Governance News

COVID-19 Special Edition

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Diversity

Slow to change: New report tracking trends in board composition, director skills and board refreshment at US publicly listed companies calls on boards to take steps to meet shifting investor expectations

A joint report from The Conference Board, Debevoise & Plimpton, the KPMG Board Leadership Center (BLC), Russell Reynolds Associates, the John L Weinberg Center for Corporate Governance at the University of Delaware and ESGAUGE. tracks changes in board composition, director skills, director turnover and the policies for director election/retirement at Russell 3000 and S&P500 companies over the period 2016 to 2019.

The report concludes that ultimately boards are falling short on a number of fronts, notably on the issues of: diversity of board representation (in the broadest sense); tenure and board refreshment; overboarding; and (especially for smaller companies) governance issues. The report suggests that companies have an opportunity to make adjustments to address these issues, at their own pace, in line with changed investor expectations.

> 'Corporate boards are now at an inflection point. As we entered 2020, boards were facing expanded responsibilities, increased workloads, and greater scrutiny of their composition. That has only increased with the current health, economic, and social crises stemming from the COVID-19 pandemic and the increased focus on race and social injustice. Companies are also on the threshold of generational change in the boardroom, as a large cohort of directors is nearing retirement age. Boards have a window of opportunity to embrace changes in their composition and practices that align with their companies' strategies and meet new investor demands, in a way and at a pace that makes sense for the company based on its individual circumstances'.

Overview: Key findings and suggested steps for boards to consider

Board Diversity

Gender Diversity: Most directors are men

- 13.4% of Russell 3000 companies have all male boards
- Female directors represent 18.5% of the total population of board members in the Russell 3000 (up 4.2% on 2016).
- There have been no all-male S&P 500 boards since 2019, but women account for less than 25% of S&P 500 board members overall.
- Only 4.7% of companies in each of the Russell 3000 and S&P 500 indexes have a female board Chair) and less than 1 out of 5 board committees in the Russell 3000 are led by women.

Ethnic/racial diversity: Most directors are white

- Most companies do not disclose (other than through photographs of individual directors) the ethnic/racial diversity of their directors. In the S&P 500 index, only 59 companies disclosed (whether in text or through charts) the racial/ethnic diversity of individual directors' race (ethnicity).
- Companies in the utilities (32.4%) and financials (21.1%) sectors were the most likely to provide this type of disclosure.
- 78% of the 658 board members whose racial/ethnic diversity was disclosed were identified as white. This does not reflect the makeup of the US general population, 40% of whom do not identify as white.

Director age: Most directors are 61 or older

- In both indexes, at least 60% of board members are age 61 or older, and the share of directors in the 76–80 age range has slightly grown since 2016. In 2016 directors in the 76-80 age bracket accounted for 4.2%, now it's 5%.
- The average age of directors is 63.4 years in the S&P 500 and 62.6 years in the Russell 3000

- Only 9% of Russell 3000 and 6% of S&P 500 board members are in their 40s with younger directors more frequently found on the boards of smaller companies.
- 69.8% of S&P 500 companies and 39.3% of Russell 3000 companies have board retirement policies based on age that enable the board to make exceptions to the enforcement of the policy.
- Only 21.6% of Russell 3000 companies and 36.7% of S&P 500 companies have mandatory director retirement policies based on age that do not enable the board to authorise an exception to the policy. Where this type of policy is used, the retirement age is typically set at 75 years (44.2% of cases in which a mandatory 'no exceptions' policy is in place, or 72 (35.1% of cases).

Director skills: Boards are still looking for directors with prior board experience

- Prior board experience is still highly valued: Overall, only 25% of Russell 3000 and S&P 500 companies reported appointing a director who did not have prior public board experience. This proportion is 'almost identical', the report comments, to the proportion that did so in 2016.
- Director skills: Financial and information technology skills are the skills most frequently mentioned in disclosures. 21.7% of Russell 3000 directors are identified as an 'audit committee financial expert' as per SEC disclosure rules and 13.8% have some form of technology background. In the S&P 500 index of larger companies, 20.9% of corporate directors include technology expertise in their biographical profile.

Advice to boards on increasing board diversity in the broad sense (gender, age, racial, ethnic, skills diversity)

The report suggest that in terms of promoting increased board diversity, companies should:

- assess their own culture to ensure that incumbent directors and management are providing a genuinely inclusive environment
- ensure diversity is an 'integral and ongoing part' of director searches
- 'get ahead of the curve' by increasing disclosure around the diversity of their board by providing narrative information about the background of board members;
- look outside the C-suite and those with prior public company board experience when recruiting new directors and taking steps to ensure their success by having support mechanisms in place

Tenure

- US directors tend to serve longer on boards than directors in other jurisdictions. For example, the average tenure for seated directors is 9.7 years in the larger companies of the S&P 500 index and 9.5 years in the Russell 3000 index overall. In contrast, the average tenure of directors at the largest companies in the United Kingdom's FTSE index is 4.1 years.
- 21.6% of Russell 3000 departing directors had served on the board for more than 15 years before stepping down in 2019, rising to 26.3% in the S&P 500.
- The longest median tenures of departing board members are seen in the financials (10.7 years) and utilities (10.5 years) sectors. The shortest median tenures are in the health care (6.2 years) and energy (7.4 years) business sectors.
- Director retirement policies based on length of tenure remain rare with only 5.6% of S&P 500 companies and 3.3% of Russell 3000 companies having such policies in place.

Advice for boards

The report argues that there is benefit for boards in having a combination of long serving and newer directors. Boards are advised to:

- actively consider how best to achieve the appropriate balance of tenures
- disclose this to investors
- consider adopting average tenure/other policies to 'encourage a healthy level of turnover but avoid the shortfalls of rigid term limits'.

Overboarding

- Policies putting a limit on the number for-profit directorships their board members can accept (overboarding policies), most usually limiting the number of outside directorships to three or four, are in place at 66.7% of S&P 500 companies (up from 64.4% in 2016) and 43.9% of Russell 3000 companies (slightly up from 42.2% in 2016).
- 80.4% of larger companies (companies with annual revenue of $50 billion or more) have overboarding policies in place with the proportion decreasing in line with the size of the company. Only 15% of companies with annual revenue under $100 million have an overboarding policy.
- Companies in the utilities sector are the most likely to report having an overboarding policy in place (61.3% of Russell 3000 companies in the utilities sector). In contrast, in the financial services sector, only 38.8% of companies have this kind of policy in place.
- A minority of companies apply more stringent rules to their CEOs (as compared with the rules for their other directors). In the S&P 500, 23.8% of companies and in the Russell 300 17.1% of companies specific policies to prevent the overboarding of their CEO. In most cases (56.4% in the Russell 300) CEOs are limited to taking on an additional two board seats. At utilities firms – the utilities sector has the highest incidence of policies – 21% of policies limit the CEO to taking on as many as three additional directorships.

Advice for boards

The report comments that pressure from institutional investors to take steps to address the issue of director overboarding has intensified over the past year, and looks set to continue to do so. This is especially the case, the report argues given directors' responsibilities are likely to continue to expand in the current environment. On this basis, the report suggests that to avoid adverse votes and/or 'other reputational repercussions' companies would be well advised to:

- familiarise themselves with the thresholds set by institutional investors/proxy advisory firms;
- reassess their policies/practices in this area;
- consider proactively engaging with large investors on the issue of overboarding; and
- factor consideration of the 'bandwidth of individual directors' into their nomination, annual performance evaluation, and committee assignment processes.

Director turnover

- 46.2% of Russell 3000 companies and 40.1% of S&P 500 companies disclosed no changes in the composition of their board of directors over the last disclosure year.
- About one-third of companies in both indexes added a new director or replaced one board seat in the previous 12 months.
- Only 8.6% of companies in the Russell 3000 had three or more new incoming directors.
- The report comments that 'director retirement seems to be the only relevant factor dictating the pace of change and board turnover'.

Advice for boards

The report suggests that in light of the increased focus on board diversification (diverse skills and professional backgrounds, gender, racial/ethnic representation etc) and in light of the fact that 40% of Russell 3000 directors are 66 and have been in their roles for more than 12 years, it would be prudent for boards to ensure they have a 'sound board succession plan' and a 'rigorous director evaluation process' tied to the company's strategic objectives in place.

The report also suggests that a 'consensus on turnover' could also help inform discussions around improving board diversity, tenure and overboarding.

Director elections/board structure: Smaller companies tend to retain classified structures and to use some form of plurality voting

- The report found that some form of plurality voting is found in 81.3% of Russell 3000 companies with annual revenue under $100 million and in 66.3 % of those with annual revenue in the $100 million–$999 million bracket.

  [Note: The report explains that plurality voting operates by default under Delaware law unless the company opts otherwise through its charter or bylaws. Under the standard, uncontested nominees who receive the most "for" votes are elected to the board until all board seats are filled, even if a majority of shares are voted against those individuals. In some cases, companies have adopted the 'plurality plus' standard, under which directors who received more 'withhold' votes than 'for' votes must formally tender their resignation to the board.]

- A majority of companies in both indexes now elect members of their boards of directors annually. However, classified boards are still found at 41.2% of Russell 3000 companies (down from 43.2% in 2016) and 10.9% of S&P 500 companies (down from 15.4% in 2016).

Advice for boards

The report suggests that in light of the fact that some investors (eg CalPERS) are targeting governance issues at smaller firms, boards (especially boards of smaller companies) should:

> 'take a careful and holistic look at changing their director election practices. While plurality voting and staggered boards can be seen as protections against activism…they can also invite activism. Staggered boards can also serve as an impediment to board refreshment, and companies may wish to consider shifting to annual elections if it helps them adjust the composition of the board in a way that keeps pace with strategic needs'.
>
> [Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 18/10/2020; Full text of the report: Corporate Board Practices in the Russell 3000 and S&P 500: 2020 Edition]

JP Morgan has announced a $30m commitment to progress racial equity

JP Morgan has committed to fund $30 billion worth of projects over the next five years to 'drive an inclusive recovery support employees and break down barriers of systemic racism'. The banks' progress will be 'tracked regularly and shared with senior leadership' within the bank and 'externally with the Chase Advisory Panel'.

Commitments include the following (among others).

- Workforce commitments:
  - Building a more 'equitable and representative workforce': The bank has committed to holding executives more accountable achieving firm-wide diversity representation targets through strengthening the way the bank incorporates diversity and inclusion priorities and progress into year-end evaluations and compensation decisions for members of the operating committee and their direct reports.
  - Roll out a new program to upskill and reskill the bank's global workforce: The program will provide employees, including frontline and call-centre staff with access to a range of high-demand credential and certificates, bachelor's and master's degree programs.
  - Paid leave to vote: Provide all US employees, including those in branch and customer service positions, with paid time off to vote as part of the Time to Vote coalition
- Supplier diversity: The bank will spend an additional $750 million with Black and Latinx suppliers.
- Access to housing:
  - Improve access to home ownership for Black and Latinx households: The bank has made a number of commitments to fund measures to assist Black and Latinx households to secure a mortgage and/or to get a better deal on their existing mortgages. For example, over the next five years, the firm plans to originate an additional 40,000 home purchase loans for Black and Latinx households and to advocate for housing reform to increase access to home ownership.
  - Affordable rental housing: The bank will finance an additional 100,000 affordable rental units in communities where they are most needed.
- Support Black and Latinx small business: The bank will provide an additional 15,000 loans to small businesses in majority-Black and -Latinx communities by delivering $2 billion in loans and advocate for small business administration (SBA) reforms and new COVID-19 aid.

- **Improve access to banking services:** The bank will invest in improving access to low cost banking services for Black and Latinix communities through hiring 150 new community managers and opening new community centre branches in underserved communities. The bank will also increase its marketing spend to reach more 'underserved, unbanked or underbanked' customers.
- **Support Black and Latinx-led Financial Institutions:** The bank will invest up to $50 in Black and Latinx-led Minority Depository Institutions (MDIs) and Community Development Financial Institutions (CDFIs).

[Source: JP Morgan Chase media release]

Starbucks has committed to publicly reporting on progress towards the achievement of its diversity goals and to tying executive pay to the achievement of diversity targets

Starbucks has announced a range of new diversity and inclusion (D&I) commitments to increase the representation of Black, Indigenous and People of Colour (BIPOC) across the organisation.

Commitments include (among others):

- Publicly disclosing data on the diversity of the company's current workforce.
- Setting and tracking progress against a target for least 30% of roles at all corporate levels and 40% of all retail and manufacturing roles by 2025 to be held by BIPOC employees.
- Setting annual diversity and inclusion goals based on retention rates and progress towards the 2025 BIPOC target.
- Publicly reporting on diversity and inclusion commitments, goals and progress through annual reporting.
- Rolling out anti-bias training for executives.
- Incorporating measurements focused on building inclusive and diverse teams into executive compensation programs from FY21.
- Establishing Inclusion and Diversity Executive Council in Q1 FY21 to provide internal governance to integrate inclusion and diversity throughout the company.

[Sources: Starbucks media release 14/10/2020; Full list of diversity and inclusion commitments; Letter to partners; Diversity data]

Disclosure and Reporting

The FRC has floated proposals to radically rethink corporate reporting

Key Takeouts

- The UK Financial Reporting Council (FRC) has released a discussion paper floating ideas for the overhaul of the current ineffective reporting model with a view to making reports more effective, flexible and useful to stakeholders.
- Broadly speaking, the paper puts forward three suggested changes: 1) the replacement of the existing single annual report with a multi-report model whereby companies would produce (as a minimum) a business report, a financial statements report and a new public interest report; 2) a shift away from writing to meet the needs of particular stakeholders (generally investors) towards an objective based, stakeholder neutral reporting model where the focus in on effective communication; and 3) harnessing technology to enable greater flexibility, provide greater connectivity between reports and enhance navigability of reports.
- The aim of putting forward these ideas the FRC states, is ultimately to 'create a blueprint for a corporate reporting system of the long term, up to 2030' and the proposals put forward in the discussion paper are intended to be the start of this process.
- The deadline for submissions is 5 February 2021.

The UK Financial Reporting Council (FRC) has released a discussion paper – A matter of principles: The Future of Corporate Reporting – outlining ideas to radically rethink the current outmoded approach to corporate reporting with a view to making it more effective, flexible and useful.

The aim, the FRC states, is ultimately to 'create a blueprint for a corporate reporting system of the long term, up to 2030' and the proposals put forward in the discussion paper are intended to be the start of this process.

Announcing the release of the discussion paper, FRC Executive Director of Regulatory Standards, Mark Babington said:

> 'As the UK's corporate reporting framework has evolved, annual reports have become a vehicle of convenience for ever-more information, however, this has undermined their purpose and usability. The future of corporate reporting discussion paper proposes a more agile approach that is responsive to the needs of users of accounts. To build trust in business we need a modern corporate reporting system that is transparent, flexible and puts users of corporate reporting at its heart.'

Commenting on how the proposed overhaul of corporate reporting fits with transformation of the FRC into the Audit Reporting and governance Authority (ARGA) and the recommendations of the Brydon Review, FRC CEO Sir John Thomspon writes, that 'a system for corporate reporting underpins audit and therefore, we see this as the right time to discuss what the future of corporate reporting should look like'.

The deadline for submissions is 5 February 2021.

What's being proposed?

Broadly speaking, the report proposes three major changes.

1. The replacement of the existing annual report with a multi-report model

In the interests of addressing the issue of overly lengthy, complex and ineffective annual reports, the FRC suggests replacing the existing single annual report with a 'network' of reports.

This would mean that instead of producing a single annual report, companies would produce at least three mandatory reports:

- **A Business Report** designed to 'provide information enabling readers to understand how the company creates long-term value in accordance with its stated purpose'. The FRC suggests that this would be similar to a 'concise strategic report' and include financial and non-financial information.
- **A mandatory financial statements report:** The FRC proposes that companies would be required to publish a standalone Financial Statements report which would include the 'full set of financial statements, prepared in accordance with the applicable framework for financial reporting and subject to audit'. The objective of introducing this requirement is to 'provide information about the financial position, financial performance and cash flows of a company that is useful in making economic decisions'.
- **A mandatory 'public interest report':** The FRC proposes to introduce a new 'public interest report' to create 'a level playing field for nonfinancial information and elevat[e] the needs of the public'. More particularly, the FRC states that the objective of this new report is to 'provide information that enables users to understand how the company views its obligations in respect of the public interest, how it has measured its performance against those obligations and to provide information on future prospects in this area'.

  The FRC comments that for some companies the Public Interest Report will bring together different aspects of existing reporting, but acknowledges that for others it will be a 'step change in the non-financial information they provide. Section 6 of the discussion paper includes more detail around the content that the FRC proposes would be included in a Public Interest Report.
- **(Potentially) other standalone 'network' reports** as appropriate to provide additional detail on information contained in the Business Report and information on specific issues.

This approach, the FRC states,

> 'unbundles existing reporting and recognises that more informative corporate reporting is better achieved through a number of interconnected reports with clearly defined communication objectives for each'.

2. Reports would not be written for particular stakeholder groups but rather written to meet agreed objectives in accordance with shared principles

The FRC proposes a shift away from the current model of reporting where individual reports are written for a particular primary user group (generally investors) towards an objective based reporting model where the focus in on effective communication. The FRC states,

> 'We propose to move from a system based on the perceived needs of a single set of primary users and with a single objective, to a corporate reporting framework that takes account of the different communication objectives which stakeholders, including shareholders, have when considering companies' corporate reporting'.

To maintain 'cohesiveness across different disclosures', 'establish information adequacy' and promote effective communication the FRC proposes development a common set of principles for all types of corporate reporting.

Figure 1 at p8 of the report provides a graphic representation of the shift in approach that the FRC envisages overall and may be helpful in understanding how these proposals contribute to the FRC's aim of achieving a more effective reporting model/approach.

3. Increased use of technology

The FRC envisages that a future model of corporate reporting will 'encourage innovation to improve the accessibility of information for users and focus on electronic communication'. 'In the new model, technology will be used to connect the reporting network and bring together information communicated by companies' the FRC states..

Section 7 of the report at p28 of the report outlines how technology might be used to enhance reporting, though the FRC acknowledges that more work is needed to develop and explore options.

Response

In a statement, The Association of Chartered Certified Accountants' (ACCA) Head of Corporate Reporting Richard Martin welcomed the focus on non-financial reporting and the forward-looking nature of the proposals. Mr Martin said,

> 'It's very positive to see that the FRC's DP [discussion paper] definition of corporate reporting recognises the importance to inform through corporate reporting the wider stakeholders in addition to shareholders and investors. It is also very positive to note that the DP emphasises the importance of non-financial reporting'.

On this issue, Mr Martin said that the FRC's work complements the work being undertaken by a number of other groups (eg European Commission, World Economic Forum, the Statement of Intent from the group of 5 and from the IFRS Foundation) on non-financial reporting standards and content. Mr Martin commented,

> 'This piece from the FRC considers more how changes to the structure / form of that reporting [non-financial reporting] might help to improve it. It is therefore complementary, but of course there are areas of overlap with these other initiatives such as the intended audience and assessing materiality. The proposals appear to be rightly looking forward and thinking about longer term developments and so is not responding to some of the more specific issues from the Brydon report for example. ACCA will be responding in full and formally in due course and this will be published in the public domain.'

[Sources: FRC media release 08/10/2020; FRC discussion paper: Future of Corporate Reporting October 2020; ACCA global media release]

Reporting on how stakeholder interests are being factored into company strategy and decision making: The FRC has released 'tips' to guide companies in understanding what information investors are looking for and how to present it in the most effective way

The UK Financial Reporting Council has released a set of suggested 'tips' to assist companies in the preparation of their section 172 statements based on feedback from companies, investors and other stakeholders about what information they would find most helpful.

Announcing the release of the guidance, FRC Lab Director, Phil Fitz-Gerald commented,

> 'The requirements for the Section 172 statement have continued to shine a light on the importance of a company's stakeholders and we are pleased that boards are increasingly discussing these matters, particularly during the challenges they are currently facing with COVID-19. Section 172 is not just about stakeholders and engagement with them, but about how directors are considering them and other matters in pursuit of the company's success. We hope the tips can help companies as they start planning their next statements'.

The table below provides a snapshot of some of the key points. The full text of the FRC's tips can be accessed here.

FOCUS AREA	FRC'S 'TIPS' FOR MORE EFFECTIVE REPORTING
Purpose of the statement	▪ The FRC calls on companies to bear in mind that: – Section 172 statements were introduced in response to concerns that boards were not paying sufficient attention to their responsibilities towards both shareholders and stakeholders. – 'Section 172 should be embedded in the directors' strategic decision making and supported by the company's culture – it is important that boards set the tone at the top, and companies should report on what they do'. ▪ A flat statement of compliance with the s 172 requirements is insufficient. Rather, the statement should explain how the board have exercised their duty and considered stakeholders and the long term success of the company in their decision making, 'even where decisions or engagement may have been carried out centrally by the group in the case of some subsidiaries'. ▪ The statement should consider all the requirements of s172 keeping in mind that investors are 'particularly interested in the promotion of the success of the company the consequences of decisions in the long term'.
What information to include and how to make sure that it is useful	▪ No boilerplate: The statement should be 'specific and genuine' and avoid 'box ticking'. ▪ Consistent: Reporting on section 172 should be consistent with the rest of the annual report 'and considered in the context of the company's story, as a whole, without contradictory information'. ▪ Linked to strategy: Statements should link back to the company's strategy and include discussion of what bearing stakeholder and other matters have had on the company's business model and the development/implementation of business strategy ▪ The statement should explain: – how the company met the s172 requirements; – what is relevant to the particular company; – what happened during the year and, – where applicable, what the board and management plan to do in future.

FOCUS AREA	FRC'S 'TIPS' FOR MORE EFFECTIVE REPORTING
	▪ Statements should provide investors with insight into how the board has exercised its oversight function and how the board has challenged management around stakeholder issues eg how issues are escalated to the board, the extent of training of the board on stakeholder issues and how the effectiveness of complaints/grievance mechanisms is assessed. ▪ Statements should include 'where material' KPIs on key stakeholders that are monitored by the board eg net promoter scores. ▪ When setting out the engagement undertaken and decisions made, companies should disclose the implications of the feedback received, the impact of decisions on relevant stakeholders and what actions have been taken or are planned as a result. ▪ Where the statement highlights issues or concerns raised by a stakeholder, it should be clear how they have been or are going to be addressed.
How to approach the process of preparing the statement	▪ Preparation should take place over the course of the year: The FRC suggests that companies should keep a note of key decisions and engagement activities over the which could be considered for inclusion in the statement as they happen over the course of the year, rather than attempting to compile the information at the end of the year. The FRC suggests that this approach could help companies and boards consider the extent of their direct involvement and activities, and whether a change or more is needed. ▪ Consider including prompts: The FRC suggests companies could consider amending templates for board agendas, papers and minutes to include reminders/prompts for the board and management to consider which stakeholders are relevant for decisions. This will both help ensure stakeholder interests are considered/provide evidence that they are being considered and make it simpler to assess what to include in s172 statements the FRC suggests.
How to present the information so that it makes sense	▪ The FRC calls on companies to ensure the statement is 'clearly labelled and referred to in the contents page of the annual report'. ▪ The FRC encourages the use of clear, pinpoint cross-referencing (including hyperlinks) to expand on points made in the statement and provide further context, to enhance understanding and aid navigation. However, the FRC cautions against using cross referencing to 'make the statement a contents page of a list of links. While cross-referencing is helpful, the statement should still provide a coherent message by itself'. ▪ The FRC also encourages the use of examples/case studies of significant strategic decisions taken over the course of the year to illustrate how stakeholder interests were taken into account.

[Sources: FRC media release 14/10/2020; Tips to help companies make Section 172 statements more useful]

Meetings and Proxy Advisers

Top Story | Permanently allowing virtual AGMs and electronic execution of documents: Draft legislation released for consultation.

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 has relased draft legislation for a short consultation period which proposes to 'make permanent and expand on' them.

Key Takeouts

- The government is consulting on draft legislation which proposes to 'make permanent and expand on' the temporary changes to execution and meeting requirements implemented in response to the COVID-19 pandemic.
- Broadly, the draft Bill proposes to allow: a) electronic execution of company documents (including deeds) and documents relating to meetings; b) meetings to be held as virtual or hybrid meetings; c) notice of meetings and other documents relating to meetings to be communicated to prospective attendees electronically; and d) minutes to be recorded, kept and stored electronically.
- The draft Bill proposes to introduce a new requirement for the minutes of electronic meetings of shareholders and members of registered schemes to 'include any questions or comments submitted by a shareholder or member (before or during the meeting)'.
- It's proposed that new rules relating to electronic execution and electronic meetings (with the exception of changes relating to the time and place of meetings) will apply as mandatory rules rather than replaceable rules.
- The deadline for submissions is 30 October.

Overview

On 19 October, Treasury released draft legislation – [exposure draft] Corporations Amendment (Virtual Meetings and Electronic Communications) Bill 2020 and draft explanatory materials – for consultation, proposing to both 'make permanent, and expand upon', the temporary changes to execution and meeting requirements in Corporations (Coronavirus Economic Response) Determination (No. 3) 2020.

Consultation on the proposed changes closes on 30 October.

Rationale for the proposed changes

The draft explanatory materials state that,

> 'The objective of reform is to ensure that companies are able to use the most efficient mix of technologies to deliver on substantive corporate governance outcomes. These reforms will assist companies to more efficiently communicate with their shareholders and facilitate greater transparency between shareholders and directors'.

The draft explanatory materials also comment that temporary changes introduced because of the COVID-19 pandemic, provided an opportunity to test the changes and the government has had feedback that the impact has been positive.

> 'Companies have embraced the use of electronic means and alternative technologies to hold meetings and execute company document. The use of these technologies has resulted in regulatory savings for industry and increased productivity. There is now an opportunity to permanently modernise the relevant provisions in the Corporations Act in a way that preserves members' rights to participate'.

What's being proposed

Broadly, the Bill proposes to allow:

- electronic execution of company documents (including deeds) and documents relating to meetings
- meetings (meetings of directors of a company, meetings of shareholders of a company (including Annual General Meetings) and meetings of members of a registered scheme) to be held as virtual or hybrid meetings;
- notice of meetings and other documents relating to meetings to be communicated to prospective attendees electronically
- minutes to be recorded, kept and stored electronically.

Further detail on the proposed changes

Enabling electronic execution of documents

If legislated, the proposed changes would mean that:

- company documents (documents executed without a common seal, documents executed with a common seal and deeds) could be executed electronically.
- where a company executes a document by fixing a common seal, the persons witnessing the fixing of the seal could do so remotely by: a) observing the fixing of the seal via videoconferencing; b) signing the document electronically or physically; and c) 'annotating the document' with a statement confirming that they have observed the fixing of the seal by using electronic means. The draft explanatory materials comment that this is intended to ensure that 'the rules relating to the execution of company documents using a common seal are not more restrictive than the rules relating to the execution of company documents without a common seal'.
- in circumstances where the signatures of more than one director or secretary is required, the directors/secretary could:
  - sign different copies or counterparts of the document provided it included the entire contents of the original document. The draft explanatory materials comment that this proposed change 'reverses the effect of the court's decision in Adelaide Bank v Pickard [2019] SASC 13 where it was held that all persons needed to sign the same single, static document'.
  - receive and sign an electronic copy of the document provided that: a) the copy provided to them includes the entire contents of the document; b) they confirm by 'means of an electronic communication' (eg by email) that they have signed the document; and c) that they identify themselves and 'indicate their intention using a method that is as reliable as appropriate for the purposes for which the company is executing the document or proven in fact to have indicated the person's identity and intention'.
- documents relating to a meeting (paragraphs 1.32-1.40 of the draft explanatory materials list the types of documents covered) could also be signed electronically by using a method to identify the signatory and indicate the signatory's intention. Consistent with the proposed approach to the execution of company documents, it would not be necessary that for all signatories to sign the same document.

Enabling virtual and hybrid meetings

If legislated, the proposed changes would mean that directors meetings, meetings of shareholders of a company and meetings of members of a registered scheme could be held electronically, subject to all participants having a reasonable opportunity to participate.

The draft explanatory materials comment that similar amendments are proposed in Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 to enable meetings conducted in the context of external administration, including meetings of creditors and committees of inspection to be held electronically.

Place and time of virtual and hybrid meetings

If legislated, the proposed changes would mean that the place and time at which meetings are taken to have occurred will depend on the meeting format.

- Virtual meetings: For virtual meetings (ie meetings where 100% of participants attend electronically rather than physically), it's proposed that the place of the meeting would be the address of the registered office of the company or responsible entity of a registered scheme. The time for the meeting would be the time at the address of the registered office.

- Hybrid meetings: For hybrid meetings (ie meetings where some members attend physically and other attend virtually), it's proposed that the place and time for the meeting would be the place where the members physically attend and the time at that location. Where there is more than one physical location, the place of the meeting would be main location (as specified in the notice for the meeting) and the time would be the time at the main location.

Timing of meetings

In terms of the timing of meetings, it's proposed that meeting be required to be held at a time that is 'reasonable' at the place where the meeting is being held. The draft explanatory memorandum comments that this 'may not necessarily be a convenient time for all of the shareholders or members who are attending using technology, in the same way that face to face meetings may be held at a time that is not convenient for all shareholders or members'.

Contents of the notice of meetings

If legislated the changes will mean that for hybrid or virtual meetings, the notice of meeting will need to include 'sufficient information' to allow those entitled to attend to participate using the virtual meeting technology. The draft explanatory materials suggest that this could include dial in details or a link to the relevant website.

The notice would also need to specify the main location of the meeting (where there is more than one physical location).

Conduct of meetings

If legislated, the proposed changes will mean that:

- meeting attendees whether attending physically or electronically will be taken to be 'present' at the meeting and counted for the purposes of determining whether there is a quorum.
- documents could be tabled at a meeting held in electronic format by providing them to all persons entitled to attend either before or at the meeting.

Voting

If legislated, the proposed changes will mean that:

- all participants entitled to vote must be given the opportunity to do so 'in real time' or 'if it is practicable for the company in advance of the meeting'. The draft explanatory materials make it clear 'it is not expected that companies would provide a method for voting in advance of the meeting for director's meetings'.
- where meetings are held in electronic format, votes will be required to be taken on a poll (not a show of hands).

Enabling electronic communications about meetings

If legislated, the proposed changes would mean that:

- Certain documents relating to a meeting (whether the meeting is held electronically or physically) could be communicated electronically (eg via email) where it is 'reasonable to expect that the document would be readily accessible so as to be usable for subsequent reference at the time that it is given' and where the sender has a nominated electronic address for the recipient.
- The types of documents that could be given/signed electronically include:
  - 'documents in which a person makes a request in relation to a meeting' eg giving notice of a resolution under s249N or 252L of the Corporations Act;
  - notices of directors meetings, shareholders' meetings, and meetings of members of a registered scheme
  - notices of a resolution or a record of a resolution
  - notices of 'a statement in relation to a meeting or a matter to be considered at a meeting may be provided and signed electronically' eg a members' statement distributed under sections 249P or 252N.
  - documents relating to a proxy, eg documents to appoint a proxy or a list of persons who are willing to act as a proxy

- questions for auditors and responses to them
- minutes eg including under existing subsections 251A(2)-(4) and 253M(2) (signing minutes) and subsections 251B(3)-(4) and 253N(3)-(4) (providing copies of minutes)

- Resolutions made without a meeting and all documents that relate to the making of those resolutions as per Division 1 of Part 2G.1 (for directors' resolutions and declaration) or Division 1 of Part 2G.2 (for resolutions of proprietary companies) would also fall into this category.
- Documents would be required to be sent either to the recipient's nominated electronic address or to 'another electronic address that the sender believes on reasonable grounds to be the person's electronic address'. In the alternative, senders would be able to provide recipients with sufficient details to enable them to download the document. The draft explanatory memorandum suggests that this could be done by giving them a card or sending them an email with a link to a website.

Time of receipt and dispatch

- It's proposed that new default rules would apply for determining when an electronic communication has been sent and when it has been received.
- It's proposed that the time at which a communication has been sent will depend on 'whether the communication leaves the information system that is under the control of the originator (or the party who sent it on behalf of the originator)'. This will mean that:
  - Where a communication is being sent to external recipients (ie where the communication leaves the sender's information system) the time at which the communication is sent would be the time that the communication left the sender's information system and not the time it enters the recipient's information system. The draft explanatory materials suggests that this would generally cover communications from companies to shareholders for example.
  - For internal communications (ie where a communication does not leave the sender's information system) the electronic communication is sent at the time that it is received by the addressee. The draft explanatory materials suggest that this would cover correspondence sent within a company.
- It's proposed that the time at which a communication has been received will be when the electronic communication becomes capable of being retrieved by the addressee's nominated email address.

Minutes of meetings

If legislated, the proposed changes would mean that:

- The minutes for meetings of shareholders and members of registered schemes could be taken, kept and stored electronically.
- Where minutes are stored electronically, they will need to be open for inspection at the same place where a hard copy would have been required to be retained under sections 251A or 253M of the Corporations Act. The draft explanatory memorandum suggests that this will usually be the 'registered office, principal place of business or another place approved by ASIC'.

The proposed changes would also introduce a new requirement for the minutes for electronic meetings of shareholders and members of registered schemes to 'include any questions or comments submitted by a shareholder or member (before or during the meeting)'. Shareholders and members of registered schemes will then be able to access these minutes under s251B and 253N of the Corporations Act.

Mandatory rules

It's proposed that the new rules relating to electronic execution and electronic meetings (with the exception of changes relating to the time and place of meetings) will apply as mandatory rules rather than replaceable rules.

The draft explanatory memorandum comments that,

> 'This ensures that all companies have the power to hold meetings virtually and execute company documents electronically if they elect to do so. As the rules are facilitative in nature, they do not preclude companies from conducting meetings or executing documents using traditional means'.

Mandatory review

The draft Bill includes provision for a mandatory review of the effectiveness of the changes 'as practicable after the end of five years after the new rules apply' and that a written report must be prepared.

> [Sources: Treasury media release 19/10/2020; Exposure draft Bill: Corporations Amendment (Virtual Meetings and Electronic Communications) Bill 2020 No. , 2020; Draft explanatory materials]

Recent AGM results: BHP, CSL, Cleanaway, Origin

BHP Group Ltd AGM

BHP's AGM was held as a virtual meeting in Australian on 14 October. The meeting of shareholders of BHP group Plc was held in London on 15 October. All board supported resolutions were carried.

Remuneration report: The resolution to approve the 2020 Remuneration report was carried with 95.67% of votes in favour (4.33% against). CalPERS voted in support of the remuneration report.

Election/re-election of directors: All directors standing for election/re-election were elected. All were elected with over 98% of votes in favour of their re-election. CalPERS voted in support of all directors standing for election/re-election with the exception of Susan Kilsby (who has served on the board since April 2019 and is Chair of the Remuneration Cottee and a member of the nomination and governance Committee).

Shareholder ESG resolutions

Neither of the two shareholder resolutions were supported by the board, and neither were carried. The rationale for the board's recommendation against the resolutions is explained in the Notice of Meeting.

The special resolution seeking to amend the constitution received 9.6% support.

The contingent ordinary resolution calling on the company to review the advocacy activities undertaken by its industry associations related to economic stimulus measures in response to COVID-19 restrictions, and to suspend membership of industry associations whose activities and lobbying are not in line with the company's commitment to the Paris Agreement (industry lobbying resolution) was not put to the meeting. The resolution received 22.4% proxy support ahead of the meeting.

A third shareholder resolution (cultural heritage resolution) was withdrawn ahead of the meeting after First Nations Alliance reached agreement with BHP (see: Governance News 14/10/2020 at p11)

CalPERS voted in support of the constitutional amendment but against the lobbying resolution.

In a statement commenting on the results, the Australasian Centre for Corporate Responsibility (ACCR) Director of Climate and Environment Dan Gocher said,

> 'Despite telling its shareholders for three years that suspension of membership of any industry association was simply not workable, last week BHP did just that. With this vote, investors have demonstrated to BHP that they remain focused on the impact of its industry associations on both Australian democracy and on climate action. The advocacy by key BHP industry associations throughout the COVID-19 pandemic has been fundamentally at odds with the Paris Agreement's goals…Shareholders must keep up the pressure to ensure that BHP's industry associations cease to be an obstacle to climate action.'

Questions to the BHP board: According to Market Forces, a number of questions to the BHP board at the meeting were focused on how BHP will meet its Paris commitments, and how it current strategy/actions align with these commitments.

> [Sources: BHP ASX announcements: BHP results of AGM; Speeches; Notice of Meeting; CalPERS voting decisions; Market Forces media release 14/10/2020; ACCR media release 14/10/2020]

Cleanaway Waste Management Ltd AGM

Cleanaway's AGM was held as a virtual meeting on 14 October. All resolutions considered at the meeting had board support and all were carried.

Remuneration report: The resolution to approve the remuneration report was carried with 89.74% support (10.26% votes against).

Resolutions granting performance rights to Cleanaway CEO Vik Bansal were withdrawn ahead of the meeting with Mr Bansal's agreement. This followed the decision to apply a 25% reduction to Mr Bansal's short term incentive plan to take into account: a) the financial impacts of COVID-19 on the business/challenges faced by Cleanaway as a result of the pandemic; b) the impact of COVID-19 on the Australian community; c) 'operational challenges faced by team members'; and d) 'concerns identified by the Board in relation to Mr Bansal's behaviour over this period'.

The board's full reasons for withdrawing the resolutions are outlined in the company's 24 September statement.

A resolution to increase the non-executive director fee pool was carried with 99.70% of votes in support.

CalPERS voted against the remuneration report.

Election/re-election of directors: Phillipe Etienne and Terry Sinclair were each re-elected to the board with 98.55% and 95.27% of votes in support respectively. Sarah Hogg was elected to the board with 99,93% of votes cast in support.

CalPERS supported the election of Sarah Hogg to the board, but voted against the re-election of both Mr Etienne and Mr Sinclair.

[Sources: ASX Announcements: Results of Meeting; AGM Addresses; CalPERS voting decisions]

CSL Ltd AGM

CSL's AGM was held as a virtual meeting on 14 October. All resolutions considered at the meeting had board support and all were carried.

Remuneration report: The resolution to approve the remuneration report was carried with 93.73% support (6.27% votes against).

A resolution to approve the grant of performance shares to CEO and Managing director Paul Perreault was received 76.35% of votes in support (23.65% of votes against).

CalPERs voted in support of both resolutions.

Election/Re-election of directors: Ms Carolyn Hewson and Pascal Soriot were each elected as directors with 99.36% and 99.07% of votes in support (including CalPERs) of their elections respectively.

Mr Bruck Books was re-elected to the board with 98.6% of votes in support. CalPERs voted against his re-election.

[Sources: ASX Announcements: Results of Meeting; Chair's Address to shareholders; CalPERS voting decision]

Origin Energy Ltd AGM

The Original AGM was held virtually on 20 October. All board supported resolutions were carried.

Remuneration report: The resolution to approve the remuneration report was carried with 83.79% support (15.23% votes against). CalPERs voted in support of the resolution.

The resolution to approve equity grants to Origin Managing Director and CEO Frank Calabria under a revised long term incentive plan was withdrawn prior to the meeting in response to shareholder feedback. Origin's reasons for withdrawing the resolution are detailed in the company's 5 October statement here.

Election/re-election of directors: Maxine Brenner was re-elected as an independent non-executive director with 93.09% support.

CalPERS voted against Ms Brenner's re-election.

Shareholder ESG proposals

The three shareholder resolutions (submitted by the Australasian Centre for Corporate Responsibility) were not supported by the Origin board, and were not carried.

The board's reasoning is set out in the notice of meeting here.

The special resolution seeking to amend the constitution received 9.16% support.

Two contingent ordinary ESG resolutions – the first calling on Origin's board to commission an independent review into the processes undertaken by its predecessors to secure the informed consent of Traditional Owners to fracking in the Betaloo sub basin and to make a summary of the report publicly available by June 2021 (consent to fracking resolution) and the second calling on the Origin board to review the advocacy activities undertaken by its industry associations related to economic stimulus measures in response to COVID-19 restrictions, and to suspend membership of industry associations whose activities and lobbying are not in line with the company's commitment to the Paris Agreement (industry lobbying resolution) – were not put to the meeting.

The consent to fracking resolution received 11.8% proxy support and the industry lobbying resolution received 25.25% proxy support.

In his address to shareholders, Origin Chair Gordon Cairns commented briefly on Origin's engagement with Traditional Owners in the Northern territory, noting that 'this is the third year in a row we have had resolutions of this nature at our AGM'. Mr Sargent reiterated that the company's activities in the Betaloo basin are being undertaken with the agreement and support of the Traditional Owners.

> 'I am very confident in the way we engage with Traditional Owners with our processes for engagement guided by the principles for free, prior and informed consent.

Support for the shareholder resolutions

CalPERS voted in support of the constitutional amendment but against the two ordinary shareholder resolutions.

BlackRock voted against the proposed constitutional amendment and the consent and fracking resolution, but for the industry lobbying resolution.

BlackRock states that it voted against the special resolution to amend the constitution on the basis that,

> 'BlackRock is not generally supportive of this type of constitutional amendment resolution, as the relative ease of the filing process increases the risk that these types of proposals are potentially distracting, time-consuming or are submitted by shareholders whose interests may not be necessarily aligned with those of the broader shareholder base'.

BlackRock voted against the consent and fracking resolution on the basis that: a) it considers that 'Origin has demonstrated adequate business practices related to its fracking operations, based on our analysis of the company's disclosures and our engagement, and has made appropriate efforts to procure consent from the Native Titleholders'; b) Origin has engaged and obtained consent from the Northern Land Council 'which requires spending considerable time and resources to ensure adequate knowledge of the fracking process amongst the community'; c) the major opponents of the project do not have rights over the land operated by Origin; and d) the proposal is overly prescriptive in light of the timeframe (30 June 2021) given for publication of the report.

BlackRock voted for the industry lobbying resolution despite the fact that the 'company has demonstrated leadership among its peers regarding the transparent management of its industry associations' as a means of signalling the 'importance of the opportunity for Origin to continue to use its leadership position to constructively encourage its trade associations to further advance the global energy transition'.

BlackRock comments,

> 'The company argues that it can influence the position for its industry associations by remaining a member. Given the reputational risk to the company of misalignment in public positions on key strategic policy issues, we believe it would help investors' understanding of this argument if the company continues to improve its disclosures regarding where and how it has been able to shift the policy stance of the more contentious associations of which it is a member. As our support for this resolution is not a signal of dissatisfaction, BIS has not voted against any members of Origin's Board of Directors, which would typically be our approach to flag significant concerns about a company's management of material ESG issues'.

ACCR response

Commenting on the industry lobbying resolution, ACCR Director of Climate & Environment Dan Gocher said that the strong support is a signal to Origin of shareholder expectations around lobbying efforts. He commented,

> 'More than a quarter of Origin's shareholders have put the Board on notice that they will not tolerate its lobby groups' advocacy for a gas-fired recovery…In the absence of mainstream proxy adviser support, both Origin and the proxy advice industry must accept that the problem of lobbying on climate and energy policy is not going away. While Origin's exit from the QRC earlier this month is welcome, Origin has not disclosed the conditions under which it would rejoin. Origin must insist that the QRC ceases its support for the relentless expansion of the coal and gas industries. Piecemeal annual reviews will no longer cut it. Origin will be expected to exit further industry associations, in addition to the QRC.'

Commenting on the consent and fracking resolution ACCR Executive Director Brynn O'Brien welcomed the uptick in support as compared with last year.

> 'Despite a jump in investor voting, from 5.5% last year to 11.8% today, the vast majority of investors continue to vote down measures to improve transparency on the issue of consent of Traditional Owners in the Beetaloo Basin. Investors can no longer rely on regulatory regimes in place in Australia to protect the interests of Traditional Owners - as the Juukan Caves blasting clearly demonstrates -- and further due diligence should always be applied in such relationships. ACCR has been following this issue for three years. Our interest is in ensuring that Origin's stated commitment to the UN Declaration on the Rights of Indigenous Peoples is implemented in practice. The resolution simply called for a review of Indigenous consent arrangements in this region, under agreements negotiated between Origin's predecessors and the Northern Land Council. To date Origin has played down Native Title Holders' stated concerns, but those concerns appear to persist. Investors are entitled to know the true picture. That is the purpose of ACCR's engagement on this issue.'

[Sources: Origin ASX Announcements: Results of meeting; Copy of AGM addresses and presentation; BlackRock Voting Bulletin: Origin Energy Ltd; CalPERs voting decisions: Origin Energy Ltd; ACCR media release 20/10/2020]

In Brief | ISS is consulting on proposed changes to 17 discrete voting policies. Proposed changes include changes in the areas of board diversity, board composition, director accountability, director overboarding and shareholder litigation rights disclosure. The deadline for submissions is 26 October

[Sources: ISS media release 14/10/2020; Proposed draft voting policy changes]

Institutional Investors and Stewardship

ACSI's annual benchmark report on climate disclosure at ASX 200 companies has identified 'significant improvement' but calls on companies to do better at linking their actions/strategy to their stated commitments

Key Takeouts

- The Australian Counsel of Superannuation Investors' (ACSI's) latest annual benchmark review of climate-related disclosure by ASX 200 companies has identified a significant (and welcome) improvement in climate-related disclosure and management though disclosure in some cases still lacks sufficient detail to enable investors to understand the pathway companies are taking towards achieving tehir stated climate goals.
- ACSI expects an 'emerging trend' in 2020/21 will be the linking of short and long-term incentives to decarbonisation targets.
- Commenting on the report, ACSI CEO Louise Davidson said that 'The uplift of net-zero and other carbon reduction commitments in the ASX 200 demonstrates that this is fast becoming the "new normal" for leading companies'.
- Ms Davidson makes clear that she considers disclosure (though welcome) to be only the first step. 'Investors want to understand how companies are stress-testing their business and how this is informing company strategy, and actions, over the short and medium-term to meet the Paris goals' Ms Davidson states.

The Australian Counsel of Superannuation Investors' (ACSI's) latest annual benchmark review of climate-related disclosure by ASX 200 companies assessed climate disclosures made by ASX 200 companies filed up to 31 March 2020.

Overall the report concludes that there has been significant improvement in climate-related disclosure, with increases in both the number of companies reporting against the TCFD recommendations setting net-zero 'aspirations' on the rise.

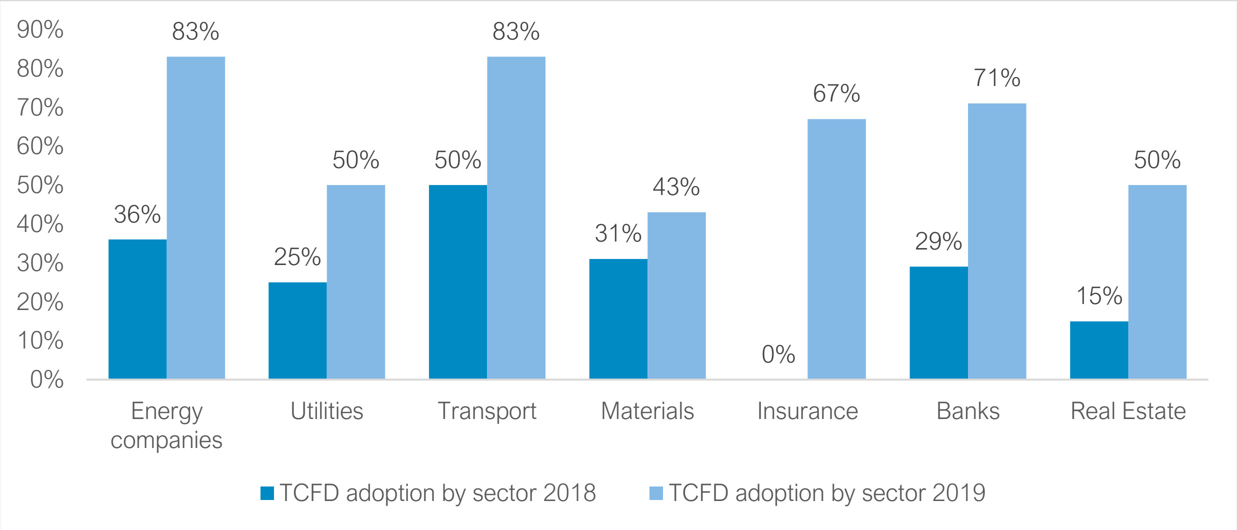
However, the report makes clear that from an investor perspective, disclosure in some instances lacks sufficient detail to enable investors to clearly understand the pathway companies are taking towards achieving their stated climate goals, how companies are stress-testing their businesses and the bearing this is having on company strategy and decision-making over the short and medium term.

Some Key Points

TCFD adoption

- 60 ASX 200 companies have adopted the TCFD framework (up from 11 companies in 2017).
- As yet, disclosure tends to be found in free-standing climate change reports rather than being integrated into financial statements, though ACSI comments that there are signs that this is shifting with some companies linking risks resulting from the transition to a low carbon economy being integrated into companies' asset impairment analysis.

- Companies in 'higher risk' sectors are leading the trend, with 56% of companies in these sectors overall reporting against the TCFD recommendations .
- The table below provides a snapshot of the substantial increase, identified in the report, in the number of companies in higher risk sectors reporting in alignment with the TCFD recommendations.



Emissions reporting and targets

Setting emissions reduction targets

- Almost 60% of ASX 200 companies now disclose their direct emissions (scope 1 and 2 emissions) – that is, the carbon footprint of their own operations. ACSI attributes this in part to the requirement for companies with significant greenhouse gas emissions to report under Australia's national Greenhouse and Energy Report Act 2007.
- A small minority (6%) of companies provide 'some level' of GHG emissions reporting not only on their direct emissions (scope 1 and 2) but across their value chain (Scope 3).
- 37% of companies have set emissions reduction targets. Of this group most (55 companies) set only short term targets (present to 2025); only 28 companies set medium term targets (2026-2039) and 13 set long-term targets (2040 and beyond). Table 3 at p13 of the report includes a graphic naming the companies in each category.
- Companies in sectors most exposed to climate transition risks have not yet set emissions reduction targets. For example 75% of material companies and 67% of energy companies have yet to set emissions reduction targets. ACSI states that it is concerned that so many companies appear to be 'waiting on national policy to drive change and investment'.

Net zero emissions commitments

- ACSI found that eighteen ASX 200 companies have now set net zero ambitions/targets. Of this group, only a small proportion (five) have set both short and medium term targets.
- ACSI found that companies are not providing sufficient information around how their capital expenditure, investment decisions, research and development spending etc are contributing to meeting either the goals of the Paris Agreement or to meeting their net-zero commitments.
- ACSI suggests that one reason for companies failing to provide detail around the actions they will take in the medium term to drive down emissions is the 'limited insight' they have into emerging technology, material substitution, abatement opportunities and technological opportunities'. Likewise, the report found that a key reason for companies holding off setting targets is 'uncertainty' around how the target would be achieved for example because they are reliant on 'step change technology' which is not currently commercial.
- Though acknowledging these challenges the report makes clear that investors expect companies who are reliant on new technologies to meet their targets to: a) 'disclose key milestones for commercialisation'; and b) disclose how much investment is being made into research and development. ACSI states that a key concern for

investors is that companies are committing to Paris targets, but doing so with no plan for achieving them, ie leaving the plans/actions for achieving them to future leadership teams.

More companies are undertaking scenario analysis

- ACSI found that the number of companies testing the resilience of their business using a range of climate scenarios significantly increased on 2018 levels from 18 in 2018 to 32 in 2019. A further 28 companies reported that they are in the process of undertaking scenario analysis or planned to do so in FY 21.
- ACSI found that few companies (13) are using a 'strict' 1.5 degree scenario. ACSI suggests that his may be an indication that many companies are 'failing to stress test their portfolios against sufficiently challenging and robust scenarios'. Table 6 at p16 of the report includes a table naming the companies using 'Paris aligned' scenarios (either 1.5 degree scenarios or 'well below 2 degree' scenarios).
- ACSI found that 62% of ASX 200 materials companies, 50% of utilities companies and 25% of energy companies have not undertaken stress testing or indicated their intention to do so in future despite their high exposure to transition risk. This is of concern, ACSI comments, because it means investors have limited insights into the resilience of these businesses.
- Quality of reporting: ACSI found that disclosure of scenario analysis varied widely and that overall there was 'limited disclosure and variable depths of information'. In addition, the report highlights comparability as a challenge for investors given the very wide range of scenarios being used, even among industry groups. The report calls on companies to include more detailed information including (among other things) an explanation of how scenario analysis is informing company strategy and actions or climate related opportunities over the short and medium term.
- Companies are not reporting the downside: ACSI found that 'across the board, companies paint a rosy picture of financial performance under all scenarios' and raises concerns that this 'general level of optimism may be unrealistic'.

Few companies reported on the physical risks of climate change in a 'meaningful manner'

- The report comments that disclosure of physical risk is in the 'early stages of development with no standardised disclosure'.
- Though 28 companies provided some general physical risk disclosure, it tended to be 'cursory and provided no insight into physical risk management'. Only ten companies were assessed as doing so in a manner that suggested a 'robust internal analysis was being undertaken'.

[Sources: ACSI media release 18/10/2020; ACSI report: Promises, Pathways and Performance: Climate change disclosure in the ASX 200]

Stepping up pressure for companies to lower emissions: LGIM cautions climate 'laggards' that it will name them publicly

Context: In 2016, Legal and General Investment Management (LGIM) committed to engage with around 80 of the largest companies in the energy, transport, food retail and financial sectors around the strength of their sustainability strategies. Companies assessed to be demonstrating best practice were publicly celebrated while those assessed as climate laggards faced votes action and divestment.

Expansion of LGIM's 'Climate Impact Pledge': LGIM has announced a ten-fold increase in the number of companies being it will target with the aim of driving down emissions in line with achieving the net-zero target by 2050.

- LGIM plans to make publicly available on its website quantitative metrics, including LGIM's proprietary climate modelling climate ratings for over 1,000 companies in key sectors.
- Where companies are identified as falling short of LGIM's minimum standards, eg where companies lack 'comprehensive disclosure of emissions or key sustainability certifications' LGIM will consider taking voting action or consider divestment.
- LGIM states that it intends to 'ratchet up' the stringency of both its standards and sanctions over time.

Announcing the expansion of the program, LGIM Head of Sustainability and Responsible Investment Strategy Meryam Omi and member of the COP26 High Level Champions Team – Finance commented

> 'Inaction on climate change threatens the long-term stability of the market, but we know engagement with consequences can get companies to change. The challenge is having more speed and scale. That is why we are combining cutting-edge data with in-depth research into key sectors to support companies that are building resilient strategies, and systematically hold to account those that are not'.

Lord Nicholas Stern, IG Patel Professor of Economics and Government at the London School of Economics (LSE) and Chair of the Grantham Research Institute on Climate Change and the Environment, commented,

> 'There is mounting evidence that firms that put sustainability at the heart of their strategy perform better, too. It is vital that asset managers like LGIM must continue to use their influence to accelerate the sustainability revolution across all sectors'.

[Source: Legal and General Investment Management media release 14/10/2020]

In Brief | The University of Tasmania says it will divest from fossil fuel-exposed investment funds by the end of 2021 and make no further investments in companies or funds with exposure to fossil fuels 'effective immediately' to support the creation of a zero-carbon economy

[Source: University of Tasmania media release 19/10/2020]

Markets and Exchanges

ASX is consulting on proposed changes to capital requirements for non-bank ASX Clear Participants

Onn 14 October 2020, ASX released a consultation paper proposing to consolidate the two capital measures that non-bank ASX Clear participants are currently required to maintain under Schedule 1 of the ASX Clear Operating Rules into a single measure.

The ASX is seeking feedback on the proposed single capital measure and on other proposed rule amendments to ensure the currency and accuracy of references.

The deadline for submissions is 30 November.

[Source: Consultation Paper: Proposed changes to capital requirements for ASX Clear Participants]

Financial Services

COVID-19: APRA Chair Wayne Byres identifies seven lessons in operational resilience for Australia's banks

In his address to the Basel Committee on Banking Supervision (BCBS) Australian Prudential Regulation Authority (APRA) Chair Wayne Byres said that though Australian banks have responded 'quite well' to the challenges posed by the COVID-19 pandemic, he considers there to be seven areas in which their operational resilience could be strengthened.

SEVEN LESSONS	SPECIFICS
1. Board oversight of risks exceeding risk tolerance	▪ Mr Byres observed that in the early stages of the pandemic a number of banks 'found themselves operating beyond their risk tolerance and, at least in some instances, this persisted for quite a while. While inevitably there was a need for speed, and often little choice in actions taken, quickly identifying and specifying the expectations from the Board and executive on their willingness to accept risks outside tolerance can undoubtedly strengthen response and recovery plans to get back within risk appetite'.
2. Business continuity plans	▪ Mr Byres said that while he does not expect contingency plans to be capable of execution 'without a hitch', especially in light of the 'unprecedented' nature of the COVID-19 pandemic, the pandemic has nevertheless identified some areas where business continuity plans could be strengthened. For example, plans could be adapted to more effectively deal with challenges such as: a) the repatriation of services conducted by offshore providers; b) dealing with the possible impact of global lockdowns; and c) dealing with employees working from home over an extended period. ▪ Mr Byres suggested that in light of this, banks will 'need to re-evaluate what scenarios they consider plausible, and what additional scenarios they need to cater for in business continuity planning and testing. A key dimension will be the longevity of the disruption'.
3. Information security	▪ Mr Byres said that the rapid transition to staff working from home has introduced a range of additional security concerns including: a) the capacity of virtual private networks to support remote working; b) the security of information accessed in the home environment; and c) the dependency on home connectivity.
4. Change freezes/deferrals on longer-term system hygiene	▪ Mr Byres observed that a number of banks elected to freeze or defer implementation of new products/features to maximise short term stability when the pandemic hit, and that this has been effective in the short term. ▪ However, he cautioned that 'as the disruption persists, it's a less viable strategy. It's introducing a backlog of work that still needs to be done, and if the deferrals include less critical security patches, information security vulnerabilities can be building over time'.
5. Reliance on third party service providers	▪ Mr Byres said that the pandemic has 'highlighted vulnerabilities created by key service providers, especially those located offshore. It's also put a spotlight on potential concentration risks and interconnectedness from an ostensibly diverse range of banks relying on a few key critical service providers'.

SEVEN LESSONS	SPECIFICS
6. Ability to test contingency arrangements	▪ Mr Byres observed that the pandemic has meant that some aspects of contingency arrangements have gone untested. Mr Byres observed that 'while there's a natural focus on the lessons from COVID-19, other risks such as wholesale data centre loss, major cyber-attack and data corruption haven't gone away'.
7. Human toll	▪ Mr Byres said that the long duration of the COVID-19 pandemic has highlighted the pressure that lockdowns/remote working have on staff. He said that as a result of this, in future, contingency planning will 'inevitable have a much stronger human element to it'.

[Source: APRA Chair Wayne Byres Remarks to the BCBS outreach meeting on operational resilience 16/10/2020]

Extension of UCT protections to insurance contracts: Ahead of the commencement of the changes, ASIC has released updated information sheets and flagged that it is engaging with industry to 'gauge how insurers are tracking'

- **Context:** Unfair contract terms (UCT) protections will be extended to insurance contracts following the passage of Financial Sector Reform (Hayne Royal Commission Response—Protecting Consumers (2019 Measures)) Act 2020 from 5 April 2021.
- **Updated information sheets released**: Ahead of the commencement of the changes, the Australian Securitie and Investments Commission (ASIC) has updated Information sheet 210: Unfair contract term protections for consumers and Information sheet 211: Unfair contract term protections for small business to provide information about how the UCT protections will apply to insurance contracts from 5 April 2021.
- **Engagement with industry in the lead up to the commencement of the changes:** ASIC has flagged that it is undertaking targeted supervisory work with industry in the lead up to the commencement of the changes to assess industry's progress towards compliance the new requirements. This includes having discussions with insurers about contract terms which ASIC considers 'may raise concerns under the unfair contract terms protections'.
- **ASIC is focused in particular on**:
  - terms that allow an insurer to cash settle a claim based on the cost of repair to the insurer
  - terms that are an unnecessary barrier to a consumer lodging a claim
  - terms that reduce the cover offered where compliance with the preconditions is unfeasible; and
  - terms that use an outdated, and therefore inaccurate or restrictive, medical definition.

  [Sources: ASIC media release 20/10/2020; Information sheet 210: Unfair contract term protections for consumers; Information sheet 211: Unfair contract term protections for small business]

ASIC has outlined its expectations for the handling of business interruption insurance claims arising from the COVID-19 pandemic

The Australian Securities and Investments Commission (ASIC) has written to insurers, Lloyd's cover holders and brokers outlining its expectations around how they should approach handling business interruption insurance claims arising from the COVID-19 pandemic.

ASIC's expectations

- **Clear communication:** ASIC expects insurers, Lloyd's cover holders and brokers to ensure information provided to all policy holders prior to lodging a claim is 'clear, accurate, balanced and does not, whether deliberately or inadvertently, mislead or deceive'. The letter also strongly encourages communication with policyholders in a way that 'helps Australian small businesses make appropriate and informed decisions about whether they should lodge claims for business interruption losses arising from COVID-19'.
- **Prompt assessment and (where appropriate) payment of claims on policies without pandemic exclusions/limited exclusions:** ASIC expects that where claims are made on policies that do not contain a pandemic exclusion or that contain a limited exclusion, claims will be 'assessed and where appropriate paid in a timely manner to

ensure that financial pressures on small businesses are not exacerbated by slow payments'. Where it's determined that 'there are reasonable grounds' to pay a claim in part rather than in full, ASIC encourages insurers and Lloyd's cover holders to make an interim payment. ASIC comments that this should occur regardless of the eventual outcome of the Australian business interruption test case currently before the NSW Court of Appeal which is set to determine the effectiveness of certain infectious disease exclusions.

- **Where policies include a pandemic exclusion for losses arising from a pandemic where the 'disease' has been designated under the now repealed Quarantine Act 1908 (Cth), or the current Biosecurity Act 2015 (Cth)** ASIC expects insurers and Lloyd's cover holders to have a plan in place for responding to the outcome of the Australian business interruption test case which is considering the effectiveness of these exclusions. ASIC's expectation is that these plans include how insurers/Lloyd's cover holders will communicate with policyholders if the Court finds in favour of policy holders in the case. General insurers are also expected to provide 'appropriate information' to brokers to pass on to small business policy holders.

  [Source: ASIC letter to insurers 16/10/2020]

COVID-19: So far funds have paid out $34.3bn 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 11 October.

- 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 11 October, superannuation funds received 26,000 applications (down from 31,000 applications in the week to 4 October).
- Of the applications received in the week to 11 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.
- 9,000 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 11 October, superannuation funds made payments to 28,000 members worth $199 million.
- Funds have made approximately 4.5 million payments since the inception of the scheme worth a total of $34.3 billion. This figure represents 98% of applications received since inception of the scheme.

  [Source: APRA media release 19/10/2020]

APRA reminds RSE licensees and relevant persons of their obligations to meet the controlling stake requirements

The Australian Prudential Regulation Authority (APRA) has written to registrable superannuation entity (RSE) licensees to remind them of their obligations to meet the controlling stake requirements which took effect on 5 July 2019.

More particularly the letter reminds RSE licensees of: a) the requirement to seek approval from APRA; b) the form of that the approval request needs to take; and c) the actions APRA requires all RSE licensees take to determine if this letter applies to them.

- The changes mean that an application for approval to hold a controlling stake (15% or more) in a registrable superannuation entity (RSE) licensee needs to be considered whenever there are changes to the ownership of shares in an RSE licensee. An application will always be required for a new RSE licence and may be required in other circumstances.
- The letter calls on RSE licensees to review their current ownership structures in light of 5 July 2019 changes. Where changes have been made (requiring APRA approval) where approval has not been given, licensees

should contact APRA within 30 days. Licensees should also ensure that there is a framework is in place to ensure these obligations are met for any future changes.

- The application process to apply for approval to hold a controlling stake has changed. Revised instructions and the new application form are available on the APRA website here.

[Sources: APRA media release 15/10/2020; APRA letter: Know your obligations - approval to own or control an RSE licensee]

Hayne implementation update: Assistant Financial Services Minister says that the compensation scheme of last resort and single disciplinary body for advisers will be legislated by mid-next year

Key Takeouts

- In her address to the Association of Financial Advisers virtual conference Assistant Minister for Financial Services Jane Hume underlined the government's support for the financial advice sector, stating that the sector will play an important role in Australia's economic recovery.
- Ms Hume also reiterated the government's commitment to implementation of the Hayne Commission recommendations.
- Implementation of Hayne recommendation 2.10: Ms Hume said that the government is 'working through the detail' on establishing a new disciplinary system for financial advisers, including a single, central disciplinary body as recommended by the Hayne Commission. The government intends to introduce the necessary legislation by 'mid-2021'.
- Implementation of Hayne recommendation 7.1: Ms Hume said that the government is aiming to introduce the necessary legislation to establish a forward-looking compensation scheme of last resort by 'mid-2021'.
- Ms Hume said that deregulation of the financial advice sector is a priority, stating that she 'looking for opportunities for red tape reduction, identifying obstacles to productivity and profitability, and reducing the burden on your industry and its participants'.
- Technology will play an increasingly important role: Ms Hume said that going forward, technology will be increasingly important in enabling advisers to provide useful and affordable advice.

The focus of Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume's address to the Association of Financial Advisers was the future of financial services and in particular, the financial advice industry.

Some Key Points

- **COVID and financial advice:** Ms Hume said even before the pandemic, the financial advice sector was 'undergoing significant transformation' to lift standards in response to the Hayne Commission and that during the pandemic, financial advisers had provided valuable support and guidance to clients at a time when they most need it.
- **Deregulation is a priority:** Ms Hume said that during her time as Assistant Minister for Financial Services she has met with 'hundreds' of individual advisers, brokers and worked with industry bodies to discuss issues facing the industry and assured advisers that she is 'working to your biggest concerns.' Ms Hume said that in addition to implementing the Hayne recommendations, and working to lift industry standards 'I'm also constantly looking for opportunities for red tape reduction, identifying obstacles to productivity and profitability, and reducing the burden on your industry and its participants'. Ms Hume observed that,
- **'Financial advisers are a critical part of our economy and will be critical in our COVID recovery.** I'm not ashamed to say that the Government has a vested interest in ensuring that you can provide financial advice to as many Australians as possible without being tied up in red tape' Ms Hume said.
- **The professionalisation of the industry is progressing:** Ms Hume said that she considers that the sector has 'come quite some way along the journey to professionalisation' and that this is set to continue with all financial advisers meeting new education requirements by 2026. Ms Hume said that she is 'confident' that the 'standards will bring financial advisers in line with other professions – such as lawyers, doctors and accountants. Standards will also ensure there is consistency across the industry and that all financial advisers have the skills necessary to provide high-quality advice to consumers, and better position the industry to serve consumers'.

- **Implementation of Hayne recommendation 2.10** to establish a single disciplinary body for financial advisers: Ms Hume said that the government is 'working through the detail' of establishing a new disciplinary system for financial advisers, including specifically a single, central disciplinary body as recommended by the Hayne Commission. Ms Hume said that the government intends to introduce the necessary legislation by 'mid-2021'
- **Implementation of Hayne recommendation 7.1** to establish a forward looking compensation scheme of last resort: Ms Hume said that the government is aiming to introduce the necessary legislation to establish the scheme by 'mid-2021'.
- **Recap of the government's progress towards implementation of the Hayne Commission's recommendations:** Ms Hume said that before the outbreak of COVID-19, the government had made 'significant progress' towards implementation of the Commission's recommendations, 'with 24 recommendations implemented and another 35 progressed via consultation'. Due to the pandemic, the government made the decision to defer the introduction of commitments that had yet to be legislated by six months and deferring commencement of some measures. For example, the enhanced breach reporting regime and new obligations for financial services licensees to report and remediate misconduct by financial advisers will was deferred until 1 October 2021. Ms Hume stated that implementation of the Hayne recommendations remains a 'key priority' for the government.
- **Investment in Fintech:** Ms Hume said fintech will also play an important role in the future of the advice sector and recapped the funding commitments in Federal Budget to support fintech stating 'I'm committed to supporting a sector that helps consumers be more engaged with financial products and services; that enhances financial literacy and capability; and that helps us all spend less time and less money managing our finances'.
- **Consumer Data Right:** Ms Hume said that the continuing roll out of the consumer data right (CDR) is a key focus for the government and that this is reflected in the Federal Budget funding commitments. Ms Hume said that since the CDR was launched in July, there has been 'strong interest from the Australian fintech ecosystem', with approximately 100 companies already opened applications to become accredited as data recipients. Going forward, consumers will continue to benefit as the CDR is rolled out to energy, telecommunications, superannuation, insurance and beyond. 'The sky is the limit — as the technology evolves, so too will the offerings that will be available' Ms Hume said.
- **Increased use of technology by the sector:** Ms Hume said that going forward, technology will play an important role in enabling advisers to provide affordable targeted advice. Ms Hume said that her focus is on 'helping advisers get access to the tools they need to deliver high quality compliant advice at an affordable price. That can happen, but to do it, it's going to need a greater role for technology. An it's going to involve the regulators taking a more forward leaning approach to the rollout of technology that helps advisers to do their job'.

  [Source: Assistant Minister for Superannuation, Financial Services and Financial Technology Jane Hume's address to the Association of Financial Advisers Virtual Conference 14/10/2020]

Related News

A separate speech - Keynote address to FSC Future of Advice Summit - also delivered on the 14 October (but not publicly released on the Senator's website until 20 October) covers substantially the same ground as the Senator's speech to the AFA virtual conference.

> [Source: Assistant Minister for Superannuation, Financial services and Financial Technology Jane Hume's Keynote address to FSC Future of Advice Summit (delivered) 14 October 2020]

Afterpay to offer 'transaction and savings accounts and other cash flow management tools' through Westpac's digital bank-as-service platform from Q2 2021

Westpac has announced that Afterpay is the first partner on its new digital bank-as-service platform.

According to Westpac's statement, this will enable Afterpay to provide its 3.3 million customers in Australia with 'Westpac transaction and savings accounts and other cash flow management' by Q2 2021.

Announcing the partnership Afterpay CEO, Anthony Eisen commented,

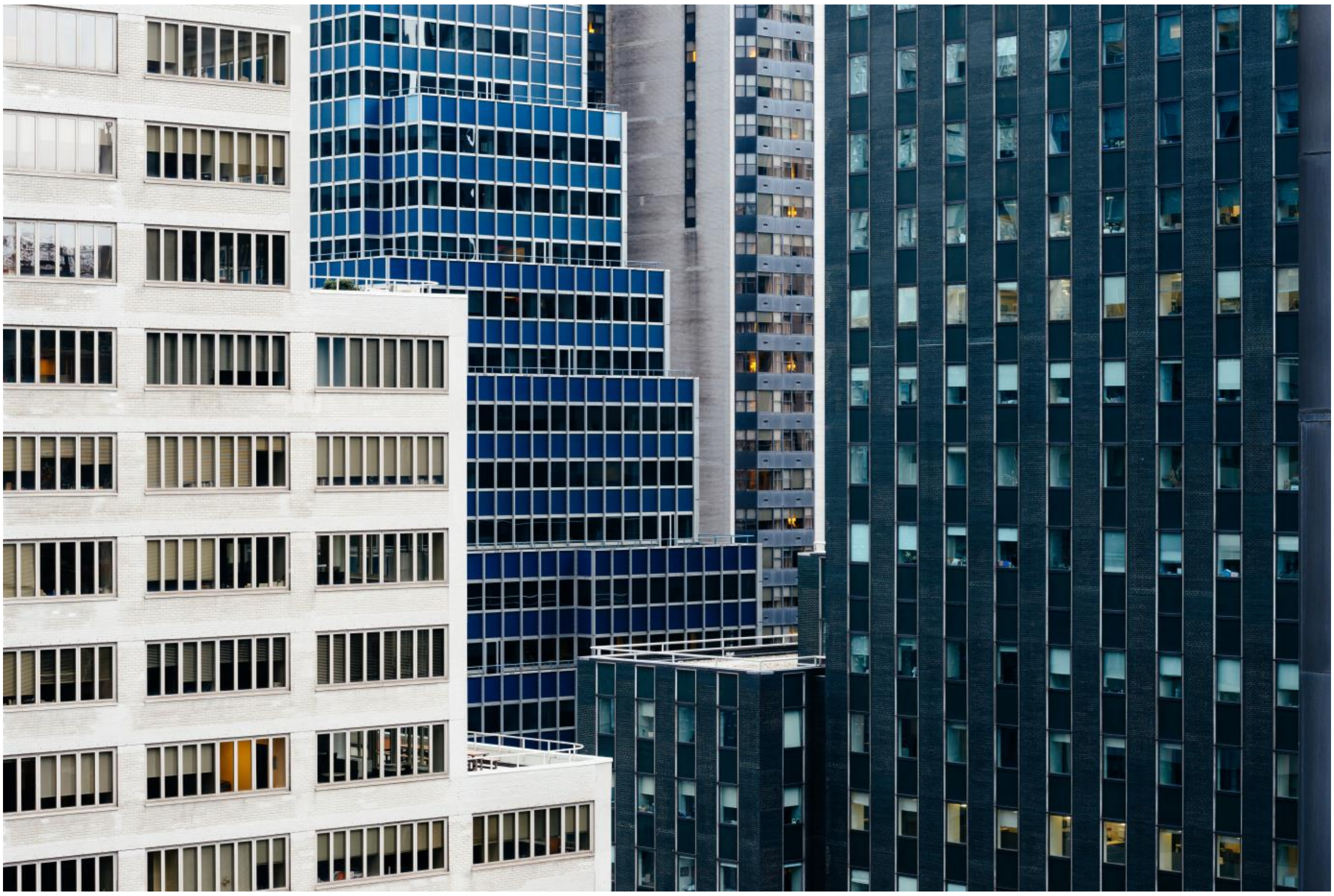
> 'We believe Australians deserve greater support and insight to help manage their money. Together with the power of our retail platform, the latest banking technology from 10x, and the support of Westpac, we will begin by offering cashflow management in a simple way. Afterpay is in a unique position to extend and

deepen the relationship with our customers and help them to manage their money more seamlessly through savings and budgeting tools. For Afterpay, this is clearly just the beginning as we explore this opportunity globally'.

In a separate announcement, Afterpay states that the new 'money management services' that will be offered via Westpac's platform will 'complement Afterpay's existing business model by offering additional customer-centric alternatives to traditional banking products'. The partnership is also expected to (among other benefits for the Afterpay):

- provide Afterpay with 'further insight' into how customers manage their finances and 'how responsible spending behaviour can be further encouraged and rewarded'
- generate new revenue streams over time in Australia and (eventually, globally), without the need for Afterpay to develop traditional banking or credit products
- deliver efficiency benefits to Afterpay's existing activities from a risk management and processing cost perspective.

[Sources: Westpac media release 20/10/2020; Afterpay ASX Announcement 20/10/2020]



No further regulatory action: AUSTRAC has finalised its external audit of BNPL provider Afterpay

AUSTRAC has confirmed that it has determined not to undertake further regulatory action against Afterpay Australia Pty Ltd (Afterpay) on the basis that it considers the company's response to the findings/recommendations of the external audit report into Afterpay's compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (the AML/CTF Act) to be sufficient.

AUSTRAC states

> 'Afterpay has uplifted its AML/CTF compliance framework and financial crime function, and completed all remediation necessary to ensure compliance. After considering the report and the response by Afterpay, AUSTRAC has decided not to undertake further regulatory action'.

AUSTRAC states that it will continue to work with Afterpay to ensure 'they understand their compliance obligations and role in fighting financial crime to protect the Australian community from harm'.

AUSTRAC reminded new and emerging financial services businesses of their obligations under the AML/CTF Act and the imperative that they put in place appropriate systems/controls to identify and mitigate AML/CTF risks.

Response

In a brief statement acknowledging AUSTRAC's decision, Afterpay Chair Elana Rubin commented,

> 'We are pleased to have received AUSTRAC's decision following the external audit as it provides the company and its stakeholders with certainty and acknowledges the work the company has undertaken to strengthen its AML/CTF compliance. The external audit provided Afterpay with the opportunity to better understand our obligations and to improve the way we manage our AML/CTF risks. We will use these learnings and our ongoing engagement with AUSTRAC to continue enhancing our AML/CTF framework as the business continues to grow.'
>
> [Sources: AUSTRAC media release 14/10/2020; Afterpay ASX Announcement 14/10/2020]

Pre-emptive action, though expensive, is nevertheless the most cost-effective response to the climate challenge says APRA

Key Takeouts

- Climate risk is a risk to the stability of the financial system, and in the context of insurance, a significant risk to the sustainability of the industry
- In some parts of the country, insurance is already unaffordable and given the increasing frequency of extreme weather events, much of Australia is at risk of becoming uninsurable
- The most cost effective response to the damage caused by extreme weather events is investment in mitigation efforts
- Mitigating the effects of climate risk cannot be borne entirely by any one sector, but insurers should take steps to ensure that measures taken by consumers to mitigate against damage caused by extreme weather events are reflected in appropriate reductions in premiums

In his address to the Australian Business Roundtable for Disaster Resilience and Safer Communities Webinar Australian Prudential Regulation Authority (APRA) Executive Board Member Geoff Summerhayes spoke about the importance of ensuring that the community is prepared for increasingly frequent extreme weather events and the importance of ensuring that the insurance sector remains on a sustainable footing given the challenges posed by the changing climate.

A central message of Summerhayes' address was that the cost of mitigating against the damage caused by natural disasters is significant, but is still considerably cheaper than failing to do so.

Some Key Points

- **Climate risk poses a significant risk to the economy and to the insurance sector:** Mr Summerhayes observed that

  > 'APRA's interest in issues around natural disasters and climate-related risks is obvious' in light of the economic impact these events have, including the impact they have on the insurance sector. Should the experiences of last summer prove to be the "new normal" as is the 'clear message from Australian and global scientific experts', the resilience of the economy, and the insurance sector in particular will be tested.

- **The sector is 'highly engaged' on the issue:** Over the past several years, APRA has been working with insurers to make sure they understand and are managing climate risk, and APRA data indicates that the general insurance sector is highly engaged on the issue.
- **Continued access to insurance is a key concern for APRA:** Mr Summerhayes said that

  > 'APRA's biggest concern when it comes to the impact of climate-related risks on insurance is…not the prospect of an insurer becoming insolvent – it's the possibility that general insurance might become unaffordable or even unavailable in parts of Australia'.

  Were this to occur, the economic consequences after disasters would be magnified, threatening the financial stability of the country. Mr Summerhayes observed that for residents in northern Australia, insurance is already becoming unaffordable as the frequency of extreme weather events increases and the frequency and costs of claims increases.
- **The best way to ensure the availability and affordability of insurance is to address the 'root cause' of the problem:** Mr Summerhayes said that APRA considers that the

  > '…declining insurance affordability and accessibility in Australia's north can best be meaningfully and sustainably addressed by tackling the root cause: the high, rising and volatile cost of natural disasters. The most effective way to do this is through greater investment in mitigation to protect homes, businesses and infrastructure from damage. There may be other approaches that serve, for example, to subsidise the cost of insurance, but on their own they will ultimately be less effective because don't lower the risk and may reduce the incentive to mitigate it…There is a lot of merit in the Productivity Commission's assessment that paying for mitigation is far cheaper than paying for post-event remediation, and enduring the subsequent economic repercussions'.
- **Who should bear the cost of paying for mitigation efforts?** Mr Summerhayes said that sole responsibility for mitigating against climate risk cannot be borne by governments alone. Rather households and businesses should bear some responsibility for protecting their own properties. Insurers, he said, can do more to incentive mitigation by ensuring mitigating efforts translate into 'appropriate premium reductions for their policyholders'. Mr Summerhayes observed,

  > 'It's not realistic to expect a homeowner to spend tens of thousands of dollars installing reinforced doors and roof battens, shatterproof windows and waterproof seals if the consequent premium relief is negligible. If insurers want their argument that lowering the risk lowers the premium to be taken seriously, they must do more to recognise mitigation by home and business owners, and reward it accordingly'.
- **The private sector is already investing in mitigation efforts:** Mr Summerhayes gave a number of examples of insurers/other initiatives that are investing in measures to mitigate against the risks of climate change. He observed.

  > 'What these and other businesses recognise is that funding measures to prevent or minimise the damage caused by natural disasters is about more than being a good citizen; it's an investment that will save vastly greater sums of money over the long-term'.
- **Mitigation measures are expensive, but not as expensive as the alternative:** Mr Summerhayes said that the cost of investment in measures needed to protect Australian communities and keep insurance affordable and accessible comes at very significant cost, but that 'failing to take action can be far more costly in the long-run, and the price paid is often far more valuable than can be measured in dollars'. He observed,

  > 'even accepting modelling from the US suggesting that every '$1 spent on resilience saves up to $11 in response and recovery costs, covering these losses would require the Australian community to invest about $3.5 billion each year on natural disaster mitigation and resilience. That's an enormous sum, but it's much smaller than the $39 billion cost!'

  > [Source: Executive Board Member Geoff Summerhayes - Speech to Australian Business Roundtable for Disaster Resilience and Safer Communities webinar 14/10/2020]

What credit squeeze? The ABA confirms that 'Australia's banks remain open for business for small business customers'

The Australian Banking Association has issued a statement confirming that the flow of credit to business has remained strong throughout 2020.

According to the ABA:

- Since 1 February, Australian banks have approved over $41 billion in credit for SMEs and sole traders. Total lending approved to all businesses, of any size, is more than $200 billion since February.
- In the six weeks up to 7 October, banks approved loans of more than nine billion dollars to small and medium businesses and sole traders.
- Banks have approved around 70% of loan applications received.
- On average, banks have approved more than 500 new SME loans a day for more than 250 days.

ABA CEO Anna Bligh commented that the data shows that

> 'Australia's banks remain open for business for small business customers. The banks' commitment to small business has been supported by a number of Government and regulatory measures, including the RBA's Term Funding Facility, changes to business lending rules, the instant asset write-off, and the SME loan guarantee. Australian banks are continuing to provide a lifeline to small and medium businesses across the country. The rate of lending has held up strongly despite the pandemic. These small businesses will drive Australia through the crisis, and after it has passed, employ millions of Australians as the economy rebuilds.'
>
> [Source: ABA media release 20/10/2020]

In Brief | Boosting SME capital: The Treasurer has announced the formal establishment of the Australian Business Growth Fund and welcomed the appointment of Anthony Healy as the inaugural CEO. Mr Frydenberg said that the fund, which has an initial investment capacity of $540 million is expected to 'shortly begin engaging with SMEs that are seeking patient equity investment in their business to enable them to grow and expand'

[Source: Treasurer Josh Frydenberg media release 16/10/20020]

In Brief | The Financial Stability Board has published a global transition roadmap for LIBOR setting out a timetable of actions for financial and non-financial sector firms to take in order to ensure a smooth LIBOR transition by end-2021

[Sources: FSB media release 16/10/2020; FSB global transition roadmap for LIBOR]

In Brief | Industry Super Australia and Women in Super have called for the government to adjust the Low-Income Superannuation Tax Offset (LISTO) to cover workers earning up to $45,000 to help boost the retirement savings of 1.2 million people, including 700,000 women

[Source: Industry Super media release 14/10/2020]

In Brief | The Federal Court has imposed a total of $75 million in financial penalties on OTC derivative issuer AGM Markets and former authorised representatives OT Markets and Ozifin following the February 2020 decision which found that they had each engaged in systemic unconscionable conduct while providing over-the-counter derivative products to retail investors in Australia

[Sources: ASIC media release 19/10/2020; Australian Securities and Investments Commission v AGM Markets Pty Ltd (in liquidation) (No 4) [2020] FCA 1499]

In Brief | Societe Generale Securities Australia Pty Ltd will pay a total penalty of $30,000 for breaches of client money obligations. ASIC Commissioner Cathie Armour welcomed the decision commenting that 'ASIC will continue to devote resources to ensure that client monies are dealt with appropriately'

[Source: ASIC media release 21/10/2020]

In Brief | Hayne case study: The Federal Court has directed NAB to pay a $15m civil penalty in connection with the (now disclontinued) introducer program, which was found to contravene s31(1) of the National Credit Act

[Sources: Australian Securities and Investments Commission v National Australia Bank Limited [2020] FCA 1494; ASIC media release 19/10/2020]

In Brief | A former financial adviser and Hayne Commission witness has been fined a total of $10,000 after falsely claiming to hold a masters of commerce degree in certain communications with clients and in marketing materials. ASIC highlights that in handing down the sentence, Magistrate Atkinson noted the need 'for the Court to send a message to the community at large that being a financial advisor is a specialist position. Marketing material and websites, including qualifications, need to be correct'

[Source: ASIC media release 20/10/2020]

In Brief | Keith Skeoch (former non-executive director of the FRC) has been appointed as Interim Chair of the UK Financial Reporting Council from 12 October 2020 for a period of up to 6 months while a permanent replacement for former chair Simon Dingemans who stepped down in May, is being recruited

[Source: BEIS media release 15/10/2020]

Accounting and Audit

The FRC is consulting on proposed changes to strengthen the auditing standard for the auditor's responsibilities relating to fraud

The UK Financial Reporting Council (FRC) is consulting on substantive, proposed changes to strengthen UK auditing standard ISA (UK) 240 (Updated January 2020 – the Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements, to address concerns, including concerns raised in the Brydon Review, that auditors are not doing enough to detect material fraud.

Announcing the consultation, Executive Director of Regulatory Standards Mark Babington said that the revised standard 'makes auditors' obligations clearer, enhances the risk assessment they carry out, and sets clearer requirements for what the auditor then does'. The full text of the proposed draft standard is here.

Timing: The deadline for submissions is 29 January 2021.

Proposed commencement: Once finalised, it's proposed that the revised standard will be effective for audit periods commencing on or after 15 December 2021 to coincide with ISA (UK) 315 (Revised July 2020) – Identifying and Assessing the Risks of Material Misstatement. This is intended to enable firms to update their procedures to meet the requirements in both standards at the same time, rather than separately.

[Sources: FRC media release 20/10/2020; Exposure draft of the proposed revised standard; Consultation paper and impact assessment: Proposal to revise ISA (UK) 240 (Updated January 2020) the Auditor's responsibilities Relating to Fraud in an Audit of Financial Statements]

Risk Management

The RBA is set to resume work on increasing transparency around payment system outages, banks may be required to publish data on payment systems outages from mid-2021

The Reserve Bank of Australia Payments System Board Annual Report 2020 has flagged (among other things) a 'significant increase in the frequency and duration of retail payments outages in recent years' with a sharp uptick in the duration of outages and the number of incidents in 2019/20. Graph 16 at p37 of the report provides a snapshot of this.

Banks to be required to publish data on payment systems outages from mid-2021

In response to this and supported by the Australian Prudential Regulation Authority (APRA), the RBA began working with the industry in late 2019 to enhance its quarterly data collection for retail payments incidents, and to develop a 'standard set of statistics on operational outages to be publicly disclosed by individual institutions'.

The report states that this work was put on hold because of the COVID-19 pandemic but that the RBA expects to recommence industry discussions 'in the latter part of 2020, with the aim of introducing the new requirements from around mid-2021'.

Resilient to COVID-19 challenges

The report states that 'overall retail payment providers have coped well since the COVID-19 outbreak began' in light of the fact that there were: a) few 'very severe' outages to electronic payment services, despite the heavier use of electronic payments by consumers; and b) given that systems have remained secure (despite the increased threat of malicious cyber activity).

The report comments however that 'the good outcomes on retail payments reliability may be partly explained by organisations having temporarily halted some system changes and updates, which could generate a backlog of important work that will need to be completed at a later time'.

[Source: Reserve Bank of Australia Payments System Board Annual Report 2020]

Crown confirms AUSTRAC investigation into potential AML/CTF non-compliance

Crown Resorts Ltd (Crown) has issued a brief statement confirming that following concerns raised in the course of a September 2019 compliance assessment, AUSTRAC's enforcement team has launched a formal investigation into potential non-compliance by Crown with requirements under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 and the Anti-Money Laundering and Counter-Terrorism Financing Rules 2007.

Crown states that AUSTRAC's concerns relate to: ongoing customer due diligence and 'adopting, maintaining and complying' with an AML/CTF program. Concerns raised in the compliance assessment 'focused on Crown Melbourne's management of customers identified as high risk and politically exposed persons'.

Crown says that it will 'fully cooperate' with AUSTRAC and respond to all information requests by the regulator.

Confirmation of the investigation by the regulator comes ahead of Crown's AGM which is scheduled to be held as a virtual meeting on 22 October.

[Source: Crown Resorts Ltd ASX Announcement: 19/10/2020]

The Reserve Bank of New Zealand is consulting on draft cyber risk management guidance

The Reserve Bank of New Zealand (RBNZ) has released draft cyber risk management guidance for consultation, setting out the bank's expectations around how all entities that the bank regulates manage cyber resilience.

Broadly, the draft guidance sets out RBNZ's expectations in relation to: governance arrangements; capability to identify, protect against, detect and respond to and recover from incidents; third party management (including expectations around outsourcing of cloud services) and the preparations RBNZ expects entities to make for sharing information on cyber incidents.

RBNZ comments that the guidance 'draws heavily from leading international and national cybersecurity standards and guidelines'.

RBNZ has also released a consultation paper seeking feedback on the proposed guidance as well as on its initial views on how information gathering and sharing can help build cyber resilience.

The consultation paper also outlines a future area of policy work aimed at establish protocols among public and private sector bodies to effectively share information and respond to cyber incidents when they do occur.

Announcing the consultation, Deputy Governor and General Manager of Financial Stability Geoff Bascand commented that,

> 'The proposed guidance and our information collection plans have been designed to complement the work of other government agencies with a direct interest in promoting cyber resilience in the financial sector – including the Financial Markets Authority, the National Cyber Security Centre and the Computer Emergency Response Team'.

Timing

The deadline for submissions is 29 January 2021. The Reserve Bank will release the final guidance early next year.

[Sources: RBNZ media release 20/10/2020; Cyber resilience consultation paper; [draft] Guidance on cyber resilience]

In Brief | CBA has released a range of resources for business to raise awareness and increase their understanding of cyber risk. CBA's Group Chief Information Security Officer Keith Howard called on businesses to: 'ensure they update their operating systems and applications on their computers and phones; ensure all staff are using strong and unique passwords; establish robust payment processes with multiple approvers; train staff on how to recognise suspicious emails; and set expectations with staff on how to handle corporate and customer data securely'

[Source: CBA media release 20/10/2020]

Insolvency and Reconstruction

Top Story | Small business insolvency reforms draft legislation; what you need to know now

Subject to the Australian Parliament passing the Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 (Cth) (Draft Bill), a new framework for the proposed new restructuring and simplified liquidation processes for eligible small companies will commence on 1 January 2021.

Though the details are yet to be finalised, understanding key components of the draft legislation will help organisations prepare for the changes and MinterEllison's team have prepared an expert summary to assist in this.

This can be accessed here.

In Brief | AFSA has encouraged businesses to consider whether the PPSR can 'provide peace of mind': In light of the significant proportion of business debts owed to trade creditors - AFSA data shows that people in businesses who entered into a personal insolvency owed 32% of their debts to a business, sole trader or individual - AFSA has called on businesses to take steps to guard against the risk of providing goods on credit

[Source: ASFA media release 12/10/2020]

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