Governance News

Weekly wrap up of key financial services, governance, regulatory, risk and ESG developments.

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Boards and Directors

Top Story | Podcast: Understanding Directors' Duties and Climate Risk

How can we tell whether a company is genuine about sustainability - or whether it's just greenwashing? MinterEllison has released a podcast featuring MinterEllison partner, Sarah Barker in conversation with Philippe Joubert, CEO of Earth on Board, Trustee of ClientEarth, a Fellow and Member of the Advisory Board of the Cambridge Institute for Sustainability and a Chevalier de la Légion d'Honneur – a Knight of the French Legion. They discuss directors' duty of care in relation to sustainability and climate change.

You can access the audio here.

Meetings and Proxy Advisers

Proposed proxy reforms: SAFAA joins proxy advisers is raising concerns

Context

- The government recently released a consultation paper setting out a number of potential reform 'options' to tighten the existing regulatory regime for proxy advice. You can find our brief summary of the options being considered here.
- Institutional Shareholder Services (ISS), Glass Lewis and Ownership Matters have each separately raised concerns and questioned the need for any change. You can find a short overview of some of the concerns raised by ISS and Glass Lewis in Governance News 12/05/2021 at p7.

SAFAA raises concerns about possible changes to proxy advice regulation

In a short submission, The Stockbrokers and Financial Advisers Association (SAFAA) has raised concerns about the reform options being considered, and in particular about options 3 and 4.

- Option 3 proposes to introduce a new requirement for proxy advisers to provide their report (ie the report outlining their research and voting recommendations), to the relevant company before distributing it to subscribing investors.
- Option 4 proposes to introduce a new requirement for proxy advisers to notify their clients about how they can access the company's response to their report.

Unintended consequences – the proposed reforms may capture a broader range of firms than is intended

The key concern raised in SAFAA's submission is the potential for the reforms to capture a broader range of firms than stated/intended in the consultation paper – that is, SAFAA is concerned that though the proposed changes are only intended to apply to the four main proxy advice firms named in the consultation paper, it appears to SAFAA that the changes would in practice, apply to a much broader range of firms who provide research that may impact the voting decisions of directors eg sell-side brokers.

SAFAA comments

> 'Proxy adviser' is not a defined term in the Corporations Act. "Proxy advice" is simply the provision of financial research that may impact on the voting decisions of investors. Many sell-side brokers provide commentary that would influence an investor's decision to vote for or against a resolution at a company meeting, including a resolution on the remuneration report or appointment or reappointment of directors. This would result in them being caught up in the proposed provisions outlined in Options 3 and 4 of the Consultation Paper'.

SAFAA considers that raises a number of issues.

> 'a government requirement for an entity to provide private intellectual property to a third party that is the subject of that research outside of contractual arrangements is entirely inappropriate. SAFAA is also concerned that the proposal is in conflict with ASIC Regulatory Guide 79 Research report providers: Improving the quality of investment research…SAFAA is of the view that any legislative reform which undermines the independence of research has the potential to disrupt fair, orderly and transparent markets.
>
> [Source: SAFAA submission 28/05/2021]

An early look at emerging trends this proxy season

Key Takeouts

- Analysis from Semler Brossy has identified that:
  - the level of support for shareholder ESG proposals is 'significantly' higher than last year
  - a higher proportion of 'say on pay' resolutions have failed to be approved as compared with last year
  - support for equity grants is also down on the same time last year

Semler Brossy has published an early look at voting trends so far this proxy season. A brief overview of some of the key points in the report is below.

Support of say on pay resolutions

- Say on Pay votes at 22 Russell 3000 companies (3.3%) have so far failed to be carried (up from 1.9% at the same point last year. Semler Brossy considers that while there are various reasons for this, in at least four cases, the low level of support was at least partly due to COVID-19 related actions on the part of the company.
- The average level of support for say on pay resolutions at Russell 3000 companies is 90.8% (down from 91.6% at the same time last year)
- Overall, the proportion of Russell 3000 companies receiving 90% (or more support) is slightly higher at 79% than at the same time last year (78%)
- The average level of support at S&P 500 companies is 88.4% (down from 90% in 2020)
- Looking more closely, there was variation in the level of support across sectors:
  - Companies in the information technology and real estate sectors had the highest proportion of failed say on pay votes (9% of votes so far in 2021, in each case) of all the sectors
  - The health sector had the highest proportion (10%) of votes falling into the 50-70% support range, across all sectors
  - The industrials and materials sectors respectively have the highest proportion of votes in the 90% (or more) category (both 88%)
- Impact of ISS recommendations on voting results: According to Semler Brossy, the average level of support for say on pay resolutions at companies that received an ISS 'against' recommendation is 36 percentage points lower than for companies that received an ISS 'for' recommendation (which is above the historical average range of between 23-32% points lower).

Support for equity proposals

- So far the average level of support for equity proposals is 90.2% (down from 91.6% at the same time last year).
- Two proposals have so far received less than 50% support.

- The proportion of proposals, so far this year, that have received 90% (or more) support has fallen to 73% (down from 75% at the same time last year).

Director elections

- So far in 2021, 80% of directors have been elected with 95% support (or more). Over the course of 2020, 73% of directors were elected with this level of support.
- The proportion of directors who have been elected with between 80-95% support currently stands at 15.7% . This is lower than the 21.3% of directors elected with this level of support over the course of 2020.

Shareholder ESG proposals

- The level of support for the 44 shareholder 'social' shareholder proposals and six environmental shareholder proposals voted on at the time of the release of the report, is significantly higher than at the same time last year.
- According to Semler Brossy:
  - the median level of support for social proposals is 33%.
  - the median level of support for environmental proposals is 59% with a number of diversity and inclusion proposals receiving above 70% support.
- In 2020, only nine shareholder 'social' proposals (21%) and three shareholder environmental proposals (50%) received greater than 50% support.

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 26/05/2021; Semler Brossy 2021 Say on Pay & Proxy Results 13/05/2021]

Say on Pay: More willing than previously to vote against executive pay?

- Analysis by Farient Advisers has identified that so far in 2021 shareholders are: a) voting against executive pay packages at a higher rate than in previous years; and b) singling out pay practices that may not have attracted concern in the past.
- For example, so far of the 235 S&P 500 companies in the sample, 25 companies have received less than 75% support . This is a significant uptick on last year's 16%.
- Farient also identified that if the 'bottom 10%' of the voting distribution is disregarded, then there is little movement between the 2020 and 2021 results.

[Sources: Farient Advisors 26/05/2021]

Shareholder Activism

Two (possibly 3) activist directors elected to the Exxon Mobil board

ExxonMobil's 2021 AGM was held virtually on 26 May 2021.

Director elections

- Following a lengthy proxy contest (you can find Professor Robert Eccles succinct summary and expert analysis here), preliminary voting results show that two (and possibly) three of activist Engine No 1's board candidates - Gregory Goff and Kaisa Hietala and (possibly) Alexander Karsner - have been elected to the ExxonMobil board, against the board's recommendations. A fourth Engine No 1 candidate Anders Runevad, was not elected.
- Of the twelve board-endorsed directors standing for election/re-election:
  - eight were reelected: Darren Woods, Kenneth Frazier, Michael Angelakis, Susan Avery, Angela Braly, Ursula Burns, Joseph Hooley and Jeffrey Ubben. Of this group, both Darren Woods and Kenneth Frazier also had the support of Engine No 1 and BlackRock.
  - It is not yet clear whether four other ExxonMobil director candidates - Steven Kandarian, Douglas Oberhelman, Samuel Palmisano and Wan Zulkiflee – have been elected to the board.
- Investor support:
  - According to Ceres, California Public Employees Retirement System (CalPERS), California State Teachers Retirement System (CalSTRS), and New York State Common Retirement Fund, all members of Climate Action 100+, voted for all four Engine No 1 candidates.
  - In a voting bulletin, BlackRock explains that it voted in favour of three of the four activist nominees because it considers a rapid change in leadership to be necessary to safeguard the long-term sustainability of the company. BlackRock states,

> 'We continue to be concerned about Exxon's strategic direction and the anticipated impact on its long-term financial performance and competitiveness. In our view, the Board would benefit from the addition of diverse energy experience to augment existing skillsets. As a result, BIS supported three of the four directors nominated by Engine No. 1. We believe that they, together with Mr Ubben [who was appointed by the company in response to Engine No 1's calls for board change] bring the fresh perspectives and relevant transformative energy experience to the Board that will help the company position itself competitively in addressing the risks and opportunities presented by the energy transition…This voting also reflected our belief that Exxon's energy transition strategy falls short of what is necessary to ensure the company's financial resilience in a low carbon economy'.

Shareholder ESG proposals

- According to Exxon, two of seven separate shareholder ESG proposals that went to a vote at the meeting - the proposal calling on the company to report on lobbying payments and policy and the proposal calling on the company to report on corporate climate lobbying aligned with the Paris Agreement – both received majority support.
- Exxon states that the 'the board will reconsider' the two proposals, but has made no commitment beyond this to act on them (or on the others put to shareholders at the meeting).

[Sources: ExxonMobil media release 26/05/2021;: BlackRock voting bulletin: ExxonMobil Corporation 26/05/2021; ExxonMobil preliminary voting results 26/05/2021]

Not a 'singular event'? The spotlight is now on effective board oversight

Both ValueEdge Advisors and MSCI have separately suggested that the success of Engine No 1's campaign is attributable in large part to dissatisfaction with Exxon's board and the board's failure to adapt to changing circumstances/effectively engage with shareholders on their concerns.

MSCI argues that Exxon's board

> 'lacked directors with the experience necessary to oversee a strategic move away from carbon-intensive energy. In fact, our analysis indicates that Exxon had relatively few directors with executive experience in the oil, gas and consumable-fuels industry'.

In addition, MSCI considers that the Exxon boards' 'business as usual' approach fuelled shareholder dissatisfaction. MSCI suggests that,

> 'Beyond Exxon, this vote may serve as a warning to other boards that have dismissed shareholder concerns about climate inaction. It may also spark a rethink on what skills directors need to bring to the boardroom. And for shareholders, it may serve as a reminder of what can be achieved through proxy contests — even against a titan like Exxon'.

Separately, ValueEdge Advisors suggests that Engine No 1's victory signals not only the level of investor concern about the longer-term sustainability of fossil fuel companies, but underlines that ultimately, the level of investor discontent with board oversight in this case, gave Engine No 1 the leverage it needed to be successful in its campaign. As such, ValueEdge considers that the campaign should put other companies on notice.

> 'If investors have no recourse when they are not satisfied with an investment other than selling the stock when it is undervalued, the cost of capital will reflect additional risk. And when it becomes intolerable, a group like Engine No. 1 will recognise the potential for creating value by leveraging shareholder discontent to support meaningful change'.

ValueEdge also suggests that the success of Engine No 1's campaign highlights:

- the need for boards (and organisations) to ensure they are taking steps to 'adapt to the changing environment'. 'Failure to adapt to the changing environment, in both literal and metaphorical senses of the word, can make a company go the way of the manufacturers of buggy whips' Value Edge comments.
- the need for companies not to take their investors for granted and make the effort to engage with/communicate the reasons behind their decisions.

> 'Index funds, pension funds, and other major institutional investors have majority or near-majority permanent holdings. Because they are not going anywhere, if they do not believe the board is providing adequate oversight it is more cost-effective to support activists than to liquidate the position. They may not be willing to mount a dissident campaign themselves but they will be happy to support one. Therefore, you have to make your case to the market every day'.

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 30/05/2021; MSCI blog post 01/02/2021]

A majority of Chevron shareholders have backed a shareholder resolution calling for the company to reduce scope 3 emissions

Six shareholder resolutions went to a vote at the Chevron AGM, none of which had board support.

Shareholder resolution calling on the company to reduce scope 3 emissions

- 60.7% of Chevron shareholders voted in support of a shareholder resolution (filed by Follow This) calling on the company to 'substantially reduce the greenhouse gas (GHG) emissions of their energy products (Scope 3) in the medium- and long-term future, as defined by the Company'.
- The result at Chevron follows majority votes on similar resolutions (also filed by Follow This) at ConocoPhillips (58% support) and Phillips66 (80% support).
- BlackRock voted in support of the resolution as a means of prompting the company to accelerate its efforts. BlackRock states that despite the fact that it considers 'Chevron is on the right path', it supported the resolution

on the basis that it is 'clear and not prescriptive' and 'to reflect our desire to see the company continue to evolve its approach and demonstrate progress on these challenging topics'.

Shareholder proposal calling for the company to publish an audited report on the impacts of a net zero scenario

- 47.8% of Chevron shareholders voted in support of a shareholder ESG resolution (filed by As You Sow), calling on the company to provide an audited report on whether/how a 'significant reduction in fossil fuel demand envisioned in the IEA Net Zero 2050 scenario would affect its financial position and underlying assumptions'.
- According to As You Sow, the proposal had the support of ISS and Glass Lewis.
- Institutional investors:
  - BlackRock issued a voting bulletin confirming that it voted against the resolution because it considers that supporting the resolution 'was not warranted' in light of the steps the company is already taking 'towards a net zero future'.
  - CalPERS also voted in support of the resolution.
- As You Sow president Danielle Fugere has welcomed the result:

> 'With this vote, investors have made it clear that companies must fully address how climate change, and the global energy transition away from fossil fuels, will affect their companies' bottom lines and future success. As demonstrated by the recent IEA net zero scenario, climate impact and risk are fundamentally material and require the same auditing assurance as financial disclosures.'

Other resolutions

- 47.9% of shareholders voted in support of a shareholder resolution calling on the company to report on lobbying payments and policy.
  - BlackRock voted against the resolution on the basis that 'Chevron meets our expectations of companies regarding their activities and disclosures related to political spending and lobbying and has reflected our feedback in its recently updated climate lobbying report.'
  - CalPERs voted in support of the resolution.
- 33.3% of shareholders voted in support of a shareholder resolution calling for the ownership threshold to call special meetings to be lowered from 15% to 10%.
  - BlackRock voted against the resolution on the basis that 'Chevron already provides shareholders the right to call a special meeting at a 15% threshold, which we believe offers shareholders a reasonable opportunity to raise issues of substantial importance without having to wait for management to schedule a meeting'.
  - CalPERs voted in support of the resolution.
- 29.5% of shareholders voted in support of a shareholder resolution calling on the company to adopt a policy for an independent Chair.
  - BlackRock voted against the resolution because it considers that 'Chevron already has a strong leadership structure'.
  - CalPERs voted in support of the resolution.
- 3% of shareholders voted in support of the shareholder resolution calling for the company to become a public benefit corporations.
  - BlackRock voted against this resolution on the basis that ' BIS believes that making changes to the corporate structure of a company is a clearly defined management action and therefore, such a proposal is overly prescriptive and would constrain the business decision-making'.
  - CalPERs also voted against the resolution.

  [Sources: Chevron voting results 26/05/2021; As you Sow media release 26/05/2021; Blackrock voting bulletin: Chevron 26/05/2021]

Ending coal financing: 99% of HSBC shareholders have backed a resolution committing the bank to phasing out financing of coal by 2040

- In January, coalition of shareholders led by ShareAction, filed a resolution at HSBC calling on the bank to publish a strategy and targets to reduce its exposure to fossil fuel assets, starting with coal, on a timeline consistent with the Paris Agreement.

- Following engagement with the company, ShareAction withdrew its resolution in March 2021. With the support of ShareAction, HSBC tabled its own climate resolution committing the company to:
  - setting, disclosing and implementing a strategy with short and medium term targets to align its financing of all sectors (starting with the oil and gas and power and utilities sectors) with the goals of the Paris Agreement
  - publishing an implementing a policy to phase of financing of coal-fired power and thermal coal mining by 2030 in markets in the European Union and the OECD and by 2040 in other markets
  - reporting annually on progress against this strategy, including providing a summary of the methodology, scenarios and core assumptions used.
- At the AGM, 99.71% of shareholders voted in support of the board climate resolution, in line with the board's recommendation.

In a statement welcoming the result, ShareAction Senior Campaign Manager Jeanne Martin cautioned that the passage of the resolution should be seen as only the first step.

> 'We're delighted that our campaign has resulted in a binding commitment by HSBC to phase out coal, but the devil is in the detail and the next six months are crucial to ensure that this commitment is translated into robust sector policies. Part of HSBC's resolution commits it to "publish by the end of 2021 a policy that will… provide further detail on the phase out plan, its scope and interim targets" and to "engage with ShareAction, representatives of the group of co-filing institutions and other stakeholders in the development of this policy." ShareAction is calling on HSBC to ensure that the bank introduces financing restrictions for companies throughout the coal value chain, including those that are highly dependent on coal and building new coal mines, coal plants and coal infrastructure, and calls on its remaining clients to publish phase out plans by December 2023 at the latest'.

ShareAction has also called for HSBC's coal policy to apply to its asset management arm as well as to its banking operations and urged investors to continue to engage with the bank to ensure it sets ambitious targets.

[Source: ShareAction media release 28/05/2021]

Investors are increasingly backing calls for companies to walk the talk on diversity and inclusion: As You Sow has welcomed the increased level of support this year for shareholder DEI resolutions

As You Sow has welcomed the uptick in the level of investor support for shareholder ESG resolutions calling on companies to report on the effectiveness of their diversity, equity and inclusion (DEI) programs so far in 2021.

For example DEI resolutions at the following companies received significant shareholder backing:

- Union Pacific Corporations: 81.4% support (the full text of the resolution is here)
- American Express: 59.7% support (the full text of the resolution is here)
- Berkshire Hathaway: 53.5% of independent shareholder support (27.1% if Warren Buffet and board shares are included) (the full text of the resolution is here)
- Charter Communications Inc: 41.4% support (the full text of the resolution is here)

In addition, As You Sow has welcomed the fact that a majority of companies (70% of S&P 500 companies) have published statements about their commitment to a diverse workplace with many also releasing data on workplace diversity, recruitment, retention and promotion rates.

Principal of the consultancy Whistle Stop Capital and workplace equity program manager at As You Sow Meredith Benton commented that the results underscore the value that investors place on evidence of concrete action on the issue.

> 'Investors are no longer willing to accept feel-good stories about diversity and inclusion programs. Just as investors don't accept vague promises about revenue or operating expenses, they don't want vague promises about DEI results, either. They want hard numbers.'

[Source: As You Sow media release 25/05/201]

Markets and Exchanges

ASIC has released an information sheet on activist short selling in Australia

Key Takeouts

- Preparers of short reports are expected to take active steps to ensure their accuracy, including checking the facts with the target entity before releasing the report
- Preparers of short reports are also expected to release reports outside of Australian trading hours and 'not immediately before market open'
- Target entities are expected to take steps to minimise the chances of being targeted by short sellers (eg by keeping the market updated on key decisions) and if they are targeted, to respond comprehensively and quickly to every assertion in a short report, requesting a trading halt to allow time to prepare a response, where necessary
- Market participants are expected to report suspicious short-selling activity to ASIC as soon as practicable – ie 'once they become aware of the activity, not after they start investigating the activity'

The Australian Securities and Investments Commission (ASIC) has released Information Sheet 255 Activist short selling campaigns in Australia (INFO 255). INFO 255 outlines what ASIC considers to be 'better practices' for activist short sellers and authors of short reports, market operators, target entities and market participants as well as some of the actions ASIC may take in response to activist short selling campaigns.

'Better practices' for activist short sellers and authors of short reports

The information sheet briefly outlines ASIC's expectations around what constitutes 'better practice' for activist short sellers preparers of short reports. Broadly, ASIC considers that:

- The information in short reports should be objective and accurate:
  - Short reports should 'avoid overly emotive, intemperate or imprecise language'
  - Short reports should be 'based on reliable information and any recommendation or opinion should be formed on a reasonable basis'. For example, ASIC states that 'any estimates of security price valuations should be based on quantifiable analysis'.
  - Short reports should not be selective in their use of facts ie they should not deliberately omit facts that do not support their 'thesis'.
- Active steps should be taken to ensure accuracy: Importantly, ASIC considers that, to ensure the accuracy of the information in the report, the authors of short reports should 'check their facts with the target entity to identify and address errors before the release of a short report'.
- Conflicts of interest should be clearly disclosed. For example, ASIC considers that any payment or benefit received by the report authors or material interests in financial products that relate to the target entity should be disclosed. ASIC suggests that it would also be 'responsible practice' to disclose whether the report was commissioned, by whom and their conflicts of interest.
- 'Selective distribution' of short reports should be avoided: ASIC states that:

  > 'Short reports by their very nature are designed to have a price impact, and possession of information about the impending publication of a short report may amount to possession of inside information…Authors of reports that contain inside information should ensure that the report and underlying research is locked down ahead of publication so that the material is not accessible by any parties that do not have a business 'need to know': see RG 264'.
- Short reports should be released outside of Australian trading hours and 'not immediately before market open' to allow 'time for the target entity to prepare a response so the market can be fully informed when the short report is released. It also allows time for investors to digest the information before trading recommences'.

Better practice for target entities

INFO 255 suggests that target entities can take steps to 'make themselves less appealing to activist short sellers' including through ensuring the market has access to clear and timely information around their business models and financial statements and ensuring that they provide investors with decision-useful information.

Where entities do become a target, ASIC suggests that they employ the following 'strategies'.

- Responding to a short report: ASIC expects target entities to respond to short reports promptly and that the response will address each claim in the short report 'with sufficient detail and where possible backed up with evidence'. ASIC comments that 'broad statements dismissing an entire report as being false are unlikely to address investors concerns'.
- Timely response is expected:
  - Where a target entity has no prior notice of the short report, and the short report is likely to have a material impact on the price or value of their securities, ASIC's expectation is that the target entity 'immediately request a trading halt' to allow time for them to prepare a detailed response.
  - Where a target entity is notified before the release of a short report, ASIC's expectation is that they have a detailed response prepared to release 'at around the same time the report is to be published and before trading in the target entity's securities recommences'. Should the target entity dispute the claims in the report, ASIC's expectation is that they request a trading pause to give them time to prepare a detailed response, to ensure that investors have all relevant information before trading recommences.

Better practice for market operator listing authorities

Broadly ASIC considers that in the interests of ensuring the market is kept properly informed, and that 'all key stakeholders comply with relevant listing rules and the Corporations Act' market operators should:

- Pause trading where it becomes aware that a listed entity is the target of a short report that has had a material price impact
- Request the target entity to provide a detailed response to the report as soon as possible
- Consider, in light of the information in the short report, the target entity's response and previous disclosures whether the market may have been misinformed and whether there may have been any breaches of the Listing Rules. Market operators are then expected to take 'appropriate regulatory action' eg seeking additional disclosure and/or referring the matter to ASIC.
- Monitor the impact of any follow up short reports on the price of the entity's securities and assess whether the target entity should provide additional information in response to any new issues raised.

Better practice for market participants

ASIC expects market participants to report suspicious short-selling activity to ASIC as soon as practicable – ie 'once they become aware of the activity, not after they start investigating the activity'.

Steps ASIC may take

INFO 255 briefly outlines the range of steps ASIC may take in response to activist short-selling campaigns. These include:

- examining the trading activity of short sellers throughout the campaign
- engaging with the activist short sellers (where their identity is known) to:
  - ascertain whether they have conducted a financial service in Australia and if so, whether they hold the necessary licence
  - testing the accuracy of the claims in the short report
  - the process and timing of the short report's release and its impact on the market
  - how conflicts of interest are disclosed
  - where the activist short seller is based outside Australia, 'engaging with their home regulator, and taking action for breaches of the law (see INFO 151)'.
- engaging with the target entity both to 'test the veracity of the claims in the short report and the target entity's compliance with financial services law'
- engaging with the market operators on 'steps to ensure a fully informed market, on the timing of trading halts and to consider the claims in short reports'.

[Sources: ASIC media release 01/06/2021; ASIC Information Sheet 255: Activist short selling campaigns in Australia]

Financial Services

Top Story | Two (plus) years on: Tracking progress against each of the Hayne Commission's 76 recommendations

The Financial Services Royal Commission's final report was publicly released on 4 February 2019. In the two (plus) years since its release a number of actions have been implemented in response – though in many cases, the changes have yet to commence or are yet to be completed.

We have prepared a table briefly outlining the actions taken to date and/or the planned actions to be implemented in response to each of the Commission's 76 recommendations.

This can be accessed here.

Open banking: The ABA and consumer groups oppose the proposed 'opt-out' joint account data sharing model

Context

Treasury and the Data Standards Body are consulting on the development of rules and standards to implement: a) a peer-to-peer data access model in the energy sector; and b) an 'opt-out' data sharing model for joint accounts in the banking and energy sectors. Consultation closed on 26 May 2021. You can find our short overview of the consultation in Governance News 05/05/2021 at p21

Concerns raised

In a joint submission, the Financial Rights Legal Centre (FRLC), Consumer Action Law Centre (CALC) and the Australian Communications Consumer Action Network (ACCAN) outlined seven reasons for their strong opposition to the proposed 'opt-out' joint account data sharing model.

Broadly, the groups argue that the proposed approach:

- 'contradicts and undermines the consent model central to the Consumer Data Right (CDR)'
- 'runs counter to current privacy principles';
- 'runs counter to recommended strengthened consent requirements and pro-consumer defaults in the Privacy Act';
- 'wrongly equates one's transaction preferences with their privacy preferences';
- 'prioritises the business interests of the FinTech sector over the interests of consumers to maintain privacy and security';
- 'will undermine consumer trust in CDR'; and
- 'increases risks to those subject to financial abuse, elder abuse, or domestic or family violence'.

The Australian Banking Association's (ABA's) submission raises similar concerns and the ABA has also called to the opt-in approach to be retained on this basis.

Like the joint submission, the ABA considers that the proposed approach 'undermines the foundational principle of the CDR, which is informed consent'. The ABA's submission also questions the need for further amendments to the consent model given the lack of 'evidence that the opt-in model is a problematic friction point' and given the potential for the proposed change to confuse consumers and potentially undermine trust in the CDR.

[Source: Joint submission by Financial Rights Legal Centre, Consumer Action Law Centre and the Australian Communications Consumer Action Network on Australian Treasury's 'Opt-out' joint account data sharing model 26/05/2021; ABA submission 26/05/2021]

COVID-19 has accelerated debit card use according to ABA data

Analysis by the Australian Banking Association (ABA) shows that the pandemic has accelerated continuing trends towards increased use of debit cards (over other methods of payment) and a decline in the use of cash.

For example, over the course of 2020:

- use of debit cards jumped 17%, making them the most popular payment method online or in person. Use of debit cards has been increasing since 2002 and is now almost triple the use of credit cards.
- cash withdrawals fell 10%. Use of cash has been trending downwards since 2008 and this trend was accelerated by the push for cashless transactions in 2020.
- use of cheques declined by almost 40% accounting for less than 0.3% of all payment transactions for the year. In contrast, in 2002, cheques made up 19% of all transactions.

[Sources: ABA media release 28/05/2021; Further data]

Green steel push: Six global banks to develop best practice principles for the continued funding of steel making in line with the goals of the Paris Agreement

- Ahead of the United Nations Climate Change Conference in November 2021 (COP26), and under the banner of the Mission Possible Partnership (MPP), six global banks - Citi, Goldman Sachs, ING, Societe Generale, Standard Chartered, and UniCredit - have established a working group called the Steel Climate-Aligned Finance Working Group.
- The aim of the group is to develop an industry-backed agreement around the best pathway to achieving net-zero steel making by 2050 and how financial institutions can best align their continued financing of steel with this goal.
- The agreement will be modelled on the Poseidon Principles, the first sector-specific climate-aligned finance agreement for maritime shipping, which were launched in 2019.
- The Rocking Mountain Institute (RMI) Center for Climate-Aligned Finance (the Center) will facilitate engagement between the Working Group and the Net-Zero Steel Initiative (NZSI) (which also falls under the Mission Possible Partnership banner) to ensure alignment between the objectives of steelmakers and the lenders.

[Sources: RMI media release 27/05/2021; ING media release 27/05/2021]

Product Intervention Power: New Bill proposes to remove 'ambiguity' around ASIC's power to intervene

Treasury Laws Amendment (2021 Measures No. 4) Bill 2021 was introduced into the House of Representatives on 26 May 2021.

Among other measures:

- Schedule 4 of the Bill proposes to amend s1023D(4)(c) of the Corporations Act 2001 (Cth) and paragraph 301D(4)(c) of the National Consumer Credit Protection Act 2009 (Cth) to 'provide that ASIC is not prohibited from making a product intervention order that has conditions relating to fees, charges or other consideration payable by a retail client or consumer in relation to a financial product or a credit product'.
- According to the Explanatory Memorandum the changes are needed to 'to address unintended outcomes and to ensure that the product intervention regime operates as intended'. More particularly, the Explanatory Memorandum states that the proposed changes will remove any 'ambiguity' around ASIC's ability 'to intervene in relation to the costs of a financial and credit product (such as administrative fees, interest charges, surcharges, or default fees) paid by a retail client or consumer, through the use of a product intervention order'. This is considered 'critical for retail client and consumer protection against significant detriment'.
- Proposed date of effect: It's proposed that the changes in Schedule 4 will apply from the date of Assent.

[Source: Treasury Laws Amendment (2021 Measures No. 4) Bill 2021]

Culture in the superannuation sector: APRA has outlined some examples of what it considers best practice in risk culture

In her speech to the ASFA Spotlight on Risk and Compliance event, Executive Director of the Australian Prudential Regulation Authority's (APRA's) Superannuation Division, Suzanne Smith spoke on the theme of risk culture in the superannuation context and talked through several examples of what APRA considers to be good practice.

- 'Transforming' GCRA continues to be a focus for APRA: Ms Smith said that in recent years APRA has stepped up its focus on transforming and improving governance, culture, remuneration and accountability (GCRA) standards across all regulated sectors, with a particular emphasis on risk culture (ie an entity's attitude to risk management), including taking enforcement action where appropriate. Ms Smith said that APRA's 'chief concern when it comes to misconduct…is what it says about an institution's culture, and whether that culture potentially enables or even encourages damaging behaviour'.

- Board composition and risk culture flagged as key areas of focus: Ms Smith said that two areas of concern identified through the risk governance self-assessments of 2018/2019 and the recent Supervisory Risk and Intensity (SRI) assessments in the superannuation context are: a) 'instances of immature risk cultures, an approach to risk management that has not kept pace with the growth and maturity of the organisation'; and b) 'sub-optimal board composition including the lack of specific trustee capabilities, and conflicts of interest'.
- What 'good looks like': Ms Smith spoke briefly about the way in which APRA assesses risk culture, and underlined that the regulator does not look at 'any one measure' but rather 'assess trustees against 10 different factors', the 'Risk Culture 10 Dimensions'. These ten dimensions are: 1) Leadership; 2) Risk appetite and strategy; 3) Decision-making and challenge; 4) Communication and escalation; 5) Risk capabilities; 6) Risk governance and controls; 7) Responsibility and accountability; 8) Performance management and incentives; 9) Shared values; and 10) Risk culture assessment. Ms Smith then 'walk[ed through' some examples of what APRA considers constitutes good practice and what types of practice give APRA 'cause for concern'.
- Leadership: The 'tone from the top': Ms Smith observed that 'nothing influences an institution's risk culture more than the words and actions of its board and senior executives – the tone from the top'. Ms Smith said that APRA is looking for organisations to have strong role models who: a) 'champion the importance of risk culture and ensure good risk management is embedded across the business'; b) regularly and actively monitor risk culture; c) take steps to address weaknesses and mitigate risks; and d) 'deal proactively with poor risk outcomes'.
- Decision-making and challenge: The approach to decision making is another focus for APRA. Ms Smith said that APRA is looking to see: whether 'decision-making is dominated by one individual or a small group of individuals'; whether risk is 'recognised as a critical part of the decision (or whether 'the voice of risk is silenced'); whether decision making 'shows respect for differing viewpoints'; and whether staff are encouraged and feel able/comfortable to constructively challenge decisions and are given feedback. Ms Smith also observed that APRA considers that an organisation's attitude to diversity and inclusion, can be a 'key factor in creating a speak-up culture.
- Individual acceptance of responsibility and accountability for risk across the three lines of defence is 'critical' in fostering an effective risk culture Ms Smith said. Ms Smith said that 'APRA gets concerned when we see evidence of individuals who avoid taking responsibility for risk in case they are blamed if something goes wrong, where individuals are not held accountable when things do go wrong, where issues drag on with no attempt to identify underlying causes, and where accountabilities for risk are not defined across the entity'. Ms Smith observed that the introduction of the Financial Accountability Regime (FAR) 'will be an important lever in bringing greater transparency to those accountable in superannuation, and something trustees should be thinking about now in readiness for its implementation'.
- Lessons from the BEAR: Ms Smith said that APRA recently 'had a look at' how the Banking Executive Accountability Regime (BEAR) has been implemented in three major Australian banks. APRA found that the BEAR has: a) clarified individual accountabilities across the organisations; b) 'sharpened challenge by boards on actions taken by accountable persons to meet their obligations'; and c) 'led to more targeted engagement between APRA and the entities to deliver prudential outcomes'. In this context, Ms Smith said that APRA considers it 'essential that an individual's behaviours are aligned with the entity's espoused values around risk management, which we assess through the dimension of shared values'. Ms Smith said that 'in terms of what good looks like we expect to see values being lived throughout the entity, where time and effort is spent by people to refresh and communicate shared values and that the values are maintained, even in periods of significant growth or crises. Simply posting a set of values somewhere on an intranet, or putting up a motivational poster on the wall, is some distance from best practice in this area'.
- Remuneration should incentivise good risk management behaviour: Ms Smith said that APRA's new standard (CPS 511) will 'lead to stronger incentives for individuals to proactively manage non-financial risks, and appropriate financial consequences where material risk incidents have occurred' as well as to increased transparency and accountability for remuneration outcomes. Ultimately, Ms Smith said that remuneration structures should ensure 'good risk management behaviour is rewarded and poor risk behaviour faces proportionate consequences'. Ms Smith said that 'signs of a weak risk culture in this area include performance objectives that don't reference risk

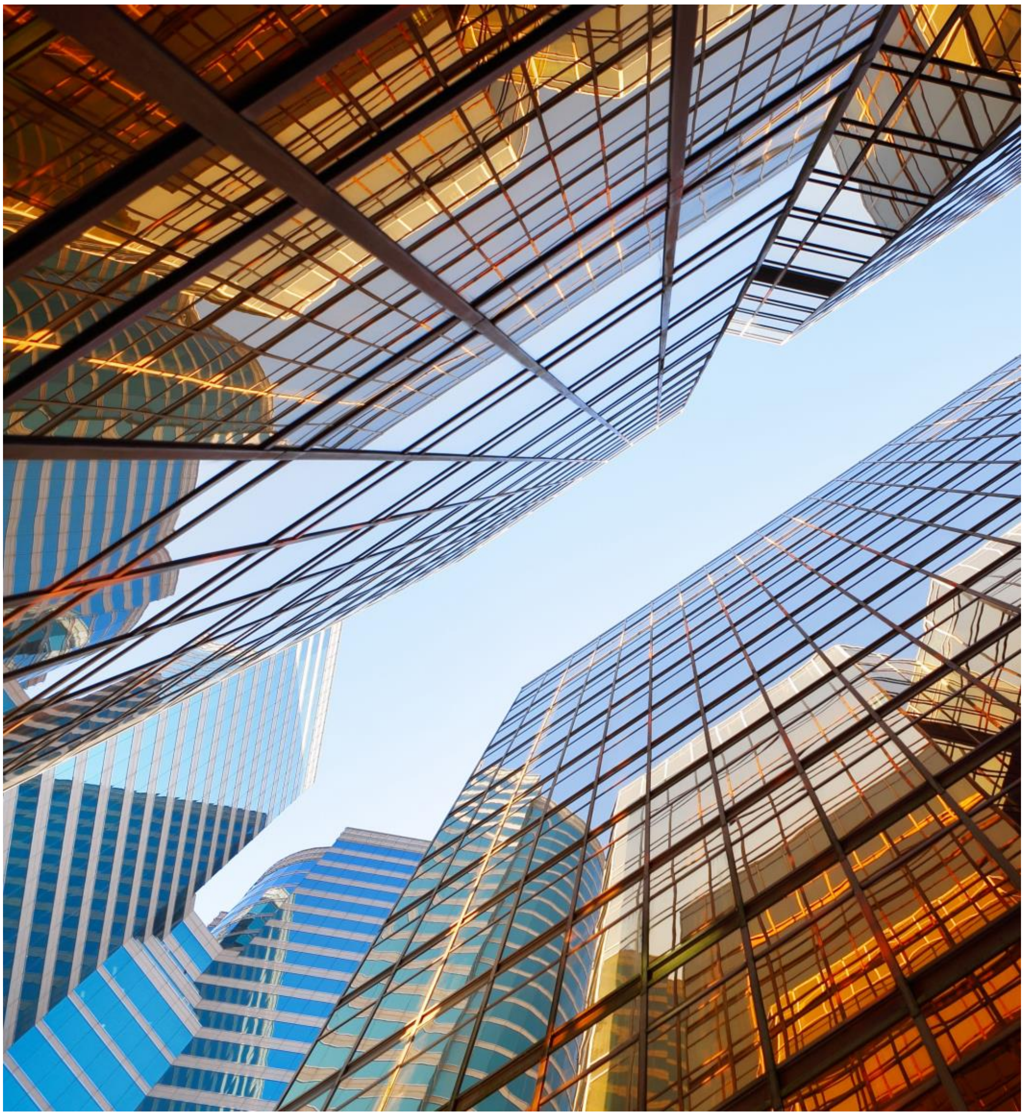
management or risk culture, or hiring and promotion decisions that fail to incentivise staff to demonstrate sound risk management behaviours'.

- **Risk culture survey:** Ms Smith said that APRA is piloting a risk culture survey which it plans to roll out to a 'number of superannuation entities in 2022'. This will involve surveying staff within entities focusing on all ten risk dimensions. Ms Smith said that APRA plans to discuss its findings with entities, 'including how they shape up against peers, so that we can help enhance and reinforce risk culture across the sector'.

  [Source: APRA Executive Director, Superannuation Division, Suzanne Smith - Speech to the ASFA Spotlight on Risk and Compliance event 27/05/2021]

The RBA has confirmed it has no plans to force BNPL providers to remove their no-surcharge rules (for now)

Following earlier consultation on the matters raised in the Review of Retail Payments Regulation issues Paper released in 2019, The Reserve Bank of Australia (RBA) has issued a consultation paper seeking feedback on its proposed policy actions, together with proposed changes to three existing card systems payment standards (that reflect the bank's preferred approach).



Proposed changes to the standards

- The RBA proposes to amend Standard No. 1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers to:
  - remove references to the American Express Companion Card system
  - require schemes to publish the interchange fees for domestic transactions on foreign-issued cards on their websites
  - formalise recent guidance about when and how new issuers should begin certifying compliance with the net compensation provisions (with a minor technical revision to the definition of 'Core Service').

This standard would apply to the MasterCard Credit Card System and the Visa Credit Card System

- The RBA proposes to amend Standard No. 2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers to:

- replace the current cents-based debit (and prepaid) interchange fee cap (15 cents per transaction) with lower caps: 10 cents for dual network debit cards (DNDCs) and 6 cents for single network debit cards (SNDCs). The RBA states that this is intended to 'limit the possibility of schemes using interchange rates to incentivise SNDC issuance, which could accelerate the shift towards SNDCs'.
- require schemes to publish the interchange fees for domestic transactions on foreign-issued cards on their websites
- formalise recent guidance about when and how new issuers should begin certifying compliance with the net compensation provisions (with a minor technical revision to the definition of 'Core Service').

This standard would apply to the eftpos, MasterCard and Visa debit card and prepaid card systems

- The RBA also proposes to amend Standard No 3 of 2016: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions to remove references to the American Express Companion Card system.

The proposed changes to the standards (in mark up) are included in Appendix B at p59 of the consultation paper.

Policy proposals

Surcharging: No changes to existing no surcharge rules

- The RBA does not propose to require buy now pay later (BNPL) providers to remove their no-surcharge rules 'at this time'.
- However the RBA states that it will 'continue to monitor developments in the industry and will review the case for the removal of no-surcharge rules in emerging payment methods, including BNPL schemes, on a regular basis'.

Dual network debit cards (DNDCs) and least cost routing (LCR)

Broadly, the RBA is proposing the following policy framework for DNDCs and LCR:

- The RBA would 'state an explicit expectation' that the major banks will continue to issue DNDCs, 'with both schemes to be provisioned in all relevant form factors offered by the issuer (such as in mobile wallets as well as physical cards)'. At this stage, the RBA does not intend to extend the requirement to issue DNDCs beyond the major banks.
- The RBA's interchange standards would be amended to set a lower cents-based interchange cap for single network debit card (SNDC) transactions than for DNDC transactions (as is reflected in the proposed changes to Standard No. 2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers described above).
- The RBA would:
  - 'state an expectation that all acquirers and payment facilitators (which provide card acceptance services to merchants) will offer and promote LCR functionality to merchants in the device-present (in-person) environment'.
  - state an expectation that the industry will follow a set of principles regarding the implementation of LCR in the device-not-present (online) environment.
- The RBA would also 'explicitly prohibit schemes from engaging in "tying conduct" involving their debit and credit card products'. Having said this, the RBA makes clear that though it wishes to address 'tying conduct' – ie address the issue of eligibility for low strategic interchange rates on credit card transactions being linked to the value and/or volume of merchant's debit card transactions - 'at this stage the Board is agnostic on whether this is best achieved through voluntary undertakings with the schemes, or by introducing a new standard expressly prohibiting any such tying conduct'. The consultation therefore does not include a proposed draft standard prohibiting this conduct.

Scheme fees

Schemes would be required to:

- provide the RBA with access to their scheme fee schedules and all scheme rules, and to notify the RBA 'promptly of any changes'.
- provide quarterly data on scheme fee revenue and rebates to the RBA.

Interchange fees

- The RBA proposes to introduce a requirement for schemes to publish interchange fees on transactions on foreign issued cards on their websites. The RBA considers that this would be a 'low cost way of shining a light on these relatively high fees'. This is reflected in proposed changes to Standard No 1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments and Standard No 2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments.

Timing:

- The due date for submission is 9 July 2021.
- The RBA expects to make a final decision on the changes to the interchange standards at its August or November meeting
- There is as yet no timeline for implementation of the changes once finalised – the RBA is seeking stakeholder views on an appropriate timeframe.

[Sources: RBA media release 28/05/2021; Consultation paper]

AFCA appoints two new Lead Ombudsmen

The Australian Financial Complaints Authority (AFCA) has announced the appointment of two new Lead Ombudsmen, for Insurance and for Small Business.

- Emma Curtis (Australian Securities and Investments Commission (ASIC) Senior Executive, Insurers) will take over from John Price, as Lead Ombudsman Insurance from 9 August 2021.
- Suanne Russell (Head of Business Bank Legal at Westpac) will be the new Lead Ombudsman Small Business. Ms Russell will take up her role on 2 August 2021.

[Source: AFCA media release 31/05/2021]

In Brief | APRA/ASIC oversight body: The Financial Regulator Assessment Authority Bill 2021 and the Financial Regulator Assessment Authority (Consequential Amendments and Transitional Provisions) Bill 2021 have been read a third time in the House and are headed to the Senate

[Source: Financial Regulator Assessment Authority Bill 2021; Financial Regulator Assessment Authority (Consequential Amendments and Transitional Provisions) Bill 2021]

In Brief | Expelled from membership of AFCA: AFCA has published the details of five financial firms that have failed to pay their AFCA membership levy and/or other fees. AFCA has called on the firms in question to contact AFCA 'to discuss payment options for any outstanding fees and reinstate their membership, if they are still required by law to be an AFCA member'

[Source: AFCA media release 31/05/2021]

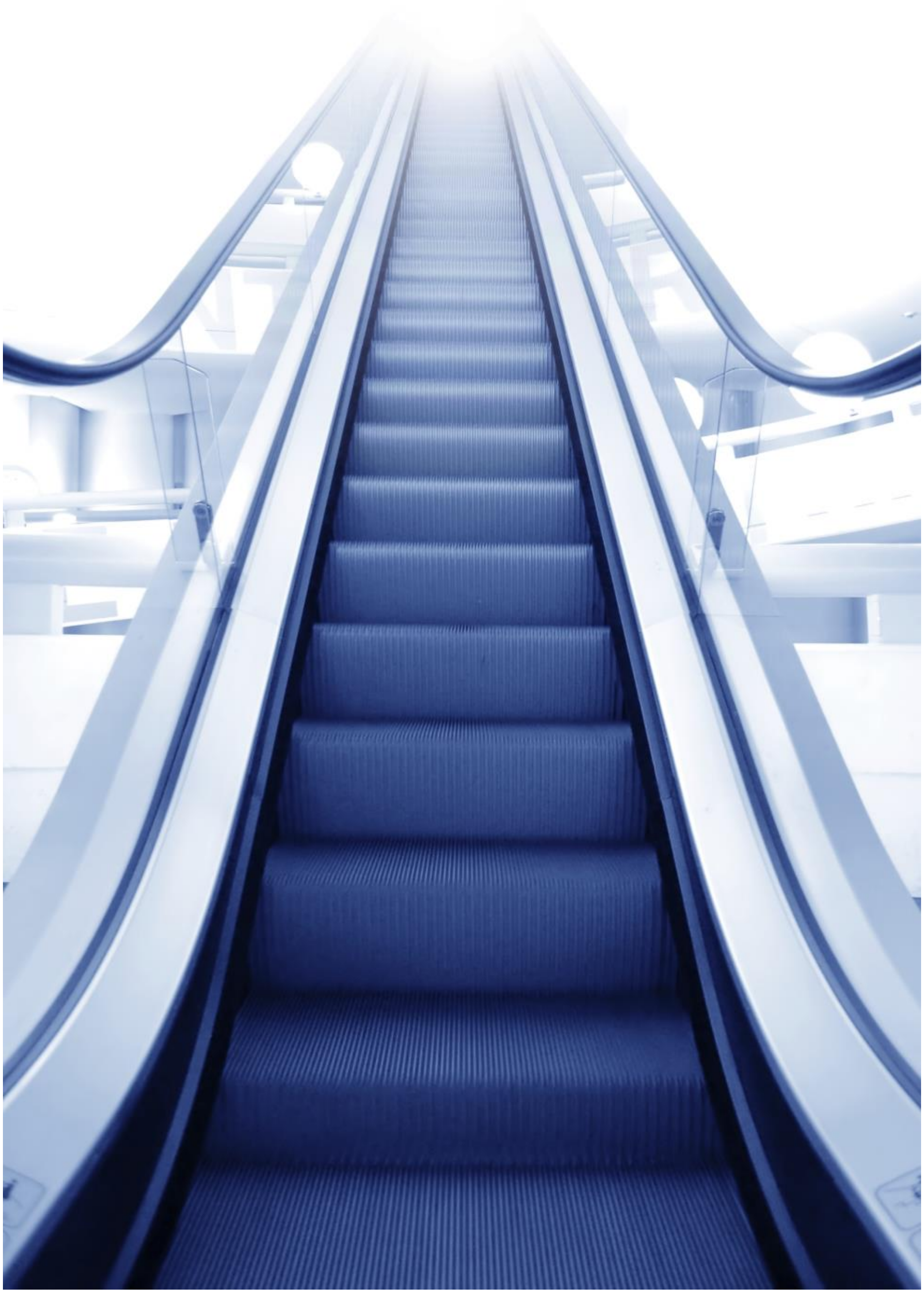
In Brief | 'Time is running out': ASIC has again urged firms to prioritise the transition away from LIBOR. ASIC has also flagged its intention to start a second round of communication with corporations and buy-side firms to 'highlight the urgency of LIBOR transition'

[Source: ASIC media release 27/05/2021]

Accounting and Audit

EU Financial Services Commissioner launches a process to lift the quality of reporting and enforcement in the wake of the Wirecard scandal

In a recent speech entitled Corporate reporting in the Capital Markets Union after Wirecard, European Commissioner for Financial Services Mairead McGuinness reflected on the Wirecard scandal as an illustration of the failure of the 'three pillars of corporate reporting': corporate governance, audit and supervision.



Commissioner McGuinness commented

> 'For me, it [the Wirecard collapse] serves as a clear reminder that there is no smoke without fire. And Wirecard is not the only corporate reporting failure. Clearly there is cause for concern…Wirecard is a very severe wake-up call. The company told and sold a great story that wasn't true. Meanwhile those who reported the real story were ignored'.

Because of this, Commissioner McGuinness announced that a process to lift the quality of corporate reporting and enforcement has been launched with a view to presenting a legislative proposal 'towards the end' of 2022. This process will include a public consultation on what changes are needed.

Commissioner McGuinness outlined some of the considerations that will be taken into account as part of this process. These include:

- How the role of audit committees can be improved eg whether audit committees should be mandatory, how oversight can be strengthened
- The reasons for the lack of quality in audits eg the extent to which this may be related to lack of competition in the audit market and/or to conflicts of interest (because audit firms are focussing on 'more attractive non-audit services'.

- Whether auditors are 'shielded too much from liability or from the risk of supervisory sanctions'
- The supervision of auditors and transparency around supervisory practices
- How to strengthen/improve the effectiveness of enforcement and supervision across borders including: how cooperation between authorities at the national and European level can be enhanced, how the governance/independence of supervisors at national level can be strengthened and how supervision of company information across the EU can be 'harmonised'.
- How to ensure that the 'ecosystem' is 'open to information' eg from whistleblowers or in the media, that 'runs counter to received wisdom'.

[Source: Speech by Commissioner Mairead McGuinness at the European Policy Centre: Corporate reporting in the Capital Markets Union after Wirecard 27/05/2021]

UK Audit Reform: The UK FRC has published updates to its auditing standard on the responsibilities of auditors relating to fraud

The Financial Reporting Council (FRC) has published a revisions to the auditing standard on the responsibilities of auditors relating to fraud: ISA (240) The Auditor's responsibilities relating to fraud in an audit of financial statements.

The FRC states that the revisions are

> 'designed to provide increased clarity as to the auditor's obligations, addressing the concern raised by Sir Donald Brydon in his review of the quality and effectiveness of audit. The revisions include enhancements to the requirements for the identification and assessment of risk of material misstatement due to fraud and the procedures to respond to those risks'.

The revised standard is effective for audits of periods beginning on or after 15 December 2021 (with early adoption permitted).

BEIS consultation?

The Department for Business, Energy and Industrial Strategy (BEIS) is currently consulting on proposals for audit reform with a view to 'restoring trust in corporate governance and audit'. The proposals respond to the recommendations made by the three independent reviews commissioned by the government in 2018:

- Sir John Kingman's Independent review of the Financial Reporting Council
- the Competition and Market Authority's statutory audit market study
- Sir Donald Brydon's independent review of the quality and effectiveness of audit

The FRC states that it will 'address these proposals in due course, taking account of the outcome of the BEIS consultation'.

[Source: FRC media release 18/03/2021; ISA (240) The Auditor's responsibilities relating to fraud in an audit of financial statements]

Risk Management

Climate Risk

A novel duty of care in negligence? Federal Court holds that the Minister for the Environment has a duty to protect young people from the health effects of climate change

In Sharma by her litigation representative Sister Marie Brigid Arthur v Minister for the Environment [2021] FCA 560, eight young people (under the age of eighteen) with the assistance of litigation guardian Sister Brigid Arthur, sought an injunction to prevent the Commonwealth Minister for the Environment from allowing the extension of a coal mine project (the extension project) to go ahead on the basis that allowing it to do so would constitute a breach of the Minister's duty to protect young people from the impacts of climate change.

Key Takeaways

- The Minister owes a duty of care in negligence: Justice Bromberg held that the Minister for the Environment owes a duty of care to protect children from the health effects of climate change when exercising her power under s130 and s133 of the Environment Protection and Biodiversity Conversation Act 1999 (Cth) (EPBC Act) because 'a reasonable person in the position of the Minister would foresee that the approval of the Extension Project would expose the Children to a risk of personal injury'.

  In his official summary of the decision, Justice Bromberg states,

  > 'The evidence demonstrates that a reasonable person in the position of the Minister would foresee that, by reason of the Extension Project's effect on increased CO2 in the Earth's atmosphere and the consequential increase in global surface temperatures, each of the Children is exposed to a risk of death or other personal injury. The evidence therefore establishes an essential precondition for the law of negligence to recognise a duty of care owed by the Minister to each of the Children'.

- Justice Bromberg dismissed the children's claim for an injunction on the basis that he was not persuaded that a reasonable apprehension of breach of the duty of care by the Minister had been established. However, Justice Bromberg stated that 'the grant of any injunctive relief that may be appropriate await the Minister making either a proposed decision or alternatively a decision under s 130 and s 133 of the EPBC Act to approve or not approve the Extension Project'.

[Source: Sharma by her litigation representative Sister Marie Brigid Arthur v Minister for the Environment [2021] FCA 560, 27 May 2021]

Australia's emissions are at record lows according to the latest National GHG inventory quarterly update

- According to the latest National Greenhouse Gas Inventory Quarterly Update, emissions for the year to December 2020 are 5.0% (26.1 Mt CO2-e) down on the previous year at 499.0 Mt carbon dioxide equivalent (CO2-e). According to the report, this is the 'lowest emission level ever recorded in the National Greenhouse Gas Inventory'.
- The drop in emissions is attributed in part to the 'continuing short-term effects of COVID-19 restrictions on emissions from transport, which fell 12.1%' as well as to ongoing reductions in emissions from electricity (down 4.9%) and an 8.8% drop in fugitive emissions, partly due to reduced coal production.
- Welcoming the report findings, Minister for Energy and Emission Reduction Angus Taylor said that 'between 2005 and 2019, the last year for which comparable data is available, Australia reduced emissions faster than many similar economies, including Canada, New Zealand, Japan and the United States'.
- Commenting briefly on the key drivers in lowering emissions, Mr Taylor said that the 'continuing structural decline in emissions from electricity is driven by Australia's world-leading deployment of solar and wind'.
- Commenting briefly on fugitive emissions, Mr Taylor said that the 'the ramp up of the Gorgon carbon capture and storage facility in Western Australia [is] making a significant contribution'.
- Mr Taylor reiterated the government's $C1.6 billion budget commitment (announced as part of the 2021-22 Budget) to 'bolster Australia's position as a leader in low emissions technologies and to meet Australia's emissions reduction targets'.

[Source: National Greenhouse Gas Inventory Quarterly Update; Minister for Energy and Emission Reduction Angus Taylor media release 31/05/2021]

In Brief | The Hague District Court has ordered Royal Dutch Shell to reduce the CO2 emissions of the Shell group by net 45% in 2030, compared to 2019 levels in a case brought by Friends of the Earth. In a statement welcoming the finding, Friends of the Earth expressed the hope that the judgement will 'trigger a wave of climate litigation against big polluters, to force them to stop extracting and burning fossil fuels'

[Sources: English translation of the judgement; Friends of the Earth media release 27/05/2021; Podcast: Sam Cossar-Gilbert from Friends of the Earth Australia discusses the case]

In Brief | Canada: New expert legal opinion from Randy Bauslaugh, in collaboration with the Canada Climate Law Initiative (CCLI), concludes that pension fund fiduciaries have a duty to take into account the financial risks and opportunities related to climate change when managing plan assets

[Source: Randy Bauslaugh, legal counsel McCarthy Tetrault LLP: Climate Change: Legal Implications For Canadian Pension Plan Fiduciaries and Policy-Makers]

In Brief | New report calls for global investments in nature-based solutions to triple by 2030 and quadruple by 2050 on current levels, in order to tackle urgent climate, biodiversity and land degradation challenges

[Source: WEF Report: State of Finance For Nature]

Cybersecurity, Privacy and Technology

The Reserve bank of New Zealand has committed to implementing measures to strengthen its cybersecurity systems

Key Takeouts

- Following the Accellion data breach, and two unrelated incidents where data was unintentionally disclosed to certain groups before being made public, the RBNZ has released two independent reports into the incidents and committed to implement the recommended actions to strengthen its existing approach to cybersecurity, privacy and data handling.
- Among other recommendations around strengthening and formalising the bank's internal control systems/processes, the report into the Accellion breach recommends that the bank develop a stronger framework for third party risk management and integrate 'baseline standards for vendor communication' into all vendor agreements.

The Reserve Bank of New Zealand (RBNZ) has released two independent reports.

Data breach report

Key causes

The first report was prepared by KPMG and assessed the causes of the December 2020 Accellion data breach and the bank's immediate response. The report found that though 'the direct cause of the incident…could not have been predicted, there were several key contributing factors which directly impacted the scale and impact of the data breach.'

These included:

- Accellion's failure to notify RBNZ of the availability of software updates to address the vulnerability in December 2020 (because the email tool failed to send), which meant that the bank was not notified until 6 January 2021
- Accellion's failure to notify RBNZ that the system vulnerability was being 'activity exploited at other customers'
- RBNZ's use of the system as an information repository and collaboration tool, rather than as purely a file transfer system (contrary to RBNZ's 2014 guidelines on 'acceptable use of the system')
- RBNZ's failure to identify/follow up on initial alerts of potential malicious activity on the system in December 2020
- Failure of key 'key controls and working practices' that were within RBNZ's control
- Failure by RBNZ to ensure that a Certification and Accreditation process of the system was undertaken to ensure that any key risks were identified and managed

In a statement RBNZ Governor Adrian Orr accepted these findings.

> 'While we were the victim of a widespread illegal attack on the file sharing system, the Reserve Bank takes full responsibility for our shortfalls identified in the KPMG report. We were over reliant on Accellion – the supplier of the file transfer application (FTA) – to alert us to any vulnerabilities in their system. In this instance, their notifications to us did not leave their system and hence did not reach the Reserve Bank in advance of the breach. We received no advance warning. KPMG outline that there are controls and practices within the Bank that needed to be, and are being, improved. If these practices were in place at the time of the illegal breach the impact would have been less'.

Mr Orr went on to say that he is however confident that the RBNZ has 'responded with urgency, precision, and care' to the breach, and committed to implementing the recommended actions to improve the bank's approach.

Key recommendations

- The report includes number of recommendations to strengthen the bank's systems, controls and processes, all of which the RBNZ has accepted and has commenced implementing.
- Key recommendations include (among others), that the bank:
  - conduct more frequent 'incident simulations' to ensure key staff are familiar with all of the requirements of the Major Incident Response Plan
  - review ongoing security training requirements for staff supporting critical systems
  - review monitoring and alerting protocols for all key security and operational alerts
  - formalise a program of audits, risk assessments and user awareness of policies and procedures to help ensure vulnerabilities, potential threats and attacks are picked up more quickly
  - integrate the cyber and enterprise risk management frameworks to ensure consistent risk treatment and/or reduce gaps in risk identification
  - clarify staff roles/responsibilities
  - develop and integrate into all vendor agreements, 'baseline standards for vendor communication', including requirements for maintaining/updating contact lists and agreed escalation protocols.
  - 'develop a framework for third party risk management that assesses the risk associated with all critical providers and defines controls that have been implemented'
- The Bank estimates that the final cost of the breach response, including internal resources, will be approximately $3.5 million.

Handling of sensitive information

- The second report was prepared by Deloitte and investigated the bank's handling of sensitive information following two incidents at the end of 2020 in which sensitive information was inadvertently disclosed to a small group of firms before being made public.
- The report includes a number of recommendations to improve the bank's handling of sensitive information and to reduce the likelihood similar incidents going forward. Recommendations include (among others):
  - updating existing classification categories to make it easy for users to accurately classify information;
  - creating information handling procedures for each classification category (as defined in the updated policy) which sets out how information should be stored, handled and shared with
  - enabling the 'easy classification' of files created or received by bank employees
  - rolling out user-awareness campaigns/training

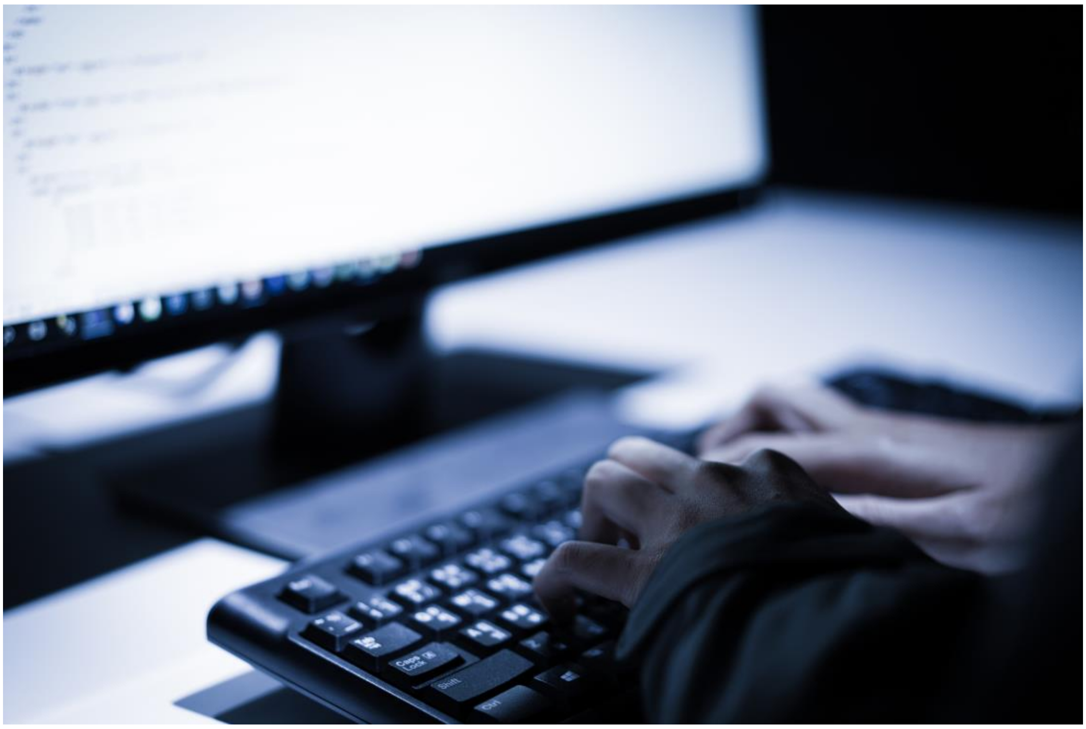
- reviewing the list of persons within the bank who have access to folders that may contain sensitive information to ensure that they access is necessary for them to perform their role
- treating 'all incidents related to sensitive information as a data breach, to make sure the relevant stakeholders are informed and the right process for response, communication and investigation are executed in a timely manner'.
- 'creating a playbook specifically for the management of incidents that relate to information breaches, with the key activities to undertake during the response process'.

[Sources: RBNZ media release 31/05/2021; Official summary of KPMG Reserve Bank of New Zealand Incident Assessment report; February 2021 - Deloitte Report into internal information breaches]

Working to restore systems: JBS foods has confirmed it was targeted by a cyber attack

Meat processor JBS has confirmed it was the victim of a cyber-attack which has impacted some servers supporting its North American and Australian IT systems.

In a short statement the company said that:



- all systems impacted were immediately suspended and relevant authorities were notified.
- back-up systems were unaffected and the company is working to restore systems as 'soon as possible'. However the company expects that resolution of the issue will take time and 'may delay certain transactions with customers and suppliers'.
- The company stated that at this stage it is 'not aware of any evidence…that any customer, supplier or employee data has been compromised or misused as a result of the situation.'

[Source: JBS USA media release 31/05/2021]

In Brief | The risk of cyber attack continues to accelerate and boards are taking notice (but they need to do more): The Australian previews some of the key findings in MinterEllison's sixth annual cyber-risk report

[Source: [registration required] The Australian 01/06/2021]

Other News

Litigation funding and the regulation of the class action industry: Consultation on plans to guarantee a minimum rate of return for class action members launched

- On 21 December 2020, the Parliamentary Joint Committee on Corporations and Financial Services (PJC) handed down its report: Litigation funding and the regulation of the class action industry.
- The report included 31 recommendations including recommendation 20 which recommended that: the government consult on:
  - 'the best way to guarantee a statutory minimum return of the gross proceeds of a class action (including settlements)';
  - 'whether a minimum gross return of 70 per cent to class members, as endorsed by some class action law firms and litigation funders, is the most appropriate floor'; and
  - 'whether a graduated approach taking into consideration the risk, complexity, length and likely proceeds of the case is appropriate to ensure even higher returns are guaranteed for class members in more straightforward cases'.
- On 1 June 2021, Treasury released a consultation paper implementing Recommendation 20. The consultation seeks views on 'the best way to guarantee a statutory minimum return of gross proceeds of a class action to class members' and in particular, on 'the potential design elements of a guaranteed minimum return, the appropriate rate and how the rate might be differentiated based on the risk, complexity, length and likely proceeds of a particular case'.
- In a statement announcing the government's intention to consult, the Treasurer and the Attorney General said that government considers guaranteeing a minimum return to class action members to be of 'particular importance', because it will ensure successful applicants are 'adequately compensated' in their cases, and prevent litigation funders and law firms from 'taking disproportionate fees in the process'.
- The deadline for submissions to the consultation is 28 June 2021.

Response to the other PJC recommendations?

- The Treasurer and the Attorney General have said that the government has already acted on Recommendation 29 of the Committee's report by introducing legislation to implement permanent changes to Australia's continuous disclosure rules.

  [Note: This appears to be a reference to Treasury Laws Amendment (2021 Measures No. 1) Bill 2021 which is currently before parliament. The Senate Economics References Committee is due to report by 30 June 2021. You can find our status update on the Bill here.]

- They have also said that government plans to finalise its response to the report following the consultation on recommendation 20 'in 2021'.

  [Source: Joint media release Treasurer Josh Frydenberg and Attorney General Michaelia Cash 28/05/2021; Treasury Consultation: Guaranteeing a minimum return of class action proceeds to class members; Consultation paper]

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