Governance News

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

26 May 2021

Contents

Diversity

Signs of progress: ISS analysis shows a spike in the number of Black director appointments on S&P 500 boards

According to analysis by ISS Corporate Solutions Inc, following the events of 2020, there has been a significant uptick in the number of newly appointed Black S&P 500 board members.

- During the period 1 July 2020 to 19 May 2021, 32% of all newly appointed directors were Black (up from 11% in the period 1 July 2019 and 19 May 2020)
- There was also a spike in the number of S&P500 companies that appointed a Black director. During the period 1 July 2019 to 19 May 2020, only 52 companies did so. During the period 1 July 2020 to 19 May 2021 this had increased to 148.
- ISS also found that companies were more willing to appoint Black directors with no previous board experience. During the period 1 July 2020 to 19 May 2021 49% of newly appointed Black board members had no previous experience on the board of a publicly traded company board (up from 36% in the previous period).
- Overall ISS found that the proportion of Black directors on S&P500 boards has increased 2.3% on last year. As at 19 May 2021, Black directors make up 10.6% of S&P500 directorships compared (up from 8.3% at 19 May 2020).

Commenting on the findings, Head of ISS Corporate Solutions Marija Kramer commented,

> 'The needle has clearly moved…As companies respond to the chorus of investors and other stakeholders who since last summer have called for greater racial and ethnic diversity within corporate boardrooms…It is particularly notable that the newest cohort of Black directors is more likely to be new to board service, compared with previous groups, and suggests the pipeline of minority director talent is growing at a faster rate than previously evidenced'.

[Source: ISS media release 25/03/2021]

In Brief | How to do better at gathering diversity data and meaningfully reporting on diversity for maximum business benefit: The Diversity Council of Australia has released a practical guide on how organisations can improve their approach

[Sources: Diversity Council of Australia media release 18/05/2021; Synopsis report: Counting Culture: Towards A Standardised Approach to Measuring and Reporting on Workforce Cultural Diversity in Australia]

In Brief | Beyond gender: The Canadian Securities Administrators (CSA) have announced their intention to conduct further research and consultation on the need for/possible introduction of broader diversity disclosure requirements (ie beyond minimum gender diversity requirements) for boards and executive officer positions. The work will take into account the extent to which corporate governance practices and the disclosure needs of investors have 'evolved' since the introduction of the 'women on boards' disclosure requirements

[Source: Canadian Securities Administrators media release 19/05/2021]

Other Shareholder News

Ensuring the voices of workers are heard in the boardroom: New report considers how FTSE 350 firms have responded to the introduction of workforce engagement requirements in the 2018 Corporate Governance Code

Key Takeouts

- The report found that overall the introduction of the new workforce engagement requirements in the 2018 Corporate Governance Code has not triggered a radical shift in approach in most cases. Rather, firms have tended to evolve their existing approaches to a greater or lesser extent.
- Reporting around workforce engagement efforts tends to be fairly minimal with little information about the practical steps that have been implemented or their impact
- Most firms have elected to appoint a non-executive director, or (less commonly) to establish an advisory panel (in some form). In some cases, firms have taken a hybrid approach appointing both a NED and an advisory panel.
- The report includes a number of case studies providing insights into emerging best practice.

The Financial Reporting Council (FRC) has released a report, compiled by Royal Holloway, University of London and the Involvement and Participation Association, into the way in which companies have responded to the introduction of worker engagement requirements in the UK Corporate Governance Code, including insights into the reasons why they have elected to adopt a particular approach, the practical changes they have implemented and emerging best practice.

Overall the report found that despite the progress being made by some firms, and despite the increased focus on the diversity and inclusion following the events of 2020, a number of firms continue to be resistant to/sceptical about the value of ensuring workers' voices are heard at board level and this is reflected in their approach.

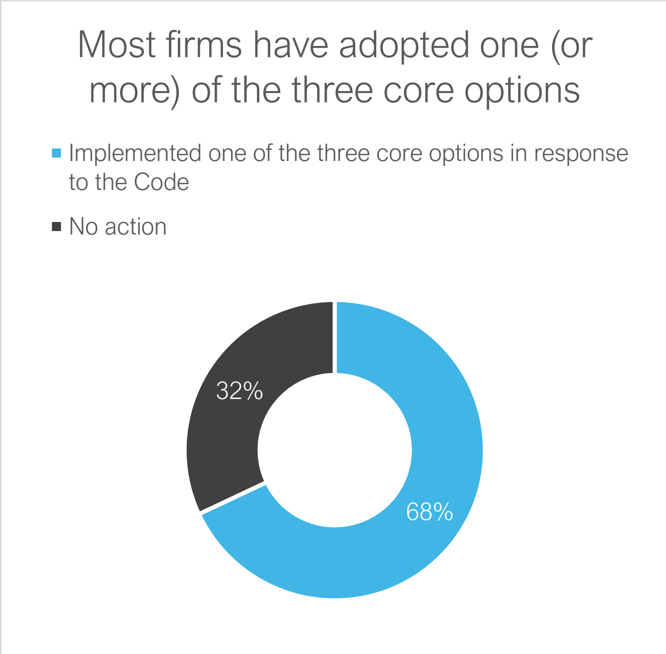
The report is based on analysis of company reports, a survey of FTSE 350 firms and interviews with directors, executive and workforce representatives.

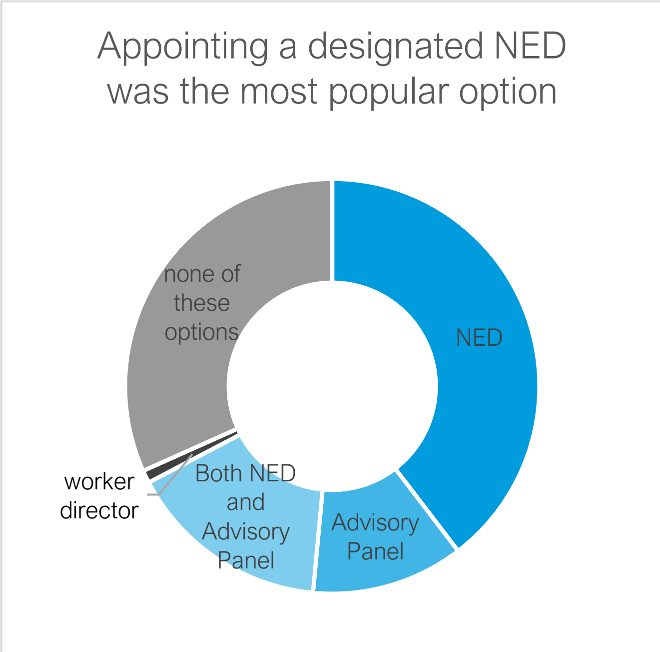
Most firms have taken some action in direct response to the 2018 Code

The Corporate Governance Code provides for three main options for workforce engagement: 1) appointing a worker director; 2) designating a non-executive director (NED); or 3) establishing an advisory panel.

The report found that:

- 68% of firms sampled adopted one (or more) of these options because of the Code.
- In the 'majority of cases' workers were not given any say on the approach to workforce engagement, rather the decision was made by the board without consultation.
- Designating a NED was by far the most popular option (40% of companies in the sample took this approach).
  - The report comments that reporting is often brief and fairly vague about the activities designated NEDs undertake. The most common reported activities are site visits and references to 'talking to employees'.
  - The report also found that it is often unclear why particular individuals were considered by the board, to be suitable for the designated NED role, based on their skills/expertise.
  - Where firms made stronger statements in annual reports about NEDs 'facilitating' two way communication between the board and employees, few details were given around what this actually entailed/evidence of how the process works in practice.
  - The report concludes that many firms (though not all) who have opted for this approach, continue in practice, to rely heavily on the findings of annual employee engagement surveys as reported to the board by HR, and on site visits, with the designated NED essentially 'complementing' or supplementing these existing processes.
  - Having said this, the report observes that that the revised Code has only been in effect since 2019, and that a number of firms have indicated that they plan to expand/evolve the role of the designated NED.





- Advisory panels:
  - 12% of companies opted to establish some form of advisory panel and 16% of companies have opted for a hybrid approach – both designating a NED and establishing some form of advisory panel (though few firms use this term).
  - Composition: The report found that in most cases, advisory panels tend to be composed of a combination of representatives selected by management and by the workforce (though this was not always the case).
  - Understanding and responding to annual surveys is a key focus for most advisory panels: The report found that as well as scope for discussion of broader issues, the agenda of advisory panels is often primarily structured around consideration of issues arising from annual staff engagement surveys with feedback from the panel shared with the board either via the designated NED or through another board member. The report comments that it was rare for worker representatives on the panel to report to the board directly on the outcome of meetings. Panels were also found to play a role in many instances in 'providing input' into action plans to address any issues identified through annual staff surveys.

- A structured mechanism for communication between the board and the workforce: The report observes that advisory panels are still a relatively new innovation and that processes are still evolving. Having said this, the report comments that having an advisory panel provides a structured/formalised mechanism for obtaining employee views and feeding these into board decision-making. Commenting briefly on the hybrid approach (having a designated NED and an advisory panel) the report suggests that this may
allow for more scope for structured/formalised two way communication between the board and the workforce (though the report comments that there were 'relatively few concrete examples' of where the views of the panel influenced board decisions/advice).

- Worker directors:
  - By far the least popular option (only one company sampled) opted to appoint worker director following the release of the Code. In total, there are now five FTSE 350 companies with worker directors (four of which pre-date the Code).
  - The report includes discussion around why firms opted not to adopt this approach. Generally, firms expressed the view that: a) one worker could not represent the views of the whole workforce; b) there would be various 'practical problems' with having an employee take on director responsibilities eg workers may lack the experience/technical background required; and c) concern that worker directors would be 'too loyal to the CEO who appointed them'/distrusted over time by the workforce. The HR director of a firm with a worker director suggested that boards may be reluctant to adopt this course because of 'perceived loss of control' and concern that workers may not have the skills required/require support.
  - The report observes that a common argument against appointing worker directors is that the 'company is too big, too multinational, or too complex to be represented by a single person or panel of people'. The report challenges this, pointing out that 'firms tend not to argue in their annual reports that they are too large or complex to be governed by a single board of directors or single Chief Executive'.
  - The report also suggests that companies may be underestimating the abilities of worker representatives (whether as directors or members of advisory panels), commenting that interviews 'revealed many examples of excellent workforce representatives'.
  - The report makes clear that the appointment of worker directors is not considered (by firms in the sample who have adopted this course) to be sufficient in itself. Rather it's perceived as supplementing or complementing other engagement mechanisms/practices.

- Almost a third of companies did not adopt any of these options:
  - The remaining 32% of FTSE 350 firms in the sample did not adopt any of these three options, either opting to adopt 'alternate arrangements' (which is allowable under the Code), or 'claiming that their existing engagement mechanisms are adequate to satisfy the Code's requirements'.

- The most common 'alternative arrangements' adopted were:
  - Systems that 'sounded very much like an advisory panel' (though the firms did not identify them as such).
  - Various 'ad hoc arrangements' eg site visits, town halls, staff focus groups or other informal conversations with employees. The report comments that a number of firms place 'heavy reliance on an annual employee survey as their primary tool for engagement with the workforce', sometimes supplemented with site visits/other informal discussions with employees.

Impact on board practices/decision making?

- The report found that the introduction of the Code requirements appears to have had little significant impact on the range of issues discussed at board meetings: 63% of firms indicating that it had made little difference.
- Overall, the report found that workforce issues arise at relatively few board meetings – with most firms indicating the workforce issues came up either 'a few times' or 'once or twice' over the last 12 months.
- 42% of firms identified only one or two occasions over the past year when workforce engagement led to a 'change in approach' and 25% indicated that this had not ever occurred.

An evolution of existing practices, rather than a radical shift in approach?

- The report found that overall the introduction of the new requirements in the Code has not triggered a radical shift in approach in most cases, but rather that firms have tended to evolve their existing approaches to a greater or lesser extent. For example, only 16% of firms said that their approach to workforce engagement had 'completed changed' in response to the 2018 Code.
- The majority of firms (80%) self-described their current approach as an 'evolution' of existing arrangements already in place before the 2018 Code.

- The report found that the extent to which firms' approach to workforce engagement changed in practice varied considerably.
  - At one end of the spectrum, some firms have built on existing 'strong foundations' in the form of staff forums or work councils to further strengthen their approach.
  - In the middle, the majority of firms were found to be 'complying with the Code as best they can, employing a range of engagement mechanisms, but often in a rather patchwork fashion, and with little evidence of substantive outcomes'.
  - At the other end of the spectrum, some firms appear to adopted what they saw as the easiest course and 'appear to have taken the path of least resistance and done little to develop even rudimentary workforce engagement mechanisms' beyond conducting an annual staff survey.

The perceived value of workforce engagement

- The report found that generally boards perceive the key benefit of engagement with the workforce 'to be less around driving board-level decision-making per se and more in allowing the board to be informed of workforce views in their interactions with executive management'.
- From the workforce perspective, the report found that communicating board decisions back to workers is a 'patchy affair'.

(Emerging) best practice?

The report comments that there is a great deal that firms could learn from one another in terms of best practice, noting that the case studies in the report highlight several approaches that may potentially have wider application.

Some of the 'key lessons' highlighted in the report are below.

- Broadly, examples of good practice identified in the report, underline that the exact engagement mechanism is of less importance than the desire for genuine engagement with employees/genuine appreciation of the value of such engagement.
- Boards should avoid a 'tick a box' approach to workforce engagement and instead focus on embedding the voices/concerns of workers into boardroom deliberations so that they are reflected in decision making.
- Whatever mechanism/approach is adopted, there should be scope for regular input from the workforce, particularly in response to rapid changes eg COVID-19.
- Boards should take care to ensure that worker voices, from across all areas and levels of the organisation are heard. The report flags that boards should be aware of the risk that minority voices could be underrepresented.
- Different 'channels' or approaches need to work well/integrate with each other. For example: designated NEDs and advisory panels need to work together as well as with staff surveys and other engagement practices. The report also suggests that 'board-level engagement practices should not cut across core trade union activities, but can beneficially include trade unions while still respecting their parallel role'.
- Commenting briefly on the appointment of workforce representatives, either as worker directors or advisory panel members, the report recommends that representatives should be chosen 'with some input from the workforce'.
- The report suggests that agendas for advisory panels, consultation meeting between NEDs and the workforce, should include a balance of both topics of worker and management interest.
- There should be an effective 'feedback loop' to ensure two way dialogue on key issues between the board the workers.

  [Sources: FRC media release 24/05/2021; Full text report: Workforce Engagement and the UK Corporate Governance Code: A Review of Company Reporting Practice]

Disclosure and Reporting

'Embroiled in a greenwashing scandal': WEF cautions that the EU's Sustainable Finance Taxonomy may actually enable greenwashing

An enabler of greenwashing?

The World Economic Forum has cautioned that the EU's Sustainable Finance Taxonomy adopted on 21 April 2021, standards intended to enhance disclosure and prevent greenwashing, have instead 'become embroiled in a greenwashing scandal' as they enable gas, a fossil fuel, to be (incorrectly) labelled as 'green'.

In WEF's view, one result of this is that the standards may 'become an enabler of greenwashing'.

Tackling greenwashing in other ways

Noting that greenwashing appears to becoming more widespread, WEF discusses the practice of naming and shaming companies that 'greenwash' as one means of tackling the issue.

Ultimately WEF considers that the effectiveness of the practice is limited because naming/shaming assumes that the greenwashers are acting deliberately, when in fact it could be simply be that they lack data, have not sufficiently embedded their ESG 'vision' into their strategy and/or that the tools necessary to deliver their vision are not yet available.

The way forward?

WEF argues that the key to identifying, and rewarding investors/companies who are setting tough targets in line with the goals of the Paris Agreement and the Sustainable Development Goals (SDGs) and making progress against them, is access to 'common definitions and reporting standards built on growing scientific understanding of climate change, poverty, biodiversity, pollution and other societal measures, and credible ways to consistently measure impact'.

Specifically, WEF argues that the following information is necessary to identify greenwashing and to ensure companies are on track to meet their stated commitments:

- inventory reporting ie information about the impact of an organisation's operations eg carbon emissions, biodiversity impacts or social equality; and
- 'impact quantification' data ie information about the impact of a particular program/investment to enable comparison against 'what would have happened in its absence'.

WEF states,

> 'The alarming evidence from recent scientific studies indicate we are not on track to meet our climate and social goals. Greenhouse gas emissions are predicted by the International Energy Agency to rise to the second highest level since records began, and we are way off track to achieve the SDGs. If not kept in check, greenwashing will further derail progress. We need to take bold action, now, that is robustly measured and transparently reported'.

[Source: World Economic Forum, 'A Spotter's Guide to Greenwashing – and what to do about it' 20/05/2021]

Consultation on product level ESG disclosure standards: The CFA institute is consulting on proposed global and voluntary ESG disclosure standards for investment products

- The CFA Institute has released an exposure draft of proposed voluntary, global Environmental, Social and Governance (ESG) Disclosure Standards for Investment Products (draft Standards) for consultation ahead of the planned release of final standards in November 2021.
- The CFA makes clear that the proposed draft Standards do not duplicate existing disclosure frameworks (though there would be some overlap with the EU's sustainable finance disclosure regime (SFDR) regulation), because they would establish disclosure requirements at the product level only, as opposed to setting disclosure requirements at the company or firm level as other existing standards (eg Principles for Responsible Investment (PRI)) do.

- A key aim is to ensure investors have access to specific information at product level, to facilitate comparison between products with ESG features as 'often, firm level information is not specific enough, particularly when an investment manager offers different types of investment products to different types of investors in different regions'.
- The draft Standards have been written with four primary user-groups in mind: a) investment managers; b) investors and asset owners; c) consultants and advisors; and d) providers of investment product databases. The CFA Institute also suggests that the Standards may be helpful to regulators and investment professionals
- The draft Standards are intended to address key elements of investment product strategy including: objectives; benchmarks, sources and types of ESG information; ESG exclusions; ESG information in financial analysis and valuation; portfolio-level ESG criteria and characteristics; process to achieve impact objective; and stewardship.
- The draft Standards have been written with the aid of a technical committee composed of 18 international ESG experts and incorporate public comments received on the Consultation Paper that was released in August 2020.
- The due date for submissions to the consultation is 14 July 2021.

  [Sources: CFA institute media release 19/05/2021; Consultation on ESG Disclosure standards; Exposure draft: CFA institute ESG disclosure standards for investment products May 2021]

Paving the way for mandating climate disclosure? US Presidential Order confirms the Administration's climate policy and flags improved disclosure, management and mitigation of climate-related risk as a key priority

In an executive order, US President Joe Biden has confirmed that it is the policy of the Administration to:

> 'advance consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk…including both physical and transition risks; act to mitigate that risk and its drivers, while accounting for and addressing disparate impacts on disadvantaged communities and communities of colour…and spurring the creation of well-paying jobs; and achieve our target of a net-zero emissions economy by no later than 2050.'

Consistent with this policy stance, the order directs that various actions be taken. Key actions include (among others):

- Directing the Director of the National Economic Council Brian Deese, and National Climate Advisor Gina McCarthy, to develop a 'comprehensive government-wide strategy' to address climate-related financial risks to federal government programs, assets and liabilities within 120 days. This draft strategy is also expected to cover financing needs for transitioning the US economy to net-zero emissions by 2050.
- Directing the Financial Stability Oversight Council (FSOC), to 'assess the climate-related financial risk, including both physical and transition risks, to the financial stability of the Federal Government and the stability of the US financial system' and to issue a report within six months on the efforts being made by FSOC member agencies - the Federal Reserve, the Securities and Exchange Commission and the Commodity Futures Trading Commission - to 'integrate consideration of climate-related financial risk in their policies and programs' and the actions being taken to improve climate-related disclosures.

  In a separate statement, Treasury Secretary Janet Yellen outlined the steps that will be taken to implement this aspect of the order, emphasising that a coordinated approach to mitigating climate risk will 'ensure the most effective approach to improving the resilience of the financial system'.
- Directing the Labor Secretary to, again with a reporting deadline of 6 months (180 days),
  - identify any actions that could be taken under existing laws, to 'protect the life savings and pensions of United States workers and families from the threats of climate-related financial risk'
  - consider consulting on proposals to 'suspend, revise or rescind' Trump-era rules (the Financial Factors in Selecting Plan Investments 85 Fed Reg 72846 (November 13, 2020) and Fiduciary Duties Regarding Proxy Voting and Shareholder Rights 85 Fed Reg 81658 (December 16, 2020))
  - assess 'how the Federal Retirement Thrift Investment Board has taken environmental, social, and governance factors, including climate-related financial risk, into account'
- Directing the Treasury Secretary to direct the 'Federal Insurance Office to assess climate related issues/gaps in the supervision and regulation of insurers, including as part of the FSOC's analysis of financial stability, and to further assess…the potential for major disruptions of private insurance coverage in regions of the country particularly vulnerable to climate change impacts'.

The measures in the order are expected to 'help the American people better understand how climate change can impact their financial security. It will strengthen the US financial system. And it will inform concrete decisions that the federal government can take to mitigate the risks of climate change'.

In a statement, Ceres welcomed the measures, which Ceres CEO and President Mindy Lubber described as a 'bold, thoughtful and important step toward ensuring that every business across every sector of our economy is adequately preparing for the climate crisis'.

[Sources: Executive Order on Climate-Related Financial Risk 20/05/2021; Fact Sheet: President Biden Directs Agencies to Analyse and Mitigate the Risk Climate Change Poses to Homeowners and Consumers, Businesses and Workers, and the Financial System and Federal Government Itself 20/05/2021; Treasury Secretary Janet Yellen media release 20/05/2021; Ceres media release 20/05/2021]

Meetings and Proxy Advisers

Early insights into 2021 proxy voting trends: Heading for a 'record year' for shareholder ESG proposals?

Alliance Advisors have published an early look at the issues/trends observed so far this proxy season.

Some Key Takeaways

- Director elections/re-elections:
  - Alliance Advisors found that the level of average level of support for directors has so far remained stable (as compared to the same time last year) at 95.6%, though this is expected to drop as the season progresses based on 2020 full-season results.
  - There are a range of reasons given for voting against directors including, among others: lack of board diversity, board accountability (eg for governance failures), lack of progress on climate disclosure and compensation related issues
- Say on pay: Alliance Advisors states that based on early vote results, shareholders/proxy advisers appear to be evaluating companies in 'strict accordance' with their COVID-19 guidance and appear willing to exercise their voting rights accordingly. There has been an uptick in the level of opposition to say on pay votes at Russell 3000 companies: 89.0% Russell 3000 and 87.1% S&P 500. The failure rate has also doubled to 2%.

Shareholder ESG proposals:

- 2021 is expected to be a record year in terms of the level of investor support for shareholder ESG resolutions:
  - The level of support for climate change, political activity and diversity related shareholder proposals has increased as compared with last year, including the level of support from large institutional investors. For example, BlackRock is significantly more willing to back reasonable shareholder ESG proposals.
  - According to Alliance Advisors, from 1 January to date, BlackRock has backed 91% of environmental proposals (up from 6% in the one year to June 2020), 23% of social proposals (up from 7% in the year to June 2020) and 26% of corporate-governance proposals (up from 17% in the full year to June 2020).

  [Note: Separately, analysis by Morningstar (here) has identified that ESG shareholder resolutions voted on so far this proxy season, have attracted a record level of support. You can find a short summary in this issue of Governance News at p15. Ceres has also previously flagged this trend. You can find a summary in Governance News 19/05/2021 at p13.]

- Climate change proposals: The majority of shareholder ESG proposals are climate related, and most of these concern greenhouse gas emissions reduction consistent with previous years.
- Say on climate? Commenting briefly on the emergence of 'Say on Climate' shareholder proposals, Alliance Advisors' expectation is that 'hundreds' of proposals are likely to be filed by the end of 2021. As yet, the reaction from investors appears mixed with some strongly in favour as a means of 'holding companies' feet to the fire' and others questioning the likely impact/effectiveness of the advisory vote as a means of driving progress on the issue.
- Rise in the number of diversity-disclosure resolutions: There have been 22 more shareholder resolutions seeking more detailed diversity information (EEO-1 information) than 2020, with many filed at companies that publicly voiced their support for the BLM movement in 2020. Alliance Advisors suggests that in addition to the events of 2020, regulatory change such as Californian legislation setting minimum board diversity requirements and Nasdaq's proposed rule, may be contributing to the increase.
- Governance proposals: Alliance Investors suggests that investors may be more willing to support shareholder proposals seeking the appointment of an independent board Chair than they were in 2020 (when combined CEO/Chair roles were accorded some 'slack' due to the pandemic). Alliance Advisors suggests that 'as a lack of board independence continues to be cited as a crucial reason for investor dissent, companies might be wise to review their board structure. Given the relative high level of support, a policy change from one of the major investors could be the difference between a pass or fail'.

  [Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 20/05/2021]

In Brief | 'Manifestly unfair and nonsensical': Ownership Matters' submission to Treasury's consultation on potential options for the reform of the proxy system is highly critical of the 'options' put forward, and raises questions about the need for change

[Note: You can find our short overview of the proposed reform options being considered here. Both Institutional Shareholder Services (ISS) and Glass Lewis have separately issued statements raising concerns about the proposed reform options and questioning the need for reform. You can find a short summary in Governance News 12/05/2021 at p7]

[Source: Ownership Matters submission to treasury on proxy advice reforms 20/05/2021]

Shareholder Activism

Activist Engine No 1 reiterates its case for strategic change at Exxon ahead of the AGM, BlackRock has reportedly voted for three of the four alternate board candidates

Final call from Engine No 1 for board change

Ahead of the 26 May 2021 AGM, activist Engine No 1 has issued a message to ExxonMobil Shareholders reiterating and clarifying its demands in response to what it considers to be Exxon's mischaracterisation of its stance.

Among other things, the message emphasises the necessity of board change and calls on investors to support all four board nominees.

> 'We believe given the years of underperformance at ExxonMobil and the magnitude of the challenge, having 1/3 of the Board possess relevant industry is consistent with that goal and would put ExxonMobil on par with companies that have outperformed it including ConocoPhillips, Equinor, and Shell. We also note that electing fewer than 4 of our nominees would result in retaining one or more of the following: a director that ISS called the “wrong choice” for the Board and 3 others who oversaw management and strategy during a period in which by ISS’ account poor strategy and a lack of sufficient Board oversight seriously marred the Company’s performance'.

The message also reiterates that the campaign has the endorsement of 'ISS and every other proxy advisory firm'.

The message concludes by stating that the need to address the long-term business risks of climate change has only accelerated since the campaign was launched, most recently with the publication of the IEA's report (summary of key points in Governance News 19/05/2021 at p32) outlining the need for immediate and 'dramatic changes' in the energy sector. Engine No 1 states that with board change, and a change in direction, 'it is not too late' to 'unlock' Exxon's potential to succeed in the longer term.

In recent articles for Forbes, Professor Robert Eccles discusses the campaign in detail and outlines why he believes it should succeed. You can find the full text here and here.

BlackRock has voted in support of three (of the four) alternate board candidates?

According to Reuters, BlackRock has voted for three of the four Engine No 1 board candidates.

Commenting on this, Executive Director of Majority Action Eli Kasargod-Staub said,

> 'After years of escalating demands from activists, clients, shareholders, and elected officials to use its outsized voting power to hold recalcitrant companies accountable, it appears that BlackRock has voted for three of the four directors proposed in the alternate slate. The Exxon proxy battle is only the beginning of a reckoning for board directors across industries who fail to meet the urgent imperative of economy-wide decarbonisation and to protect value for diversified long-term shareholders. As a top shareholder in most of the largest companies in the country, BlackRock must use its outsized voting power to vote against failing directors across climate-critical industries, as it committed to do - and its full voting record will reveal whether it has comprehensively upheld this commitment.'
>
> [Sources: Reenergise Exxon campaign, Engine No 1 media release; Majority Action media release 25/05/2021]

Institutional Investors and Stewardship

Top Story | Institutional investors have changed their tune on supporting ESG shareholder proposals?

Research suggests that a marked shift in the voting behaviour of institutional investors is pushing the level of support for shareholder ESG resolutions to record levels.

Separate analysis by Morningstar and Alliance Advisors has found that the level of support for ESG shareholder proposals looks set to reach record levels in 2021. The research suggests that the uptick in the level of support is being driven in large part by a change in the voting behaviour of institutional investors.

What does the research say?

Alliance Advisors has published an early look at the issues/trends observed so far this proxy season. Among other things, the research found that the number of shareholder ESG resolutions has significantly increased this year and that the level of support for climate change, political activity and diversity related shareholder proposals has spiked, due in part to the uptick in support from large institutional investors.

For example, according to Alliance Advisors, since 1 January 2021, BlackRock has backed 91% of environmental proposals (up from 6% in the one year to June 2020), 23% of social proposals (up from 7% in the year to June 2020) and 26% of corporate-governance proposals (up from 17% in the full year to June 2020).

Separate analysis by Morningstar has found that the ESG shareholder resolutions voted on so far this proxy season, have attracted a record level of support. Morningstar, like Alliance Advisors, again attributes this to a shift in the voting behaviour of large institutional investors, including BlackRock, Vanguard and State Street (which together manage nearly 40% of the money in mutual funds).

Morningstar points out that both BlackRock and Vanguard have published updated proxy voting guidelines that leave the way more open for them to support reasonable ESG shareholder proposals. Morningstar suggests that there is evidence that this new approach is translating into a material increase in the level of support for ESG shareholder resolutions as compared with 2020.

For example:

- As at 7 May 2021, 21 ESG shareholder resolutions were supported by a majority of shareholders (up from 15 in 2020).
- From the beginning of January 2021, average shareholder support for ESG resolutions has increased to 44% (up 12% as compared with the same period in 2020).

Looking at repeat resolutions – resolutions that were on the ballot in one of the previous two years – Morningstar found that the increase in the level of support is even clearer.

For example, in 2019, a resolution calling for regular disclosure of DuPont's plastic pellet spills received 7% support. In 2021, despite management's 'against' recommendation, the same resolution received 81% support. A diversity disclosure resolution at the same company received 84% support. Given BlackRock, Vanguard and State Street hold a combined 27% of Dupont shares, Morningstar considers it extremely likely that all three supported both proposals.

In light of these early trends, and given the fact that the three largest asset managers have singled out climate and diversity as priority themes, Morningstar considers it likely that the upswing in support for shareholder ESG resolutions is likely to continue to gain momentum.

[Note: Ceres has also previously flagged this trend. You can find a summary in Governance News 19/05/2021 at p13.]

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 20/05/2021; Morningstar media release 12/05/2021]

New framework released to help guide investor action on climate risk and accelerate the net zero transition

Key Takeouts

- As part of a broader push to push companies to transition to a net-zero economy by 2050 (or sooner), the founding partner of the Investor Agenda have released a new tool to help companies self-assess their current approach to climate risk and guide them in progressing and improving their approach.
- The Investor Agenda plans to monitor how many investors are developing and implementing climate action plans aligned with this new tool in the hope that all major investors have an investor climate action plan (ICAP) with net-zero targets in the next five years.

The founding partners of The Investor Agenda (AIGCC, CDP, Ceres, IIGCC, IGCC, PRI, and UNEP FI) have released a new tool – the Investor Climate Action Plans (ICAPs) Expectations Ladder and accompanying Guidance – to assist institutional investors to evaluate their current approach to climate risk and to improve and accelerate their progress by providing them with 'clear expectations for issuing and implementing comprehensive climate action plans'.

A framework designed for investors at every stage of their 'climate journey'

The Expectations Ladder is intended to be used by all investors, regardless of the extent to which they have/have not started to think about identifying/managing/mitigating climate risk and opportunity. As such, it adopts a tiered approach, outlining actions for investors who are least advanced on their 'climate journey' (Tier 4) and progressing (up the ladder or tiers) to those who are the most advanced (Tier 1).

It's anticipated that investors will use the Ladder to self-assess their approach, and once they identify where they fit on the Ladder, use the expectations set out under each Tier to help guide improvements in their approach. It's anticipated that investors will meet 'most of the actions' in a particular tier before progressing to the next one.

Investor Agenda expects that aligning their strategy with the expectations in the Ladder may result in investors:

- 'Assessing their current approach to managing climate change risk and opportunity
- Publishing a standalone ICAP
- Embedding elements of the ICAPs into their climate change strategies and disclosures
- Communicating their current activities and future plans to stakeholders'.

The accompanying ICAPs Guidance provides guidance on interpreting the Ladder, and assisting in the task of self-assessment.

Overlap with the TCFD recommendations?

According to Investment Agenda, though there is 'significant commonality' between meeting the TCFD requirements and the ICAPs Expectations Ladder's Investor Disclosure focus area, meeting the TCFD requirements will not necessarily mean that investors have also met expectations under the Ladder.

For example, Investment Agenda points out that the TCFD 'does not explicitly require investors to report on their policy advocacy or on how they integrate just transition principles into their decision-making'.

The aim is for all major investors to have an ICAP with net zero targets in the next five years

The Investor Agenda plans to monitor how many investors are developing and implementing climate action plans aligned with the Ladder, with the hope that:

- at least 50% of all major investors will issue an ICAP or incorporate elements of the Expectations Ladder into their plans, reports and strategies in the next year; and
- that all major investors have an ICAP with net-zero targets in the next five years.

Part of a broader push to transition to a net-zero economy by 2050 (or sooner)

Investor Agenda observes that there is growing momentum among investors and policymakers to reach net zero emissions by 2050 or sooner, and to set interim reduction targets for 2025 and 2030. The release of the ICAP Expectations Ladder and Guidance follows various initiatives, endorsed by Investor Agenda aimed at pushing investors to make net-zero commitments and to align their investment portfolios with that aim (eg the Net Zero Asset Managers initiative, Paris Aligned Investment Initiative, Science Based Targets initiative and United Nations-Convened Net Zero Asset Owner Alliance).

[Sources: Investor Group on Climate Change media release 20/05/2021; Investor Climate Action Plans website; FAQs]

Norges Bank has excluded three companies on ethical grounds

The Executive Board of Norges Bank Investment Management has announced its decision to exclude Honeys Holdings Co Ltd, Shapir Engineering and Industry Ltd and Mivne real Estate KD Ltd from the government pension fund global on ethical grounds, in line with the recommendations of its Council on Ethics.

- Honeys Holdings Co Ltd has been excluded 'due to unacceptable risk that the company contributes to systematic violations of human rights' based on consideration of 'workers' rights' at two factories that the company owns in Myanmar.
- Shapir Engineering and Industry Ltd and Mivne Real Estate KD Ltd have been excluded 'due to unacceptable risk that the companies contribute to systematic violations of individuals' rights in situations or war or conflict', based on the companies' activities associated with Israeli settlements on the West Bank.

Announcing the decision, the Executive Board made clear that it has not conducted an independent assessment of all aspects of the Council of Ethics recommendations to exclude the companies, but that it is nevertheless 'satisfied that the exclusion criteria have been fulfilled'.

The Executive Board stated that before deciding to exclude a company, it considers whether the exercise of 'ownership rights' may be appropriate. The Executive Board determined that this was not appropriate in these three cases.

[Source: Norges Bank Investment Management media release 19/05/2021]

Financial Services

Top Story | Should financial planners be individually registered? The Financial Planning Association suggests that the government take the opportunity to strengthen its proposed approach to implementing Hayne Recommendation 2.10.

Context

- Hayne Recommendation 2.10 recommended the establishment of a single disciplinary body for financial advisers and that all financial advisers who provide personal financial advice to retail clients should be registered.
- Consultation on a draft Bill proposing to implement the government's response to this recommendation recently concluded (14 May 2021). You can find a summary of the proposed measures in Governance News 21 April 2021 at p15.

FPA's submission to the consultation: An opportunity to strengthen the proposed approach?

The Financial Planning Association's (FPA's) submission to the Treasury's consultation is broadly supportive of many aspects of the proposed approach including measures intended to streamline existing processes and address duplication such as the proposal to wind up FASEA and 'remove the redundant oversight of the Tax Practitioners Board'.

The submission is also broadly supportive of the proposal to establish a disciplinary function based on the Financial Services and Credit Panels (FSCPs) within the Australian Securities and Investments Commission (ASIC).

Individual registration

The FPA's submission does however include several recommendations to 'improve' the proposed approach including calling for the introduction of an individual registration model for financial planners (as opposed to the proposed model, under which registration of financial planners would be the responsibility of the Australian Financial Services Licensee (AFSL holder)).

Specifically, the FPA recommends that:

- the proposed registration requirement for financial planners be redrafted as a personal responsibility for financial planners
- applications for registration/renewal should be submitted by individual financial planners (not the AFSL holder)
- professional registration should not be tied to employment or authorisation under an AFSL

The FPA argues that individual registration is a better approach because it would underline individual advisers' commitment to high professional standards, thereby lifting standards across the sector. The FPA also considers that the introduction of individual registration is 'central' to Hayne recommendation 2.10.

The FPA states,

> 'The creation of a personal registration is an essential component of any professional framework and is commonplace in professions as diverse as health practitioners, lawyers, architects and tax agents. A personal registration becomes a valued symbol that a practitioner has completed their professional qualifications, is in good standing in the community and whose behaviour is guided by adherence to the profession's ethical principles. The benefits of registration are largely lost if it is tied to a financial planner's employment, duplicates the authorisation process and is treated as another administrative task to be completed by their licensee'.

Further to this, FPA CEO Dante De Gori commented individual registration has benefits for consumers.

> 'A true professional registration will have flow-on benefits for consumers as it will improve the quality of the information on the Financial Adviser Register and ensure anyone can easily check the qualifications, registration status and disciplinary record of their financial planner. Establishing a professional registration for financial planners is a perfect opportunity to build the Financial Adviser Register into the valuable resource that it could be'.
>
> [Sources: FPA media release 19/05/2021; Financial Planning Association submission: Single Disciplinary Body for Financial Advisers 14/05/2021]

Responsible lending: Consumer group again urges the government to rethink the roll back of responsible lending protections

Context

The National Consumer Credit Protection Amendment (Supporting Economic Recovery) Bill (summarised here, update on status here) is currently before the senate.

Among other things, the Bill includes measures to roll back what the government considers to be overly prescriptive responsible lending obligations, with the object of improving the flow of credit and supporting the nation's economic recovery.

CHOICE has reiterated calls for the government to reconsider scaling back responsible lending protections

Consumer group CHOICE has again urged the government to rethink the planned changes to responsible lending obligations. Citing data showing that 'significant parts' of Western Sydney and Melbourne's west are already in mortgage stress, CHOICE CEO Alan Kirkland said that the repeal of responsible lending protections would place more people at risk of taking on loans they cannot repay. Mr Kirland said,

> 'Safe lending laws were put in place to avoid the huge damage to families and communities caused by mortgage stress - by making banks take care to avoid giving people loans they won't be able to afford to repay. If the Government gets away with its plan to axe safe lending laws people who are desperate to get into a rising housing market will be at risk of overexposure and people who need to refinance won't be adequately protected'

Mr Kirland went on to welcome indications from senators, including Senator Hanson, that they intend to block the measures and called on the government to rethink its plan.

[Source: CHOICE media release 20/05/2021]

ASIC is consulting on proposed changes to the ePayments Code

Overview: ASIC Consultation Paper 341: Review of the ePayments Code: Further consultation

Key Takeouts

- The Australian Securities and Investments Commission (ASIC) is consulting on proposed updates to the ePayments Code as an interim step, to ensure it remains current/effective, ahead of the Code being made mandatory by legislation (though there is no timing around when this may occur).
- Among other proposed changes, ASIC proposes to:
  - 'modernise' the Code to take into changes since it was last substantively reviewed in 2010 including defining biometric authentication in the Code and incorporating it into specific provisions as/where relevant;
  - extend the protections in the Code to apply to small businesses (except where Code subscribers opt-out);
  - remove the requirement for Code subscribers to report annually on the incidence of unauthorised transactions;
  - clarify the application of the unauthorised transaction provisions (including making clear that they do not apply where the consumer has made the transaction themselves either by mistake or by falling victim to a scam)
  - make various changes to the mistaken internet payments (MIP) framework including making clear that the definition of 'mistaken internet payment' is limited to situations in which the consumer has made a genuine mistake in typing the account identifier and does not extend to scam scenarios.
- It's proposed that existing subscribers to the current Code will not automatically become subscribers to the updated version (one finalised). Rather they will need to reapply to ASIC.
- The deadline for submissions to the consultation is 2 July 2021.

As part of the review of the continued effectiveness the voluntary ePayments Code (Code) the Australian Securities and Investments Commission (ASIC) has released a second consultation paper (CP 341) seeking further feedback on its proposed Code updates. ASIC states that the review is an interim measure ahead of the Code eventually becoming mandatory through legislation.

Proposed changes

ASIC's proposed updates primarily relate to the eight broad issues or areas. An overview of some of the key proposed changes is below.

ISSUE	PROPOSED CHANGE	RATIONALE
Changes to compliance monitoring and data collection	▪ ASIC proposes to remove the existing requirement for subscribers to report annually on the incidence of unauthorised transactions. ▪ Instead, ASIC proposes that the existing power in the Code enabling ASIC to conduct targeted ad hoc monitoring of compliance with the Code should be amended to enable it to also conduct monitoring/surveillance of matters 'relevant to subscribers' activities relating to electronic payments'.	▪ ASIC states that removing the reporting requirement would significantly reduce the regulatory burden. ▪ ASIC also considers that the proposed approach will give it the flexibility to focus on particular areas of Code compliance based on priorities/issues of concern rather than having an ongoing focus on the one topic of unauthorised transactions. ▪ ASIC states that the proposed approach will also allow it to tailor information/data requests, in consultation with subscribers.

Proposed changes to the mistaken internet payments framework	▪ ASIC proposes to extend the mistaken internet payments (MIP) framework in the Code to enable consumers to retrieve partial funds if the full amount of the payment is not available in the unintended recipient's account.
	▪ The Code would also be amended to include a non-exhaustive list of examples of what a receiving ADI can do to meet the requirement to make 'reasonable endeavours' to retrieve the consumer's mistaken internet payment.
	▪ Other proposed changes include (among others):
	  ▪ limiting the definition of 'mistaken internet payment' to situations in which the consumer has made a genuine mistake in typing the account identifier (and not extending it to scam scenarios)
	  ▪ 'enhancing' the content of the existing on-screen warning about mistaken internet payments to make it clearer to consumers that typing a correct account name 'will not remedy an incorrect BSB and/or account number'.
		▪ The partial return of funds: Currently the Code does not provide for the return of partial funds where a mistaken internet payment has occurred and there are insufficient funds available in the unintended recipient's account. ASIC considers that there is a 'strong benefit in allowing consumers to retrieve some of the funds, even if they cannot retrieve the total amount'.
		▪ Reasonable endeavours: ASIC observes that except for the example in clause 32.1 (facilitating repayment by instalments), the Code does not currently provide any guidance on what amounts to 'reasonable endeavours' by the receiving ADI for retrieval of funds in the unintended recipient's account where the funds are insufficient. ASIC agrees with feedback provided by some stakeholders that a non-exhaustive list of scenarios would be useful in 'serving as a benchmark for receiving ADIs about what types of options they might need to consider in individual cases'.

Extending the Code protections to small business customers	▪ ASIC proposes to extend the Code protections to small businesses (unless subscribers elect to opt-out of doing so, by notifying ASIC). ▪ ASIC proposes to define a 'small business' as a business employing fewer than 100	▪ The proposed change is intended to extend protections to small businesses who may have the same/similar vulnerabilities and need for protection as consumers in the context of electronic payments.

ISSUE	PROPOSED CHANGE	RATIONALE
	people or, if the business is part of a group of related bodies corporate (as defined in the Corporations Act 2001 (Cth)), 'fewer than 100 employees across the group'. ▪ The proposed extension to small business would not operate retrospectively ie the change will not apply to small businesses that acquire their facilities before the new Code commences.	▪ The proposed 'opt-out' option is intended as a 'reasonable compromise', in acknowledgement of the 'sometimes starkly opposing views' on the issue. ▪ Not retrospective operation: ASIC states that the proposed approach will mean that subscribers will not need to identify all existing customers who meet the definition of small business. The change will also make it easy for small businesses to ascertain whether they are covered by the Code (as they will be able to refer to their facility terms/conditions).
Unauthorised transactions and pass code security requirements	▪ ASIC proposes to make a number of changes to clarify the application of the unauthorised transaction provisions, including: – clarifying that provisions only apply where a third party has made a transaction on a consumer's account without the consumer's consent and that they do not apply where the consumer has made the transaction themselves either by mistake or by falling victim to a scam. – clarifying that a breach of the pass code security requirements of itself, is insufficient basis to hold a consumer liable for an unauthorised transaction. Instead, in addition, the subscriber must prove (on the balance of probability) that the consumer's breach of the pass code security requirements contributed to the loss.	▪ ASIC considers that it is not clear in the current Code whether consumer transactions made as a result of scams are captured. In ASIC's view, the unauthorised transaction provision in the Code do not apply 'where a consumer made the transaction instructions, whether as a result of third-party inducement, a scam or otherwise'. The proposed changes are intended to make this clear. ▪ ASIC considers that breach of pass code security requirements alone is insufficient to hold a consumer liable for an unauthorised transaction. The proposed changes is intended to make this clear.
Modernising the Code to reflect changes in the field of electronic payments since the last review of the Code in December 2010	▪ ASIC proposes to define biometric authentication in the Code and incorporate biometric authentication into certain clauses within the Code (where relevant). ▪ ASIC makes clear that it does not propose to incorporate biometrics into the definition of 'pass code' 'in a way that would mean that pass codes and biometrics could be used throughout the Code interchangeably'.	▪ The existing Code does not currently refer to the use of biometrics to authenticate a payment. ▪ However, in ASIC's view, it is not workable for biometric authentication to be treated in the same was as 'pass codes' are treated within the Code because of the inherent differences between the two. For example, it's not feasible for consumers to be instructed 'keep their fingerprints safe' (as it is for pass codes). On this basis, ASIC's preferred approach is to add references to biometric authentication into the Code on a provision-by-provision basis, as relevant/appropriate. ▪ ASIC considers that this approach provides 'certainty for stakeholders about their rights and obligations under the Code in specific circumstances where biometric

ISSUE	PROPOSED CHANGE	RATIONALE
		authentication is used in place of a pass code'.
	▪ ASIC proposes extend the protections in the Code to include situations in which a 'Pay Anyone' payment is made through the NPP.	▪ ASIC considers that the Code's protections should be available to consumers regardless of the platform they use to make payments.
	▪ ASIC proposes to replace the term 'device' in the Code with the term 'payment instrument' and to include virtual debit and credit cards in the definition of 'payment instrument'.	▪ Currently the Code uses the term 'device' to describe any 'device given by a subscriber to a user that is used to perform a transaction' eg a debit/credit or ATM card. ASIC considers that this terminology could be confusing for subscribers and suggests that the change in terminology may assist in addressing this issue.
	▪ ASIC proposes to amend the Code to cover the provision of electronic transaction receipts as well as paper receipts.	▪ Restrictions in the current Code on the contents of receipts only apply to paper receipts. ASIC's view is that protections under the Code should apply regardless of whether the receipt is provided in paper or electronic form.
Complaints handling	▪ ASIC proposes to require all Code subscribers to have internal dispute resolution (IDR) procedures as set out in Regulatory Guide 271 Internal dispute resolution (RG 271) and to be members of AFCA (rather than having different requirements depending on licencing status). ▪ Having said this, ASIC acknowledges that some requirements may need to be tailored based on the subscriber's licensed status eg requirements concerning unauthorised transaction report investigations.	▪ The current Code contains requirements for complaints handling in two sections: – Chapter F which sets out obligations for obligations for subscribers who are Australian financial services (AFS) licensees, unlicensed product issuers, unlicensed secondary sellers, Australian credit licensees or credit representatives; and – Appendix A which sets out different and lighter obligations for subscribers not covered by Chapter F. ▪ ASIC proposes to merge Chapter F and Appendix A requirements into a single framework applying to all Code subscribers. ▪ ASIC states that it has not 'identified any reason to retain two separate frameworks or to otherwise exempt Appendix A subscribers from having IDR procedures in place that meet ASIC's requirements in RG 165 (or RG 271, after it commences) or from having membership with AFCA'. On this basis, it proposes that the Code should be simplified in the interests of making the Code easier to understand for consumers and helping ensure consumers have access to protections.
Facility expiry dates	▪ ASIC proposes to align the facility expiry period in the Code with the expiry period in the Australian Consumer Law, which is 36 months.	▪ The proposed change is intended to provide consistent rules/protections for consumers across a variety of payment instruments.

ISSUE	PROPOSED CHANGE	RATIONALE
Transition and commencement of the updated Code	▪ ASIC seeks views on the appropriate transition period for transitioning to the updated Code.	▪ Though ASIC believes that the updated Code should commence 'as soon as possible' it acknowledges that many of the proposed changes will require time to implement.

ASIC states that it is beyond the scope of the review to mandate the Code or to change the scope of entities to whom the Code is relevant.

Next steps

- The deadline for submissions to the consultation is 2 July 2021.
- Following consultation, ASIC will consider stakeholder feedback and issue a report in August/September 2021 outlining its final position. ASIC will also publish a draft updated Code reflecting ASIC's final position for stakeholder feedback 'purely on the format and technical wording (not the policy positions in the Code)'.
- An updated Code is expected to be released in 'late 2021'. Once the new Code comes into effect (after an 'appropriate' transition period), entities who wish to subscribe to it (including subscribers to the current Code), will need to request that ASIC list them as a subscriber.
- In future, ASIC plans to conduct a review of the Code every five years (subject to any changes to the review period introduced in the process of mandating the Code, or the need for ad-hoc targeted reviews).

[Sources: ASIC media release 21/05/2021; CP 341 Review of the ePayments Code: Further consultation]

Treasury is consulting on the design of the cyclone reinsurance pool

Context

- On 4 May 2021, the government announced plans to improve the affordability and accessibility of residential, strata and small business property insurance for people in Northern Australia through establishing a reinsurance pool for cyclones and related flood damage.
- The government intends that the pool will be administered by the Australian Reinsurance Pool Corporation (ARPC).
- The government has said that the pool will be backed by a $10 billion government guarantee and commence from 1 July 2022.

Consultation on key design features of the proposed reinsurance pool launched

Treasury has released a consultation paper seeking views on key design features of the reinsurance pool.

A Treasury-led Cyclone Reinsurance Pool Taskforce (the Taskforce) will also consult broadly with industry, community representatives and other interested parties on the topics outlined in the consultation paper.

Broadly, Treasury is seeking feedback on the following key issues.

How the scope of reinsurance pool coverage should be identified, including consideration of:

- How ‘cyclone’ and ‘cyclone-related flooding’ should be defined (as this may determine eligibility for coverage and claims)
- Whether 'storm surge' should be included in 'cyclone related flooding'
- Which insurance policies should be eligible to be covered: a) whether there are any difficulties in including home building, home contents, or residential strata policies in the reinsurance pool; b) how the challenges associated with capturing small business policies can best be managed (and which definition of small business should be used in this context)

How the reinsurance product should be priced and designed, including consideration of:

- How cyclone, storm surge and flood related risks is currently assessed and how premiums are calculated

- Potentially using a tiered risk rating system to more effectively target premium reductions at the individual property level based on the particular property's risk profile, with higher risk properties receiving higher discounts. The consultation paper seeks feedback in particular, on how such a risk rating system should be designed and the trade-offs associated with using risk tiering and with the suggested 'level of granularity'
- How much risk exposure primary insurers should retain
- The potential impact on the claims management process and how any potential impact could be addressed through the design of the pool

How insurer participation and transition to the pool should be managed, including consideration of:

- Whether participation in the reinsurance pool scheme should be voluntary or mandatory
- Assuming that participation is mandatory:
  - how much risk insurers would need to cede to the pool
  - the threshold of cyclone risk for insurers to cede policies to the pool (and whether this could be implemented through 'hazard maps' or self-assessment by insurers)
- The best approach and timing for the transition

The most appropriate governance and review arrangements, including consideration of:

- Whether the ARPC's existing triennial review mechanism (which assesses whether there is a need for the terrorism reinsurance scheme to continue) should be expanded to cover cyclone and related flood damage, and if so what changes are required to existing review arrangements. For example, it's suggested that the frequency and scope of reviews should be considered, also whether an interim review, shortly after the establishment of the cyclone and related flood damage reinsurance pool to evaluate its early operation is needed.
- Other questions for consideration include:
  - how best to ensure that premium reductions are passed on to customers
  - how the reinsurance pool could help encourage households/businesses to 'undertake mitigation' and avoid 'encouraging increased risk taking'

The deadline for submissions is 18 June 2021.

[Source: Treasury media release 20/05/2021]

A rescue plan for private health insurance? Grattan report sets out a four point plan to 'stop the death spiral'

The Grattan Institute has released a report (full text here and shorter article discussing the key recommendations in the Conversation here) outlining a four point plan designed to address the sustainability challenges facing the private insurance sector in Australia.

The challenges for the sector

The Grattan Institute sums up the challenges facing the sector as follows:

> 'As the population ages and uses more expensive healthcare services, insurers have to pay out more in benefits to their members. As benefits paid increase, so do premiums. Rising premiums make health insurance less affordable and less attractive – particularly to younger and healthier people. As younger, healthier people drop their insurance, the insurance risk pool gets worse, premiums go up, more young people drop out, and the cycle continues'.

In addition, the report argues that industry is also facing pressures in the form of: rising costs for surgery, 'excess charging' for medical prostheses and 'over-servicing' by private hospitals, all of which are considered to be contributing to the increases in consumers' out of pocket costs.

The report also flags that premium increases are also being approved, without sufficient consideration of the value being provided, contributing to the dissatisfaction with private health insurance.

A suggested four point plan to ensure the future viability of the sector

Broadly, the report recommends:

- **Making it harder to increase premiums (without sufficient justification)**
  - The report recommends that before approving increases to premiums, the Minister for Health should consider in each case, the proportion of premiums returned to members in benefits (claims ratio) and require funds to provide additional justification for an increase if the claims ratio is less than 80 or 85%. Where the Minister is not persuaded by the need for an increase, the Minister could decline to approve the increase.
  - The report also suggests that a new private health industry plan could reinforce incentives for insurers to improve their claims ratios.
- **Reducing hospital costs:** The report suggests that a new private health industry plan could provide the necessary incentives for private hospitals – which the report found are more likely than public hospitals to provide low value/no value care) to become more efficient. For example, it's suggested that insurers could pay private hospitals based on the number of patients treated (not based on the length of patient stay/services provided). It's estimated that this measure could reduce premiums by 5%.
- **Reducing out of pocket costs**: It's suggested that a new industry plan could include the necessary reforms needed to apply downward pressure on medical bills.
- **Reducing the price insurers pay for medical devices** (eg prostheses) to ensure that private patients (and their insurers) pay no more than public patients through government action.

  [Sources: Grattan Institute media release 19/05/2021; Report: Stopping the death spiral Creating a future for private health May 2021; The Conversation 19/05/2021]

The UK FCA is consulting on a proposed new 'consumer duty' to strengthen protections for consumers in financial markets

The Financial Conduct Authority (FCA) is consulting (CP21/13: A new Consumer Duty) on proposals to enhance existing consumer protections for consumers in financial markets through the introduction of a new 'Consumer Duty'.

The FCA states that new duty is expected 'drive a shift in culture and behaviour for firms, meaning that consumers always get products and services that are fit for purpose, that represent fair value and are clearly communicated and understandable. This will help, rather than hinder, consumers to make good choices and be confident that they will receive good customer service'.

Details

Broadly, it's proposed that the 'Consumer Duty' will have three elements:

- The 'Consumer Principle', which is intended to reflect the overall standards of behaviour the FCA expects from firms. The FCA is consulting on the following two (potential) wordings:
  - 'A firm must act in the best interests of retail clients'; or
  - 'A firm must act to deliver good outcomes for retail clients'.
- New 'cross cutting rules' requiring firms to take all reasonable steps to: a) avoid foreseeable harm to customers; b) enable customers to pursue their financial objectives; and c) act in good faith.
- New guidance and rules setting out detailed expectations for firm conduct around: a) communications; b) products and services; c) customer service; and d) price and value.
- Proposed scope/application:
  - It's proposed that the Consumer Duty will apply to products and services sold to retail clients (including the provision of financial services to SMEs where the FCA regulates the provision of those services).
  - It's proposed that all firms involved in the 'manufacture or supply of products and services to retail clients, even if they do not have a direct relationship with the end customer' would be covered.
- A possible 'private right of action'? The FCA is considering whether a breach of its Principles should give rise to a private right of action, noting that there are 'opposing and equally strong views from a variety of stakeholders on the issue'. At this stage, the consultation does not include any specific proposals for introducing a private right of action, through the consultation paper sets out feedback in favour/against this course. The FCA is seeking stakeholder views on how a private right of action could support/hinder the success of the proposed approach.

- A two stage consultation process: At this stage, the focus of the consultation is on the scope and structure of the proposed rules (which will be included in the FCA handbook), what they should cover and the outcomes they should seek to deliver. A further consultation will consider the drafting of the rules themselves (except for the Consumer principle).

Timing and Next Steps

- The consultation is open for comment until 31 July 2021.
- The FCA expects to consult again on proposed rule changes by 31 December 2021. This consultation will:
  - seek feedback on the proposed text for any new rules/guidance to implement the proposals
  - include further consideration of a private right of action and the impact of the introduction of the proposed Consumer Duty on the existing principles
  - include further detail around how the FCA intends to supervise the new Consumer Duty
- The FCA intends to make new rules by 33 July 2022.

[Sources: FCA media release 14/05/2021; CP21/13: A new Consumer Duty]

Deutsche Bank announces tougher sustainability goals

Deutsche Bank has issued a statement outlining a range of tougher sustainability commitments which it states are intended to embed sustainability into the culture of the bank.

A key change is that the bank has said it will bring forward its target to facilitate over 200 billion euros in sustainable finance and investments to 2023 (two years earlier than announced last year).

According to the statement, the target has been brought forward because the bank has made more progress towards reaching its goal than was originally anticipated. By the end of Q1 2021, Deutsche's business divisions had already facilitated sustainable finance and investments of 71 billion euros.

Deutsche has also announced various other measures. These include the following.

- Publishing annual sustainable finance targets for each business division (as a share of the overall 200 billion euros sustainable finance/investments target)
- To accelerate transformation among the banks' clients in the 'medium term', the bank will make having in place 'credible transformation plans' a prerequisite for 'continued collaboration' between the bank and those clients that are facing 'complex ESG challenges'
- A more sustainable supply chain:
  - From 2022, all the bank's vendors and suppliers with an annual order volume of more than 500,000 euros will be required to have an external ESG rating.
  - From 2023, a minimum rating will be a requirement in all new tender procedures or follow-on agreements with this minimum volume.
- Building on the commitment made in 2020, the bank will not only calculate the carbon footprint of its loan portfolio by the end of 2022, but also publish a target for its green asset ratio as a proportion of its banking book by mid-2022
- By year-end 2021, 50% of client-facing staff will be offered training on the bank's inhouse taxonomy for sustainable finance (which is aligned with the EU Taxonomy).
- Increasing female leadership within the bank: The bank has set new targets for:
  - 35% of Managing Director, Director and Vice President positions to be held by women by 2025 (currently women hold 29% of these roles).
  - 30% of roles two levels below the Management Board to be held by women by 2025 (up from 24% currently)

[Source: Deutsche Bank media release 20/05/2021]

Reducing red tape for superannuation funds – Consultation on proposed ECPI changes

Treasury has released two exposure draft Bills (and accompanying explanatory materials) for consultation which propose to reduce red tape for superannuation funds by:

- Amending the Income Tax Assessment Act 1997 to give superannuation fund trustees the choice to use their preferred method of calculating ECPI, where the fund is fully in the retirement phase for part of the income year, but not for the entire income year.

- Removing a 'redundant requirement' for superannuation funds to obtain an actuarial certificate when calculating ECPI, where the fund is fully in the retirement phase for all of the income year.

It's proposed that the amendments will apply to the 2021-22 income year and later income years.

The deadline for submissions to the consultation is 18 June 2021.

[Sources: Treasury consultation 21/05/2021; Minister for superannuation, financial services and the digital economy Jane Hume media release 21/05/2021]

APRA has published additional FAQs on meeting reporting standards under Phase 1 of the Superannuation Data Transformation

The Australian Prudential Regulation Authority (APRA) has published additional FAQs and worked examples for registrable superannuation entity (RSE) licensees to provide additional guidance on meeting reporting standards for Phase 1 of the Superannuation Data Transformation.

In particular, APRA flags that FAQ 1.2 has been updated to clarify reporting under Reporting Standard SRS 332.0 - Expenses.

[Source: APRA media release 21/05/2021; Frequently Asked Questions - Superannuation Data Transformation]

In Brief | APRA data shows total superannuation assets increased 3.1% for the quarter and 13.9% over the 12 months to March 2021 to hit a record high of $3.1 trillion.

[Sources: APRA media release 25/05/2021; Minister for Superannuation, Financial services and Digital Technology Jane Hume media release 25/05/2021]

In Brief | In a recent speech recapping key Federal Budget measures, Senator Jane Hume flagged that progressing the Retirement Income Covenant is 'the next cab off the rank' for the government, after the Your Future You Super Reforms

[Source: Minister for Superannuation, Financial Services and the Digital Economy Jane Hume media release 19/05/2021]

Risk Management

Climate Risk: New Bill proposes to make 'major emitters' liable for climate-change related damage

- The Greens have introduced a Bill – Liability for Climate Change Damage (Make the Polluters Pay) Bill 2021 – that proposes to give 'victims of climate change' eg 2020 bushfire survivors, and/or a Commonwealth, State or Territory Attorney Generals, the right to bring an action against thermal coal, oil and gas companies (major emitters) for climate change damage.
- Climate change damage includes (but is not limited to): financial or physical loss of property, infrastructure or other assets; death/illness, physical or psychological harms; the costs of responding to emergencies arising from more frequent natural disasters; and 'the costs associated with obtaining and maintaining insurance'.
- The Federal Court of Australia would have the ability to: a) grant an injunction requiring the 'major emitter' to reduce/cease activities that may cause future climate change damage; and b) determine the amount of damages the 'major emitter is liable for'. In making this determination, the court 'may assume the major emitter's share of the climate change damage is at least the same as their share of total global greenhouse gas emissions'.
- It's proposed that the measures would commence the day after the Bill receives Royal Assent.
- The Greens have previously introduced similar Bills in 2019 and 2020, but they have not had sufficient support to proceed.

[Sources: Liability for Climate Change Damage (Make the Polluters Pay) Bill 2021]

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