy this by publishing the information on its website and is calling on all state and territory consumer affairs ministers to make transparent funeral pricing the norm

[Source: CHOICE media release 10/11/2020]

In Brief | UK Business Insurance Test Case: The FCA has released resources to assist policy holders understand the High Court decision and the status of the appeal. The FCA comments that none of the information is new, but is instead aimed at assisting readers to navigate the court documents

[Source: FCA media release 04/11/2020]

Risk Management

CLIMATE RISK

A way forward on climate? Climate Change (National Framework for Adaptation and Mitigation) Bill 2020 introduced

On 9 November Independent MP Zali Steggal introduced two Bills into the House of Representatives:

- Climate Change (National Framework for Adaptation and Mitigation) Bill 2020 which proposes to implement a national framework to drive Australia's response to climate change
- Climate Change (National Framework for Adaptation and Mitigation) (Consequential and Transitional Provisions) Bill 2020: This Bill proposes a number of amendments to various Commonwealth laws to support the operation of the primary Bill.

Key Takeaways

The Climate Change (National Framework for Adaptation and Mitigation) Bill 2020 proposes leave 'national action in the hands of our elected Government but mandates an effective process for national targets, actions and reporting, with the Government guided by a respected Commission whose independence is assured by a Parliamentary Joint Committee'.

Broadly, the Bill proposes to:

- Commit Australia to a 2050 net zero emissions target.
- Establish an independent Climate Change Commission (CCC) to guide policy, provide advice and independent oversight of the effectiveness of the government's actions in meeting this target. The Commission would have responsibility for:
  - preparing a national climate change risk assessment within 12 months of the commencement of the Bill (if enacted), and every five years after that
  - evaluating the effectiveness of government's planned actions in response to the Commission's risk assessment (the national adaption plan)
  - advising the Minister on setting emissions budgets and emissions reduction plans.
- A new Parliamentary Joint Committee on Climate Adaptation and Mitigation would provide oversight of the CCC.
- Require the preparation of a national adaption plan, emissions budgets and emissions reduction plans: In response to each national climate change risk assessment prepared by the new Climate Change Commission, the Minister would be required to prepare a national adaption plan, set emissions budgets and prepare emissions reduction plans.

Response

- Business/industry/community groups have called for bipartisan support of the Bill: Over one hundred businesses, industry groups and community organisations including the AMA, Atlassian among others, have called on all sides of politics to support the passage of the Bill on the basis that 'the legislation, if adopted as a bipartisan measure, would assist the private and public sector in decision making. It would also reassure the Australian community that the Government is on the right track with addressing climate change over time in a fiscally responsible way'.
- The Australian Industry Group has issued a statement calling for the government to support the Bill. The statement suggests that the election of Joe Biden as the next president of the US is an opportunity for Australia to reset its climate policy. AI CEO Innes Wilcox commented:

  > 'The dramatic escalation of international efforts against climate change in recent months, capped by the victory of President-elect Biden in the United States, should give Australia the confidence to reset climate policy. This changing international landscape provides Australia with the renewed impetus to deliver a

bipartisan, nationally agreed framework that would match our international partners, end the climate wars and give business a sound foundation to plan for the future.'

[Sources: Joint letter to parliament; Australian Industry Group media release 08/11/2020 (accessed via LexisNexis Capital Monitor)]

Prime Minister Scott Morrison has said he would welcome the US rejoining the Paris Agreement

In a statement congratulating US President elect Joe Biden and Vice President elect Kamala Harris on their election, Prime Minister Scott Morrison identified climate change among the issues on which his government looks forward working with the new administration. Mr Morrison said that the government looks

> …'forward to working with President-elect Biden and his Administration to continue to fight the COVID-19 global pandemic and recession, to develop a vaccine, drive a global economic recovery, and develop new technologies to reduce global emissions as we practically confront the challenge of climate change. We welcome the President-elect's commitment to multilateral institutions and strengthening democracies'.

No confirmation that Australia will adopt a net zero target

In a subsequent press conference, Mr Morrison did not confirm whether Australia would adopt a net zero by 2050 emissions target. Mr Morrison said that:

- Australia would welcome it if the US were to rejoin the Paris Agreeement
- Welcomed comments made during the campaign by Mr Biden which indicated that his views on the role of technology in driving down emissions which the Prime Minister considers to be similar to Australia's position.
- Committed to working with the new administration on the issue of climate change including working with the US on 'technological developments that will see a lower emissions future for the world but a stronger economy as well where we don't say goodbye to jobs we don't have to say goodbye to'.

Private members' Bill

The Climate Change (National Framework for Adaptation and Mitigation) Bill 2020 was introduced as a private members' Bill by Independent Zali Steggal into the House of Representatives on 9 November. Among other things, the Bill would commit Australia to a net zero by 2050 target.

The Bill is covered in more detail in a separate post of this issue of Governance News.

[Sources: Prime Minister Scott Morrison media releases: Statement on the US presidential election; transcript of press conference 08/11/2020; Climate Change (National Framework for Adaptation and Mitigation) Bill 2020]

In Brief | Green led COVID-19 recovery: The NSW government has released a 20 year plan to reduce emissions and grow the state's economy while ensuring cheap and reliable electricity

[Sources: Media release 09/11/2020; Electricity Infrastructure Roadmap 09/11/2020]

In Brief | A Biden presidency won't necessarily mean a huge shift in direction on climate change? BlackRock cautions that if republicans retain their control of the US Senate 'big-ticket legislative actions including large-scale fiscal stimulus and public investment, tax, healthcare and climate related legislation would likely face insurmountable hurdles'. BlackRock predicts that the focus on sustainability will nevertheless increase through regulatory actions, as opposed to tax reform or spending on green infrastructure and through re-joining the Paris Agreement

[Source: BlackRock weekly commentary 09/11/2020]

Protecting infrastructure and systems of national significance: draft legislation released

Following consultation, the government has released draft legislation - [exposure draft] Security Legislation Amendment (Critical Infrastructure) Bill 2020 - for consultation which is intended to strengthen existing protections around Australia's critical infrastructure and systems. The closing date for submissions is 27 November 2020.

Announcing the consultation, Minister for Home Affairs Peter Dutton commented,

> 'The increasingly interconnected nature of critical infrastructure exposes vulnerabilities that could result in significant consequences to our economy, security and sovereignty and industry will be important to the success of these reforms. We will continue to work closely with industry and other stakeholders to implement our plan to secure essential services – electricity, water, groceries and so on – without imposing an unnecessary regulatory burden.'

The proposed reforms are a key initiative of Australia's Cyber Security Strategy 2020.

Some Key Points

The draft legislation proposes to:

- Expand the coverage of the Security of Critical Infrastructure Act 2018 (SOCI Act) to include the following sectors: communications; financial services and markets; data storage and processing; defence industry; higher education and research; energy; food and grocery; health care and medical; space technology; transport; and water and sewerage.
- Introduce a new Positive Security Obligation: Building on the existing obligations in the SOCI Act to embed preparation, prevention and mitigation activities into the business as usual operating of critical infrastructure assets, the Positive Security Obligation involves three aspects. Namely: 1) 'adopting and maintaining an all-hazards critical infrastructure risk management program'; 2) introducing a mandatory requirement to report serious cyber security incidents to the Australian Signals Directorate; and 3) 'where required, providing ownership and operational information to the Register of Critical Infrastructure Assets'.
- Enhance cyber security obligations for 'systems of national significance': Under the Enhanced Cyber Security Obligations, the Secretary of Home Affairs will be able to require the responsible entity for a 'system of national significance' to undertake one or more prescribed cyber security activities. One example given in the draft explanatory memorandum is requiring an entity to undertake cyber security exercises to build cyber preparedness. The purpose of the proposed changes is to 'support the sharing of near-real time threat information to provide industry with a more mature understanding of emerging cyber security threats, and the capability to reduce the risks of a significant cyber attack against Australia's most critical assets'.
- Introduction of a 'government assistance' regime: The Bill proposes to introduce a Government Assistance regime to be used 'as a last resort' to enable the government to step in to 'protect assets during or following a significant cyber attack'.

[Sources: Minister for Home Affairs Peter Dutton media release 09/11/2020; Consultation home page; [Exposure Draft] Security Legislation Amendment (Critical Infrastructure) Bill 2020; [Exposure Draft] Explanatory Document; [Exposure Draft] Intelligence Services Regulations 2020; [Exposure Draft] Explanatory statement]

In Brief | ACCC plans to propose changes to Australian merger laws in 2021: ACCC Chair Rod Sims says that the rapid growth of digital platforms is fuelling world wide debate about the adequacy of existing merger laws

[Source: ACCC media release 06/11/2020]

Not 'fit and proper': The FCA has banned three individuals from working in the financial services industry for non-financial misconduct

The UK Financial Conduct Authority (FCA) has banned three individuals - a financial adviser at an authorised firm and two sole directors of authorised financial advice firms – from working in the financial services industry for non-financial misconduct.

Each individual had been convicted of what the FCA describes as 'serious non-financial indictable offences' while working in the financial services industry. One individual was convicted of making, possessing and distributing indecent images of children. Another was found to have secretly observed and video recorded his tenant having a shower without their consent. The third was convicted (among other things) of sexual assault.

In each case, the FCA determined that banning was appropriate because the individual in question

> 'is not a fit and proper person to perform any function in relation to any regulated activity carried on by any authorised or exempt persons or exempt professional persons. This is because he lacks the necessary integrity and reputation required to work in the regulated financial services sector.'

The final notices outline the FCA's reasoning in more detail in each case. The notices are available on the FCA's website here.

Announcing the regulator's decision, FCA Executive Director of Enforcement and Market Oversight, Mark Steward commented,

> 'The FCA expects high standards of character, probity and fitness and properness from those who operate in the financial services industry and will take action to ensure these standards are maintained.'
>
> [Source: FCA media release 05/11/2020]

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