Governance News

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

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Contents

Boards and Directors

Expert panel discusses the implications of COP26 for Australian boards

The Australian Institute of Company Directors (AICD) recently hosted a panel discussion with Sam Mostyn (President of Chief Executive Women) and Zoe Whitton (Executive Director at Pollination) discussing the implications of the recent COP26 conference for Australian boards. The session was Chaired by Christian Gergis (AICD Head of Policy).

A recording of the session is now available on the LinkedIn platform here.

Diversity

Increasing diversity a top board priority according to Spencer Stuart's 2021 US board index

Spencer Stuart has released its latest annual US Spencer Stuart Board Index which tracks changes in board governance practices in S&P 500 companies.

A headline finding is that increasing board diversity, is a key priority for boards, with a particular emphasis on increasing racial/ethnic diversity. Boards also appear to be looking outside the pool of former/existing CEOs and/or serving directors to consider a wider range of candidates.

However, the report flags that overall progress is slow because mandatory age limits for director retirement remain the primary trigger for new board appointments. A brief overview of some of the key conclusions in the report is below.

Key Takeaways

Board diversity

Snapshot: gender, ethnic/racial and age diversity on S&P 500 boards

S&P 500 BOARD DIVERSITY	CURRENT STATE
Gender diversity	▪ 30% of S&P 500 directors are now women (up from 28% last year and up from 16% in 2011) ▪ There are zero all-male boards. ▪ Only 4% of boards have only one woman. ▪ 96% of boards include two or more women directors (up from only 58% in 2011) ▪ 36% of boards have three female directors and another 36% have four or more. In contrast, in 2011only 18% of boards had three or more female directors. ▪ Women remain underrepresented in senior board roles, though the number of women holding senior positions is trending (modestly) upwards. For example: only 8% of independent board chairs and 13% of lead/presiding directors are women (up from 4% and 11% respectively in 2020)
Ethnic/racial diversity	▪ 21% of all S&P 500 directors are Black/African American, Hispanic/Latino/Latina, Asian, American Indian/Native Alaskan or multiracial, 70% of whom are male. ▪ 92% of S&P 500 companies have at least one director from an underrepresented racial/ethnic group.
Age diversity	▪ The average age of independent directors of S&P 500 companies is 63.1 (up slightly from 62.4 in 2011). Most boards (82%) have an average board age in the 60s. Only 15% have an average age of 59 or younger, and 3% have an average age of 70 or older.

Diversity has emerged as the top recruitment priority

- According to a Spencer Stuart's survey of nomination/governance committee Chairs, the top three recruitment priorities when looking for new board members are: 1) candidates from underrepresented groups; 2) candidates with global perspective/experience; and 3) candidates with technology experience. Interestingly, these priorities ranked ahead of financial or operational experience.
- The report highlights that there is less focus on increasing board gender diversity which dropped from third in the list of priorities last year to tenth this year.
- The focus on increasing diversity in particular, appear to be reflected in the new director appointments in the 2021 proxy year (highlights below) and in the increased disclosure provided by companies on the issue. For example:
  - 60% of boards disclosed their ethnic/racial composition, with 28% of those boards providing director-specific details.

- 39% have adopted some type of commitment to diverse slates when considering new directors, up from 24% last year.

New director appointments

- According to the report, 72% of all new directors appointed have been from underrepresented groups (ie women, Black/African American, Asian, Hispanic/Latino/a, American Indian/Alaska native or multiracial men) up from 59% last year.
- Drilling down:
  - 43% of new directors are women (down from 47% in 2020), most of whom are white. Only 18% of new women directors appointed are Black/African American, Asian, Hispanic/ Latina, American Indian/Alaska native or multiracial directors
  - 47% of new directors are from underrepresented racial and ethnic groups. Of this group, 33% are Black/African American (up from 11% in 2020). The number of new Asian directors and Hispanic/Latino/Latina directors remains very low (each group accounts for 7% of new director appointments respectively).

Prior CEO or board experience is being accorded less weight

- According to the report, 35% of the S&P 500 directors appointed in the 2021 proxy year are serving on their first public company board (up from 28% in 2020)
- Interestingly, the report found that first-time directors are much less likely than experienced directors to be current or retired CEOs (ie only 6% of new directors are current/retired CEOs versus 31% of experienced directors). Rather, first time directors are more likely to come from line/functional lead roles (29%) or to be division/subsidiary presidents (19%).

Other corporate skills are valued: Most new director appointees come from functional, line and other corporate backgrounds

- 33% of new S&P 500 directors are active and retired corporate executives, including functional and other line leaders and division/subsidiary presidents (compared with 23% last year)
- Over the past decade the proportion of new directors who are active/retired CEOs has decreased from 36% in 2011 to 22%
- 56% of new directors are actively employed (down from 59% in 2011)
- New directors from underrepresented groups are more likely to be functional/other line leaders, but less likely to be active or retired CEOs

Board refreshment

Overall board size has remained fairly consistent over time

- According to the report board size has remained more or less stable over the past decade: Today, most (71%) of S&P 500 boards have between 9 to 12 members (vs 69% in 2011). Only 16% of boards have 13 or more directors (vs 17% in 2011)
- Annual elections are more or less the norm: 90% of boards have annual elections (up from 76% in 2011)
- In terms of board turnover, the rate remains low. On average, nomination/governance committee chairs indicate that they expect one director role to turn over in each of the next three years.

Director tenure

- Average board tenure has decreased by a year over the past decade from 8.7 years in 2011 to 7.7 years in 2021.
- 46% of serving directors have been in their role for five or fewer years and 27% have served for between 6 and ten years. The longest serving director has been on his board for 60 years.
- According to the report, explicit term limits for non-executive directors remain rare (6% of boards have explicit term limits). Of those companies that do, 73% limit director tenure to 15 years or more.
- Interestingly, the report flags that 'hybrid' tenure policies are 'emerging'. The report cites Microsoft's tenure policy as an example this. That policy targets an average tenure of 10 years or less for the board's independent directors.

Mandatory retirement age for directors

- The number of S&P 500 boards disclosing that they have a mandatory retirement age for directors has declined slightly from 73% in 2011 to 70% in 2021. Nevertheless, the report makes clear that this remains the primary trigger for the appointment of new directors.
- Interestingly, the mandatory age limit for directors has trended upwards over the last decade. In 2011 20% of boards had a mandatory limit of 75 years (or older), in 2021 this has risen to 51%.
- 18% of boards report not have a mandatory retirement age for directors
- 12% of boards to not reference mandatory retirement in their corporate governance guidelines.

Director workload

Overboading

- Most directors serve on two public boards: According to the report, most directors are not 'overboarded' with 34% of directors serving on one board and 35% of independent directors serving on two public boards. Of the remaining group: 20% serve on three boards and 11% serve on four or more boards. Only one director serves on six boards.
- 77% of S&P 500 boards report having some limit on directors accepting other corporate directorships (up from 74% in 2011)
- 112 boards do not report specific limits on additional board service, but according to the report, 98% of this group do require directors to notify the board chair prior to accepting an invitation to join another company board and/or encourage directors to 'reasonably limit' their other board service.

Boards met more often

- S&P 500 boards met 9.4 times on average in the 2021 proxy year. For context this is one and a half more meetings than the 7.9 meeting average in the 2020 proxy year. The report attribute this to the disruption/challenges caused by the pandemic.
- Due to COVID-19 related travel restrictions and the convenience of virtual meetings, most meetings were held virtually.

Director evaluations

- 98% of boards report conducting some sort of annual performance evaluation.
- 47% of boards disclose that they have some form of individual director evaluations (up from 44% last year and 34% in 2011)
- 22% of boards report working with an independent third party to facilitate the evaluation process (up from 21% last year). The report comments that a number of these boards indicate that they use an outside facilitator 'periodically' (ie once every two to three years).

Director pay

- The average total compensation for directors rose 1% to $312,279 from $308,462 last year, even though some boards took voluntary pay reductions during the height of the COVID-19 pandemic.
- The report found there was wide variation in total director compensation across industries ranging from a low of $266,088 in the real estate sector to a high of $349,014 in healthcare.
- Looking at average director compensation by company size, compensation ranged from a low of $290,245 for directors of companies with revenue less than $2.5 billion to a high of $330,144 for companies with revenue greater than $10 billion.
- Director compensation at companies in the greater-than-$10-billion-revenue category rose nearly 3%, but was virtually static for directors of smaller companies.

  [Source: Spencer Stuart 2021 US board index]

Meetings and Proxy Advisers

Meetings/electronic execution reform Bill: ACSI suggests different rules should apply for listed companies

Temporary relief enabling companies to use technology to meet regulatory requirements under the Corporations Act 2001 (Cth) around convening meetings, distributing meeting related materials and signing/executing documents is now in place until 31 March 2022.

A Bill proposing to introduce permanent reform - Corporations Amendment (Meetings and Documents) Bill 2021- was introduced into the House of Representatives on 20 October 2021 and referred to Committee for report by 18 November 2021. You can find a brief recap of the temporary measures currently now place and key measures in the Bill here.

ACSI's submission

Supportive of the majority of the proposed permanent reforms in the Bill

- Australian Council of Superannuation Investors' (ACSI) submission is supportive of proposed permanent changes to electronic signing, execution and communication of documents requirements included in the Bill.
- ACSI is also supportive of some proposed permanent changes to meeting requirements including:
  - Expressly giving companies the option to hold hybrid meetings
  - Provisions to ensure that shareholders as a whole have a reasonable opportunity to participate.
  - Poll voting for listed companies.
  - The opportunity for shareholders with 5% of votes to request an observer and an independent report on a poll

ACSI opposes measures in the Bill that would permanently enable all companies regulated under the Corporations Act 2001 (Cth) to hold wholly virtual meetings

The submission acknowledges that 'virtual-only meetings may be appropriate for many entities that are regulated by the Corporations Act, such as smaller and private entities'. However, ACSI considers that this is not the case for publicly listed companies where there is 'a heightened need for the shareholders of a listed company to access information, provide their views to the company, and engage with directors'.

Broadly, ACSI's key concerns about permanently enabling listed companies to hold virtual meetings are as follows.

- Virtual meetings 'do not generally provide the same opportunity for genuine interaction and engagement between shareholders and company representatives as hybrid meetings do'.
- The safeguards built into the Bill to ensure shareholders have a reasonable opportunity to participate are insufficient.
- The requirement that only companies who are expressly permitted under their constitution to hold virtual meetings will be able to do so, does not address the fact that:
  - some companies have already been successful in securing shareholder approval of constitutional amendments enabling them to hold wholly virtual meetings which means there is now 'a risk that these companies could seek to rely on such provisions…indefinitely'
  - companies have the option of including provisions in their constitutional enabling them to hold virtual meetings ahead of an Initial Public Offering (without the need for any shareholder vote). ACSI considers this could:

    > 'create uneven standards across the market, whereby some companies have a lower level of accountability and face less shareholder scrutiny than others. It could also mean that investors will be faced with a trade-off between a potentially good investment opportunity and the downside of reduced engagement and transparency. Such a trade-off is unnecessary, and it reduces the overall integrity of the Australian listed market'.
- giving companies the option to hold virtual meetings is in any case unnecessary (in light of ASIC's new powers to grant temporary relief where necessary)

Suggested solution – a 'carve out' for listed companies

ACSI states that these concerns could be addressed by amending the Bill to limit listed companies to holding either hybrid or physical meetings only. ACSI states,

> 'the most efficient solution would be specific provision in the legislation that applies only to listed companies and removes the option for virtual-only meetings. The legislation should allow listed companies to hold hybrid or physical meetings only. While there is simplicity in standardising the rules across all organisations, this should not come at the expense of achieving the most appropriate legal framework for separate segments of the market which have different structures and shareholder profiles. There are many areas of the Corporations Act where different rules apply to listed companies compared with other entities. Indeed, the proposed Bill has taken this approach in relation to voting by poll, by including a provision that applies only to listed companies. A carve-out would establish consistency across all listed companies, instead of a patchwork whereby some companies change (or have already changed) their constitutions and others do not'.
>
> [Source: ACSI submission: Corporations Amendment Meetings and Documents Bill 2021]

Disclosure and Reporting

A PR driven approach to disclosure: Federal Court upholds ASIC's case against GetSwift

In Australian Securities and Investments Commission v GetSwift Limited (Liability Hearing) [2021] FCA 1384, the Federal Court held that GetSwift Limited (GetSwift) made misleading statements and breached its continuous disclosure obligations when making statements to the Australian Securities Exchange (ASX) between February and December 2017.

Broadly, the Court held that the announcements incorrectly gave the impression that GetSwift had entered into subscription agreements with several major companies for GetSwift's software platform (eg Amazon among others), when in reality the companies were often only trialling the GetSwift platform and GetSwift was not generating revenue from the agreements. In addition, a number of companies elected not to proceed following the trial period. This information was not disclosed to the market.

According to ASIC, over the period that these announcements were being made, GetSwift's share price spiked almost 800% and the company also raised $100 million in capital from institutional investors.

Justice Lee described GetSwift's approach to disclosure in the following terms

> [8] 'At the risk of over-generalisation, what follows reveals what might be described as a public-relations-driven approach to corporate disclosure on behalf of those wielding power within the company, motivated by a desire to make regular announcements of successful entry into agreements with a number of national and multinational enterprise clients'.

Justice Lee also considered that three GetSwift directors, to a greater or lesser degree, were 'knowingly concerned' in this conduct, Justice Lee observes:

> [9] 'There is a plethora of documentary evidence in the form of emails exchanged between some of the directors revealing efforts directed at the strategic timing of ASX announcements, making sure that announcements were marked as "price sensitive", orchestrating simultaneous media coverage, and evincing an appreciation that the failure to release announcements of new client agreements would or could have a negative impact on investor expectations'

The Court also accepted that when concerns were raised by another director (who was not named as defendant in the proceedings and who was subsequently removed from the GetSwift board), they were dismissed as 'naive'.

Ultimately, the Court held that:

- In making the announcements and failing to fully disclose material information (eg that a number of agreements had been terminated), GetSwift engaged in misleading or deceptive conduct in breach of s1041H of the Corporations Act 2001 (Cth) (the Act) and s12DA of the Australian Securities and Investments Commission Act 2001 (Cth) and breached its continuous disclosure obligations under s 674(2) of the Act.

  [Note, the judgment includes at table at p311 (immediately after [1064]) that provides a summary of whether the elements of the continuous disclosure breaches were made out against each of defendants]

The Court also held that the three GetSwift directors (to varying degrees) were:

- knowingly involved in GetSwift's continuous disclosure breaches in breach of s 674(2A) of the Act
- failed to exercise their powers and discharge his duties as a director with the degree of care and diligence required in contravention of s 180(1) of the Act.

The Court also held that two directors engaged in misleading or deceptive conduct in breach of s 1041H and s 12DA of the Australian Securities and Investments Commission Act 2001 (Cth).

A hearing as to penalties will be held at a later date.

ASIC has welcomed the court's decision.

[Sources: Australian Securities and Investments Commission v GetSwift Limited (Liability Hearing) [2021] FCA 1384, ASIC media release 10/11/2021]

FRC releases guidance on the treatment of climate-related matters in annual financial reporting

The UK Financial Reporting Council (FRC) has released a climate reporting factsheet to clarify regulatory expectations with respect to consideration and/or treatment of climate-related risks/opportunities in annual financial reporting under FRS 102 The Financial Reporting Standard, which is applicable in the UK and Republic of Ireland.

Though FRS 102 contains no explicit references to climate-related matters, the FRC considers that these should nevertheless be considered 'in the same manner as any other matters which could have a material impact upon financial statements'.

Accordingly, the factsheet provides guidance to preparers of financial statements on:

- how the minimum reporting requirements in FRS 102 should be applied in the context of climate-related matters (eg in the context of disclosure around whether the company is a 'going concern')
- how climate-related risks/opportunities may impact the recognition and measurement of items in the financial statements

The factsheet also includes a summary of current and proposed climate-related legal and regulatory requirements to 'support entities in considering how to achieve the required linkage between their financial and narrative reporting'.

The FRC states that it has released the factsheet, as part of a broader work program to lift standards of climate-related disclosure – both in the context of narrative reporting and financial statements - in recognition of the increasing stakeholder demand.

[Sources: FRC media release 12/11/2021; FRC fact sheet: FRS 102, Fact Sheet 8 Climate Related Matters]

In Brief | A framework for net-zero target setting: The Science-based Targets initiative has launched a new Paris Agreement compatible, net-zero emissions standard for businesses which is intended to provide a framework for setting science-based net-zero targets consistent with limiting global temperature rise to 1.5°C. The 'central focus' of the new standard is on the achievement of 'rapid, deep emissions cuts' ie reducing value-chain emissions by 90-95%

[Sources: SBTi media release; SBTi corporate net zero standard]

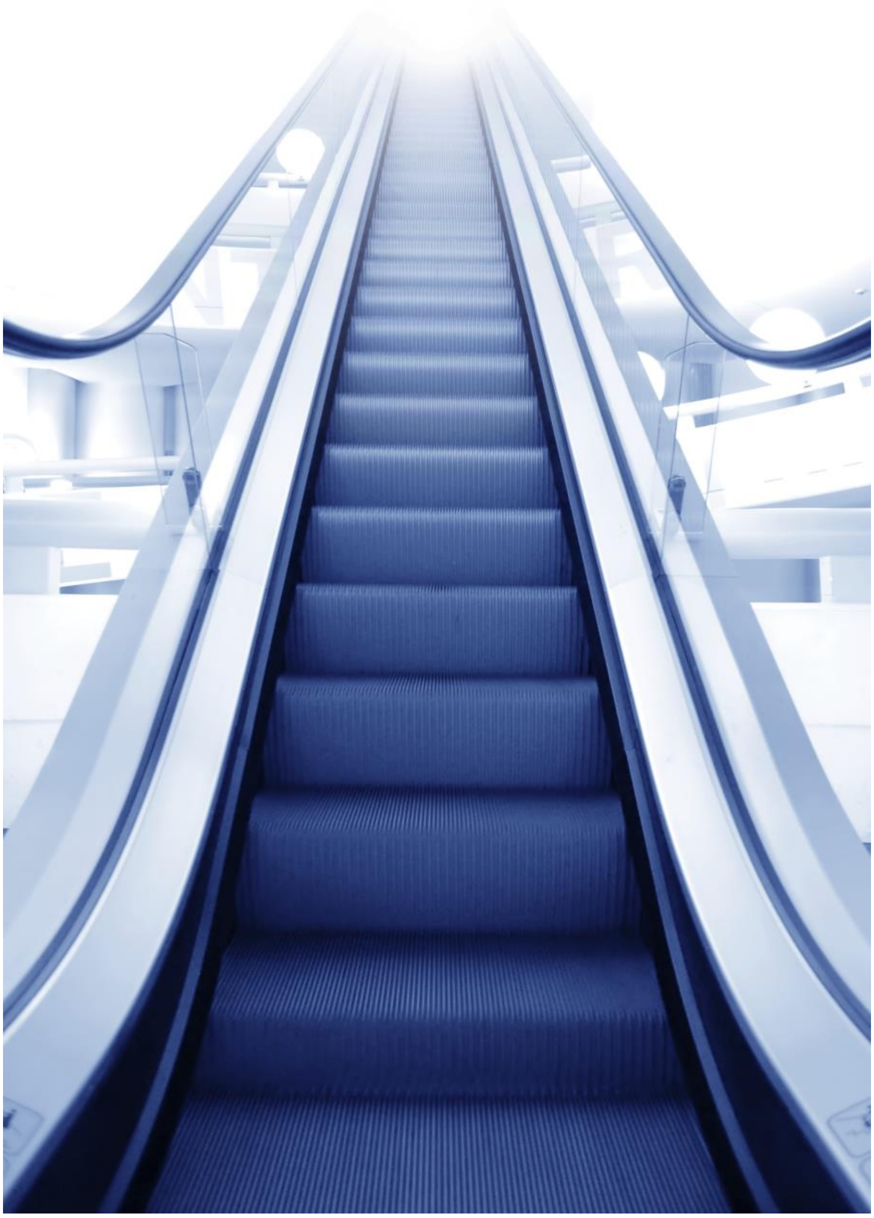
In Brief | ASX confirms that new reporting requirements in the ASX Listing Rules for Oil and Gas companies are planned (subject to the necessary regulatory approvals) to come into effect on 1 July 2022. ASX intends to issue updated guidance 'well before the transition date of 1 July 2022'. ASX encourages entities who wish to do so, to 'early-adopt the changes'

[Sources: Listed@ASX Compliance Update no. 10/21 16/11/2021; Consultation Response Proposed changes to the oil and gas reporting requirements in the ASX Listing Rules 22/10/2021]

Institutional Investors and Stewardship

'Say on climate' resolutions: A potentially useful investor tool (provided the focus remains on accountability)?

- The Responsible Investment Association (RIA) has released an article discussing the emergence of 'say on climate' resolutions and the potential benefits/drawbacks from an investor perspective. For context, 'say on climate' resolutions are modelled on 'say on pay' resolutions. Broadly, a 'say on climate' resolution (which may be a management proposal or a shareholder proposal) provides shareholders with a regular opportunity to approve (on a non-binding basis) a company's climate transition plan.



- Existing mechanisms to exert pressure have limited effect: The RIA observes that investors can exert pressure on companies/boards on climate issues in a range of ways. For example, by putting forward/supporting shareholder climate resolutions and/or by voting against the Chair as a signal of concern about the way in which the company is approaching a particular issue (eg climate risk). However, the RIA considers that voting against the Chair to register concern in this way, even where there is follow up with the company following the vote to explain the rationale behind it and to 'ensure it doesn't get lost in the mix', is not always optimal. RIA comments,

  > 'while voting to remove a sitting director is arguably one of the strongest actions you can take, the clarity of the message can get lost among the myriad reasons we vote against directors'.

- In light of this, RIA considers that 'say on climate' resolutions could be helpful both in promoting transparency around the actions companies are taking and in pushing companies that have been slow to detail their strategies to do so.

- Unintended consequences? However, despite the potential benefits, RIA also considers that there are may be 'unintended consequences' associated with 'say on climate' resolutions. The RIA sums up these concerns as follows:

  > 'Voting for transparency is not the same as voting on the quality of a company's climate plan. Are investors equipped to vote effectively on each and every climate action plan? And will this discourage investors from holding the board directly responsible for its oversight role on climate? Is it not the role of the board to set the

strategy, and the role of investors to toss the board, if they don't like the job they are doing – not ask them to pass their oversight responsibilities to investors? And most vexing of all, will it follow the path of say-on-pay votes and result in only the most egregious cases getting voted down? The binary nature of the vote means there is little room for nuance in assessing plans'.

- Concerns appear to be shared by investors: The RIA points to the fact that to date, though management proposed (and endorsed) 'say on climate' resolutions have received 'overwhelming support' at a number of companies, shareholder proposed 'say on climate resolutions' resolutions have failed to pass (receiving on average 25% support). RIA considers that this is evidence that though supportive of companies electing to give shareholders a 'say on climate', they are 'wary' about requiring boards/companies to do so.

  [Note: Professor Robert Eccles has flagged concerns about the usefulness of 'say on climate' resolutions, suggesting that though well-intentioned, they are 'futile, and a drain on the engagement bandwidth of investors who have more effective tools for getting their portfolio companies to mitigate and adapt to climate change'.]

- How to make 'say on climate' resolutions an effective tool for addressing climate concerns? The RIA considers that though imperfect, 'say on climate' could potentially provide a useful supplement if used in combination with other existing accountability mechanisms. The RIA suggests that the following issues should be considered in this context.
  - The RIA questions whether an annual advisory vote 'optimal' given the longer-term nature of transition plans, and suggests that a longer voting cycle may be more appropriate. The RIA does not put a figure on how long should elapse between 'say on climate' votes.
  - The RIA raises concerns the 'binary nature' of 'say on climate' votes which the RIA considers leaves 'little room for nuance' in assessing the quality/content of climate transition plans. 'While companies choosing to be transparent should be commended, simple transparency is not the goal – a robust climate strategy is. Investors will need to balance those two elements and reflect that in their voting' RIA states.
  - From an accountability perspective the RIA questions whether investors should take voting action against the board/individual committee members 'where the climate plan is poor'. The RIA suggests that 'the benefit of the advisory vote might be to provide investors a way to distinguish between an unsatisfactory plan and a governance failure, where the latter requires votes against directors'.
  - The RIA considers that, assuming 'say on climate' resolutions become common practice, many investors will not have the resources to assess transition plans and therefore will rely to a significant extent on proxy adviser research. This in turn means that investors need to take steps to ensure that proxy advisers 'use a robust and transparent framework for their assessment'.
  - In of the fact that a vote in support of a 'say on climate' resolution may not necessarily signify unequivocal endorsement of the company's transition strategy/plan, but 'only directional approval', the RIA considers that it will be important for investors to follow up with companies following their vote to explain the rationale behind their voting decision and raise any specific concerns.

  [Source: Responsible Investment Association media release 11/11/2021]

Global report concludes that institutional investors are increasingly 'walking the walk' on ESG investing

Key Takeouts

- The report found that globally, investors appear to be increasingly 'walking the walk' on ESG integration
- ESG is now being embedded throughout organisations
- Methods of ESG integration are becoming more sophisticated for example, negative screening is no longer the preferred/most common approach.
- Despite the 'positive signals' BNP Paribas considers there 'remains considerable areas for development'. For example: many respondents still incorporate ESG into less than half of their portfolio and data remains a key barrier to progress.

BNP Paribas has released its latest report tracking developments in asset owners'/asset managers' approach to integrating ESG. The headline finding is that since the first report in 2017, there has been a marked, rapid shift in approach to the point where ESG is now well-embedded (even if there remains room for improvement).

The findings in the report are based on a survey of 356 institutional investors across Europe, North America and the Asia Pacific.

Key Takeaways

- **Progress is quicker than BNP Paribas predicted.** In 2019, no survey respondents could see a future see a future where 75% or more of an investor's portfolio would integrate ESG by 2021. This year's survey found that there had been a significant shift in outlook and that this is translating into action. For example:
  - 22% of investors integrate ESG into at least 75% of their portfolios. The report describes this as a 'staggering upsurge in commitment'.
  - 13% of investors integrate ESG into 100% of their portfolios.
  - 21% of respondents indicated that ESG is 'central or a necessity to their business' (up from 10% in 2019).
  - 45% of respondents consider ESG capabilities to be embedded throughout the organisation (up from 23% in 2019). Interestingly, SSGA found that smaller firms are more likely than their larger peers to have embedded ESG throughout the organisation rather than have it siloed within a team. SSGA suggests that this may be a reflection of the fact that larger firms (which have in the vanguard of ESG investing) are more likely to have started with a specialist team, longer ago than smaller firms which have integrated ESG more recently and have tended to adopt a whole of organisation approach.
  - The report found 75% of respondents are now employing ESG integration as their preferred approach (as opposed to negative screening). That is, instead of 'merely excluding companies and certain sector from their investment strategies, asset managers and owners are now including ESG factors in their analysis and decisions to better manage risk and improve returns'. BNP Paribas considers that this is a sign of growing maturity in approach.
- Top motivations for ESG investing: Survey respondents ranked 'brand and reputation' as the key driver behind their approach to ESG (up from 47% in 2019). 'External stakeholder requirement' ranked second, followed by improved long term returns.
- Data remains the primary barrier to integration of ESG considerations: 59% of 2021 survey respondents cite issues related to data as a top barrier (up from 66% in 2019).
- Respondents nominated the 'social' aspect of ESG as the most difficult to analyse/integrate (51% of respondents). The report suggest that this is due to the lack of data and standardisation of data around social metrics.
- Engagement is playing an ever increasing role: The survey found that investors are engaging with companies more frequently to influence ESG outcomes. For example: 61% of investors engage with companies as part of their ESG strategy. (64% asset managers, 58% asset owners).
- Readiness for SFDR:
  - 48% of respondents based in Europe consider that they understand the Sustainable Finance Disclosure Regulation (SFDR) and what it means for their organisation. The report comments that this relatively is a reflection of both the phased rollout (the most significant enforcement due to take place in 2022) and the fact that details of final requirements are still being developed.
  - 47% consider it is too early to know what the full impact of SFDR will be.
  - 24% consider that the SFDR will set a new global standard for ESG disclosure.

  [Source: BNP Paribas report: The path to ESG: No Turning Back for Asset Owners and Managers]

Global survey flags that decarbonisation targets are set to become the norm for investors over the next few years

Key Takeouts

- Global survey found that most investors will set decarbonisation targets for their portfolios over the next three years meaning that this will become 'very much the norm'.
- The primary motivation behind investors committing to/planning to commit to decarbonising their portfolios is a desire to drive the global transition to a low carbon economy
- Engagement rather than divestment is the preferred approach

State Street Global Advisers (SSGA) has released a report into how investors are implementing/planning to implement decarbonisation strategies and the challenges to implementation. The report is based on a survey of senior executives with asset allocation responsibilities at 300+ institutions globally.

Key Takeaways

- According to SSGA, though as yet only 20% of investors globally have committed to a specific portfolio decarbonisation target, two thirds of survey respondents indicated that they intend to do so in the next three years. Looking at it by region: 70% in APAC, 71% in Europe and 61% in North America intend to set specific decarbonisation targets for their portfolio in the next three years.
- 77% of survey respondents overall indicated that they are already taking action on decarbonisation. In contrast, only 9% of respondents globally indicated they are not doing so.
- Of those respondents that have set decarbonisation targets most are prioritising decarbonisation across all asset classes, though equities, fixed income and real estate are the highest priorities.
- Engagement is generally preferred over divestment:
  - The report found that 73% of investors overall are confident in their ability to decarbonise their portfolio without substantial divestment. Drilling down: investors with decarbonisation targets in place are more confident of this (85%) and investors who have not got targets in place are substantially less confident (63%).
  - Overall, respondents view engagement and more robust criteria for asset managers as the most important strategy to address climate issues over the next three years
- A shift in investor motivation:
  - 44% of respondents overall cited their responsibility 'to drive the economic transition and help to solve the global climate crisis' as the primary driver behind their decision to factor climate issues into investment decisions and/or work towards portfolio decarbonisation making it the primary driver behind these decisions. Pressure from stakeholders ranked lowest on the list of motivators.
  - Looking at this by region, APAC respondents were by far the most likely (60%) to rank driving the economic transition and helping to solve the global climate crisis as their key motivation. In contrast, for both Europe and the US this was closer to 30%.
  - The survey comments that these results are a marked change from the 2019 survey where respondents ranked fiduciary duty and the need to meet regulation in equal first place as the key motivator.
- Top 'barriers' standing in the way of investors committing to decarbonisation targets are: 1) 'insufficient data quality to support robust target setting and reporting'; and 2) concern about the potential negative impact on performance. Concern about the perceived lack of clarity around regulatory requirements/reporting frameworks ranked behind these concerns.

  [Source: State Street Global Advisers report: The World Targets Change November 2021]

Regulators

Consultation on proposed changes to the UK regulatory framework for financial regulators

Following the withdrawal of the UK from the EU, and building on an earlier consultation, the UK government is consulting on proposed changes to the UK regulatory framework for financial regulators.

Broadly, the paper endorses the current regulatory model as set out in the Financial Services and Markets Act 2000 UK (FSMA) with some proposed amendments.

Proposed key changes include:

- adding new statutory growth and international competitiveness secondary objectives for the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA)
- Amending existing regulatory principles to 'ensure that sustainable growth should occur in a way that is consistent with the government's commitment to achieve a net zero economy by 2050'
- Introducing 'enhanced mechanisms for accountability, scrutiny and oversight' of the regulators
- Giving financial services regulators responsibility for 'setting many of the direct regulatory requirements which are currently set out in retained EU law'. This would entail broadening the regulators' existing rulemaking powers where required.

The due date for submissions to the consultation is 9 February 2022.

[Sources: HM Treasury consultation: Future Regulatory Framework Review: Proposals for reform 9/11/2021-09/02/2022; Consultation paper]

Basel Committee plans to consult on principles for the management/supervision of climate-related financial risks

- Climate related financial risks
  - The Basel Committee (Committee), as the primary global standard setter for the prudential regulation of banks, has agreed to consult on principles for the 'effective management and supervision of climate-related financial risks at internationally active banks'.
  - The Committee has commenced work on developing a 'suite' of potential measures to address climate-related financial risks to the global banking system, following the publication of a series of analytical reports earlier this year.
  - On the issue of disclosure, the Committee welcomed the establishment of the International Sustainability Standards Board (which will develop global sustainability disclosure standards). The Committee also flagged that it is 'exploring the use of the Pillar 3 framework to promote a common disclosure baseline for climate-related financial risks'.
- Cryptoassets: The Committee also plans to further consult on principles for the prudential treatment of banks' cryptoasset exposures in mid-2022 following feedback on an initial consultation.
- Disclosure standards: The Committee has approved the final standards for Pillar 3 disclosures related to the revised market risk framework and a set of voluntary disclosures for banks' sovereign exposures. The final disclosure standards will be published in the coming weeks.
- Risks and vulnerabilities to the global banking system: The impact of the 'prolonged low interest rate environment and its evolving outlook on banks' profitability, business models and risk taking behaviour' as well as banks' operational resilience were flagged as risks that the Committee intends to continue to monitor.

[Source: Basel Committee media release 09/11/2021]

Financial Services

Top Story | Status update: 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 almost three years since its release a number of actions have been implemented in response – though in many cases, the changes have not yet been fully implemented.

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. We will be updating the table regularly.

The table was last updated on 17 November 2021 to reflect developments relating the following recommendations.

- Recommendation 4.14 (Insurance in superannuation: Additional scrutiny for related party engagements)
- Recommendation 4.15 (Insurance in superannuation: Status attribution to be fair and reasonable)

You can access the updated table here

Inquiry into the Sterling Income Trust hears that ASIC is 'satisfied that the judgments made were reasonable' and that the introduction of Product Intervention Powers and Design and Distribution Obligations have changed the game

In his opening statement to the Senate Standing Committee on Economics Inquiry into the Sterling Income Trust, Australian Securities and Investments Commission (ASIC) Chair Joseph Longo said that:

- The Sterling Group 'placed its clients into arrangements that were novel, complex and high-risk'.
- The liquidators of the Sterling Income Trust and the Sterling Group have indicated that 'there is little change of meaningful returns to creditors in the winding up of sterling entities' and a possibility that creditors will receive zero returns.
- Since the collapse of the Sterling group there has been significant law reform including:
  - the introduction of Design and Distribution Obligations (DDOs) which mean that product providers are no longer able to market any product (regardless of the complexity) to consumers, provided there is formal disclosure. Instead product providers are required to identify the class of consumers a product is suitable for and target the product marketing accordingly.
  - the introduction of product intervention powers which enable ASIC to make a product intervention order when a financial/credit product will result/is likely to result, in significant consumer detriment.
- With respect to ASIC's regulatory role in relation to the Sterling collapse, the Committee heard that ASIC is 'satisfied that the judgements we made were reasonable, based on the information we had at the relevant times'. In saying this, Mr Longo acknowledged that 'those who have suffered losses have wished for us to move faster at times or to have intervened earlier'. However, he pointed to the time required to collect proper evidence and follow due process, and to the 'difficult choices about which reports of misconduct to examine and which apparent breaches to investigate'. He observed that given ASIC's 'finite resources, as well as those of the prosecuting authorities and courts, mean we cannot pursue all possible breaches of the law'.
- ASIC considers that certain aspects of the conduct involving the Sterling Group 'may have been criminal in nature and warrant close consideration by the Commonwealth Director of Public Prosecutions'.

[Source: ASIC Chair Joseph Longo, Opening statement to the inquiry into the Sterling Income Trust 16/11/2021]

APRA has released an information paper explaining its macroprudential policy framework

The Australian Prudential Regulation Authority (APRA) has released an information paper providing an overview of its macroprudential policy framework ie the framework the regulator uses to determine whether: a) macroprudential intervention is appropriate; and b) if so, which tool/combination of tools is best suited to achieving its intended objective.

The information paper includes:

- a summary of the objectives of APRA's macroprudential policy and the key indicators that APRA monitors to assess the need for a macroprudential policy response. APRA emphasises that the macroprudential framework is 'founded on' APRA's statutory purpose of promoting financial system stability in Australia, as required by the Australian Prudential Regulation Authority Act 1998 (Cth). The objective of the macroprudential framework is to 'mitigate risks to financial stability as a system wide level', typically by introducing measures through the banking system.
- an overview of the available tools/options available including: capital, credit, liquidity and other measures.
- an overview of implementation considerations.

APRA has a broad range of macroprudential tools that can be used to mitigate financial stability risks. From an implementation standpoint, APRA states that 'decisions on changes to prudential requirements are ultimately for APRA to determine. However, where changes are being made for macroprudential purposes, the Council of Financial Regulators (CFR) has an important role in assessing the level of systemic risk and coordinating regulatory responses across agencies'.

Announcing the release of the information paper, APRA Chair Wayne Byres said that purpose in releasing the information paper he said, is provide insight into this aspect of APRA's work.

> 'APRA has a wide range of tools it could potentially deploy in such circumstances. Today's paper is intended to give financial industry stakeholders a better understanding of the factors APRA considers in making decisions to use these tools, the types of macroprudential measures APRA could deploy in the future, and how they might be implemented'.
>
> [Sources: APRA media release 11/11/2021; APRA Information paper: Macroprudential policy framework]

APRA is consulting on proposed additions to APS 220 Credit Risk Management

The Australian Prudential Regulation Authority (APRA) has released for consultation a proposed new attachment to Prudential Standard APS 220 Credit Risk Management (APS 220): Attachment C Macroprudential policy: credit measures.

APRA states that the objective of the proposed new attachment is to:

> 'strengthen the transparency, implementation and enforceability of macroprudential policy. The proposed attachment to APS 220 includes a set of credit-based macroprudential measures that could be used to address systemic risks if needed. It would also require ADIs to preposition in advance to address potential barriers to implementation, supporting a timely response to any emerging risks'.

Proposed key changes

APRA states the proposed attachment, would introduce formal requirements for ADIs to:

- 'ensure they have the ability to limit growth in particular forms of lending' ie residential mortgage lending and commercial property lending. APRA flags that it may broaden the focus of the proposed measures to apply to other areas over time, if 'other portfolios potentially grow in systemic importance or other risks emerge'.
- 'moderate higher risk lending during periods of heightened systemic risk or meet particular lending standards, at levels determined by APRA'; and
- 'ensure there would be adequate reporting in place to monitor against limits'.

APRA emphasises that the new requirements 'do not change the potential macroprudential tools APRA may use, or provide APRA with additional powers' but would change the way in which certain measures may be applied.

Proposed timing and next steps

- The due date for submissions to the consultation is 28 February 2022.
- APRA expects to finalise its response to the consultation on the new Attachment C Macroprudential policy: credit measures in the first half of 2022. APRA intends that the new requirements would 'come into effect shortly thereafter'.
- From 1 January 2022, ADIs will also be required to meet the previously finalised requirements of APS 220 Credit Risk Management, including Attachment A – Collateral Valuation and Attachment B – Prescribed Provisioning.

APRA has also flagged that it may take further action

APRA states that together with other members of the Council of Financial Regulators, it continues to monitor risks in residential mortgage lending and 'may consider further macroprudential measures, should risks related to residential mortgage lending continue to build'.

[Sources: APRA media release 11/11/2021; Letter to industry]

Inquiry into Housing Affordability and Supply hears that APRA's approach to regulating residential mortgage lending is focused on ensuring banks 'are making sound credit decisions' not on targeting house prices

In a short opening statement to the House of Representatives Standing Committee on Tax and Revenue - Inquiry into Housing Affordability and Supply Australia Australian Prudential Regulation Authority (APRA) Executive Director Policy and Advice Division Renée Roberts spoke about APRA's role as a financial regulator, and more particularly APRA's approach to the regulation of residential mortgage lending.

- APRA's role: Ms Roberts said that APRA’s role is to 'set prudential requirements that are designed to protect the interests of depositors and promote financial system stability in Australia'. With respect to residential mortgage lending, Ms Roberts said that 'APRA’s objective is to ensure the financial system remains safe, with banks lending to borrowers who can afford the level of debt they are taking on'.
- APRA’s approach to regulating residential mortgage lending: Ms Roberts made clear that:

  'APRA seeks to ensure that banks are making sound credit decisions that are appropriate, individually and in aggregate, in the context of broader housing market and economic trends. APRA’s prudential requirements, which are focused on lending practices, can influence the terms, amount and price at which banks extend housing finance. They do not target house prices or matters of affordability'.

- APRA's recent actions to address 'emerging risks to financial stability':
  - Ms Roberts noted APRA's recent decision to increase the minimum interest rate buffer it expects banks to use when assessing the serviceability of home loan applications from 2.5% to 3%. Ms Roberts said that APRA expects that the overall impact of this change on aggregate housing credit growth will be 'fairly modest' given that 'many borrowers do not borrow at their maximum capacity'.
  - Ms Roberts also flagged the information paper setting out APRA's framework for using macroprudential policy which sets out the risk factors APRA uses to identify emerging threats to financial stability, the available policy tools and 'the importance of consulting with other members of the Council of Financial Regulators as part of the decision-making process'.

[Source: Renée Roberts, Executive Director, Policy and Advice Division, Opening statement to House of Representatives Standing Committee on Tax and Revenue - Inquiry into Housing Affordability and Supply in Australia 15/11/2021]

APRA Chair outlines changes to the 'architecture for ensuring bank resilience in Australia'

- In his speech to the UBS Australasia Conference, Australian Prudential Regulation Authority (APRA) Chair Wayne Byres spoke about APRA's role and recent work on building financial resilience in the banking sector. More particularly, Mr Byres' comments focused on three APRA papers – the first on the bank capital framework, the second outlining APRA's macroprudential framework and the third on the topic of resolution - which together will 'lay out the architecture for ensuring bank resilience in Australia'. All three papers will have been released by the end of the year.
- A key message in the speech was that the 'strengthening' of the 'architecture' should not be viewed by industry as an abrupt shift in policy direction, but rather as a 'natural evolution' that is 'consistent with APRA's ongoing resilience mandate'. Ultimately APRA considers that firms are already 'well equipped to handle' the changes (despite their significance). In support of this, Mr Byres observed that:
  - the Australian banking system is already operating with capital levels in excess of that required by the new capital framework.
  - APRA's macroprudential framework 'does not introduce significant new approaches; it simply seeks to provide more transparency as to how APRA will go about applying macroprudential policies'.
  - The proposed resolution framework will 'formalise much of what we have been applying through supervision in recent years'.

Further Detail

Bank Capital Framework

- Mr Byres said that improving the bank capital framework has been a 'work in progress' for the entire time that he has been APRA Chair.
- This work is underpinned by seven aims/objectives: The two primary objectives are: 1) implementation of the Basel III framework which is due to come into effect from the beginning of 2023; and 2) delivery of the 2014 Financial System Inquiry recommendation that APRA 'set capital standards such that Australian bank capital ratios were "unquestionably strong"'.
- The five further objectives are to:
  - 'enhance its risk sensitivity in key areas, including through applying more capital overall to residential mortgage portfolios given the structural concentration in this asset class for Australian banks;
  - improve the flexibility of the framework, by providing a larger proportion of capital to be held in the form of capital buffers that can be drawn upon in times of stress;
  - improve transparency and comparability, by increasing the alignment of APRA's standards with the international Basel framework and making local adjustments easier to discern;
  - support competition, primarily by narrowing the gap in capital requirements between the standardised and modelled approaches, and adding in safeguards to ensure the two approaches do not excessively diverge; and
  - increase proportionality, through the introduction of simplified capital requirements for smaller, less complex banks'.
- Mr Byres highlighted some of the features of the new framework. A key change will be raising minimum capital requirements to achieve the 'unquestionably strong' objective, consistent with the benchmarks set in 2017. Mr Byres said that APRA anticipates that the changes will mean that the largest banks will be 'in the top quartile of capital strength when measured on a consistent basis against their international peers'.
- Mr Byres made clear that the banking system 'already has more than enough capital to meet the new requirements'.
- Mr Byres flagged that strengthening of capital requirements 'will involve a larger share held in the form of regulatory buffers that can be utilised in times of stress. A portion of this buffer will be constant, and another portion – the Countercyclical Capital Buffer…will be time-varying'.
- Mr Byres said that 'rebasing risk weights' to increase alignment with Basel Standards will mean that reported capital ratios will be slightly higher under than under the existing framework which he likened to the shift from imperial to metric measures – ie 'the number of units increased when we changed from inches to centimetres, even though nothing actually got longer or taller'.
- Mr Byres said that the transparency and comparability of the framework will be improved both because:
  - 'differences between the Australian regime and the Basel standards will be lessened in some areas, and many of the local differences will be easier to identify and (if needed) adjust for'
  - 'the requirement for banks using advanced modelling approaches to also report their capital ratio under the standardised methodology will ensure there can be a more meaningful like-for-like comparison between domestic banks'.
- Mr Byres concluded that this approach meets APRA's stated objectives.

  'Overall, we believe we have created a strong and flexible capital framework. It complies with the minimum Basel standards (without the need for a lengthy phase-in). It lifts minimum requirements consistent with our 'unquestionably strong' objective. And it is more risk sensitive, flexible, proportionate and transparent than the current framework. Of course, no system is perfect, but we are confident the new framework will provide a strong regulatory foundation for the ongoing health and stability of the banking system – whatever ups and downs might lie ahead'.

Macroprudential framework

- Mr Byres said that in releasing the information paper outlining APRA's macroprudential framework APRA intended to provide 'more transparency to the objectives we pursue (and those we don't), the tools we have available, and the way in which we implement macroprudential policy'.

- Mr Byres observed that though APRA has access to a number of different macroprudential tools, 'in practice, most of the action will take place through capital and credit related tools applied to the banking sector, reflecting the critical role that leverage plays in considerations of financial stability'.
- Macroprudential flexibility has been built into the capital framework eg through the setting of a non-zero Countercyclical Capital Buffer (CCyB) as a default level.
- Mr Byres observed that to date APRA has not deployed the CCyB

  'largely because it risked complicating the build-up of capital that was occurring in response to the "unquestionably strong" benchmarks. However, as we settle into the new system, we see benefit in having a requirement that can be dialled up, and down, in response to the peaks and troughs of the economic cycle. So, we propose to utilise a default setting of 1 per cent for the CCyB, giving us scope to adjust this over time in response to conditions'
- Having said this, Mr Byres observed that APRA 'may not choose to use capital-related measures at all'.

Resolution framework and additional loss absorbing capacity

- APRA plans to release a proposed framework and proposed prudential requirements for 'resolution and additional loss absorbing capacity' before the end of 2021. Mr Byres commented:

  'We have devoted considerable resources in recent years to enhancing contingency planning within the financial sector, and developing our resolution plans. But unlike most other jurisdictions in the world, we have done so without the foundation of a set of formal prudential requirements. Our upcoming paper on APRA's resolution framework will mark the commencement of formal consultation on such requirements'.
- Mr Byres said that APRA's work in this area has three primary objectives. These are as follows.
  - 'That APRA-regulated entities are prepared for stress that may threaten their viability, and understand what options they have to respond;
  - that if an entity is reaching the point of non-viability, it can be resolved in an orderly manner such that key customers – depositors, policyholders and fund members – are protected and system stability is preserved; and
  - that wherever possible, solutions to financial stress – either contingency planning or resolution – are not reliant on taxpayer support'.
- Mr Byres flagged that APRA also plans to finalise its approach to additional loss absorbing capacity (LAC) (within this broader framework). Mr Byres said that APRA's 2019 goal of eventually achieving an 'overall level of LAC in line with international peers, would 'probably require additional LAC in the order of 1 to 2% of risk-weighted assets' and APRA considers that this 'remains the right objective'.

  [Source: APRA Chair Wayne Byres Speech to the 2021 UBS Australasia Conference 15/11/2021]

Hayne Implementation: APRA finalises revisions to SPS 250 and SPG 250

Following consultation, the Australian Prudential Regulation Authority (APRA) has finalised SPS 250 Insurance in Superannuation (SPS 250) and the accompanying guidance (SPG 250).

The revisions are aimed at 'ensuring better member outcomes through updated requirements for trustees to select, manage and monitor members' insurance arrangements'. The changes also implement APRA's response to Hayne Recommendations 4.14 and 4.15.

For context:

- Hayne Recommendation 4.14 recommended that:

  'APRA should amend Prudential Standard SPS 250 to require RSE licensees that engage a related party to provide group life insurance, or who enter into a contract, arrangement or understanding with a life insurer by which the insurer is given a priority or privilege in connection with the provision of life insurance, to obtain and provide to APRA within a fixed time, independent certification that the arrangements and policies entered into are in the best interests of members and otherwise satisfy legal and regulatory requirements'.
- Hayne Recommendation 4.15 recommended that:

  'APRA should amend Prudential Standard SPS 250 to require RSE licensees to be satisfied that the rules by which a particular status is attributed to a member in connection with insurance are fair and reasonable'.

APRA considers that it has 'now finalised its response to all 10 recommendations directed to it by the Royal Commission in 2019'.

Key Changes

Broadly, the revisions to SPS 250 will require trustees to:

- strengthen arrangements to protect members from potential adverse outcomes caused by conflicted life insurance arrangements. SPS 250 includes 'heightened obligations on the RSE licensee to assess whether there are any conflicted provisions or business practices with respect to insurance arrangements, and whether they are appropriate and in the best financial interests of beneficiaries'.
- require trustees to obtain an independent certification for related party insurance arrangements, 'before entering into, or materially altering, an insurance arrangement, and on a triennial basis.' APRA confirms that 'independent certification will only be required to consider the best financial interests of beneficiaries, and will not be required to also assess whether the arrangement satisfies legal and regulatory requirements'. However, the response paper comments that 'it is nevertheless APRA's expectation that ensuring compliance with legal and regulatory requirements will be a core part of an RSE licensee's risk management framework and practices'. APRA observes that this is a departure from the original proposed approach, in response to industry feedback.
- reinforce APRA's expectations that an 'RSE licensee undertake rigorous analysis to ensure that the kind and/or level of insurance offered does not inappropriately erode the retirement income of beneficiaries'.

APRA also expects that the changes will both: a) strengthen data management to improve analysis of member outcomes across different groups of superannuation fund members; and b) facilitate easy opt-out of insurance for members, and ensure premiums do not unduly erode members' retirement incomes.

The enhancements to SPS 250 will commence on 1 July 2022.

> [Sources: APRA media release 12/11/2021; APRA response paper: Insurance in superannuation 12/11/2021; SPS 250 Insurance in Superannuation (SPS 250); SPG 250 Insurance in Superannuation (SPG 250); Consultation on Prudential Standard SPS 250 Insurance in Superannuation]

Superannuation portfolio holdings disclosure: Regulations registered

- The Corporations Amendment (Portfolio Holdings Disclosure) Regulations 2021 were registered on 11 November 2021. .
- The purpose of the regulations is to support 'the portfolio holdings disclosure regime by prescribing the manner in which information provided under the portfolio holdings disclosure regime must be organised'. Broadly, the regulations require superannuation funds to publicly disclose information about the identity, value and weightings of their investments
- Announcing the new regulations, the government said that the changes will significantly boost transparency around superannuation fund investments, and facilitate comparison of different products by members.

  'Members will be able to clearly see how much of their retirement savings are being invested by superannuation funds across a range of asset classes and derivatives. This information will make it easier for members to compare products and identify the most suitable fund for them. Reviews of the superannuation system have found that superannuation portfolio disclosure is unduly opaque, does not meet global best practice and that requiring the disclosure of portfolio holdings would provide greater transparency and allow members to understand where their superannuation is invested'.

- The amendments apply in relation to reporting days that occur on or after 31 December 2021. The government states that this will mean that superannuation funds will be required to first report their holdings by 31 March 2022 and then on a six monthly basis.
- The government flagged that it will monitor disclosures and consider 'further refinements where necessary.

Super Consumers Australia has welcomed the changes

In a statement, Super Consumers Australia (SCA) Director Xavier O'Halloran said that the new regulations 'are a significant improvement on the status quo' because the changes:

- will make it easier for members to understand whether their fund is investing 'in line with their values while delivering on their best financial interests'

- improve 'systemic transparency and help academics, analysts and researchers get a better understanding of how each fund is investing'. This will contribute to 'the understanding of best practice and ultimately benefit people's retirement incomes.;
- complement other recent measures to enhance transparency eg requirements to notify members about marketing expenses, political donations and payments to industry bodies.

Mr O'Halloran added that SCA considers there is 'value in monitoring whether greater transparency in future could deliver further benefits to fund members'.

> [Sources: Joint media release Treasurer Josh Frydenberg and Minister for Superannuation, Financial Services and the Digital Economy Jane Hume 11/11/2021; Corporations Amendment (Portfolio Holdings Disclosure) Regulations 2021; Super Consumers Australia media release 12/11/2021]

CFR to review derivative use by superannuation funds

- The government has requested the Council of Financial Regulators (which is the coordinating body for the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), the Reserve Bank of Australia (RBA) and The Treasury) to report on the use of derivatives by superannuation funds and to flag 'any implications for the operation of our financial system that could arise from these exposures'.
- The CFR is expected to 'draw upon' both the Australian Prudential Regulation Authority's (APRA's) information gathering powers and expertise from CFR members including the Reserve Bank of Australia in preparation of the report.

What prompted this action?

- The request follows an earlier consultation on changes to portfolio disclosure requirements (which have now been finalised in Corporations Amendment (Portfolio Holdings Disclosure) Regulations 2021) which revealed that some funds have 'large exposures to derivatives'.
- The government's announcement states:

> 'Given Australia's superannuation funds have now become a systemically important part of our financial system, it is timely to ensure policymakers and regulators have a sound understanding of the extent and nature of the use of derivatives, and any implications for the operation of our financial system that could arise from these exposures'.

> [Source: Joint media release Treasurer Josh Frydenberg and Minister for Superannuation, Financial Services and the Digital Economy Jane Hume 11/11/2021]

In Brief | Draft remediation guidance released for consultation: ASIC is conducting a further round of consultation on a draft guidance on the way in which licensees would conduct remediations to return money owed to consumers. In response to industry feedback, the revised draft includes additional examples. The due date for submissions is 11 February 2021

> [Source: ASIC media release 17/11/2021; CP 350 Consumer remediation: Further consultation; Attachment to CP 350: Draft regulatory guide]

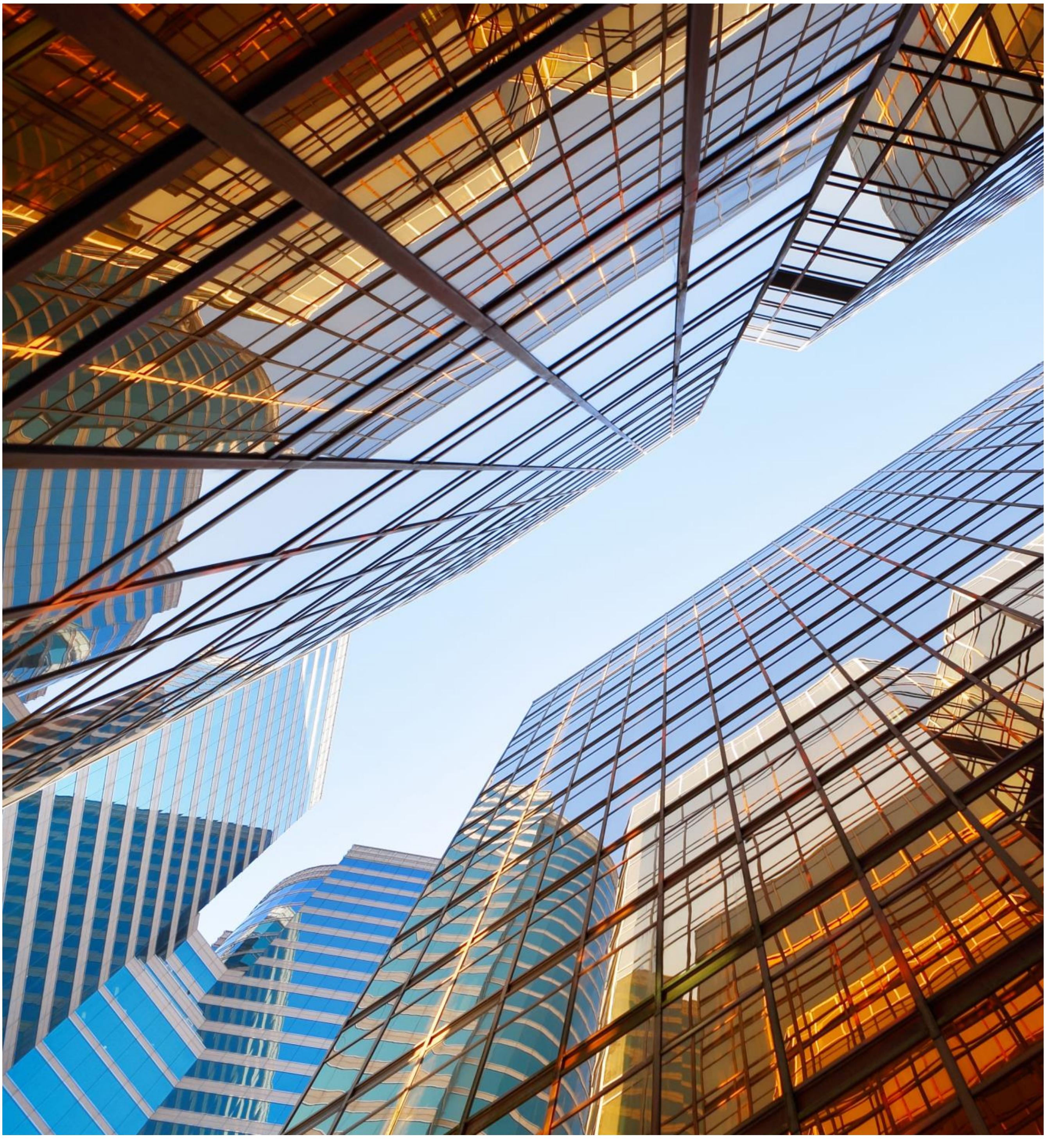
In Brief | More information available, but super members remain disengaged? APRA has called on super members to 'more actively engage' with their super after the regulator's analysis found that only 7% of members have taken action to move their savings elsewhere following the recent MySuper performance test. Executive Board Member Margaret Cole said 'Increased transparency is a powerful tool for regulators to bring about improvements in superannuation fund performance, but members should never forget they also have the power to make decisions that will better secure their future in retirement'

> [Source: APRA media release 10/11/2021]

Accounting and Audit

In Brief | The UK FRC has published an audit 'blueprint' outlining the regulator's expectations for delivery of a 'high quality audit'. FRC CEO Sir John Thompson said the report is the 'first time, the FRC has set out its expectations of what good looks like'

[Sources: FRC media release 16/11/2021; Full text report: What makes a good audit?]



Risk Management

Top Story | (Still) time for business to prioritise ethics: The Governance Institute has released its latest annual Ethics Index

Our key takeaways from the Governance Institute of Australia's 2021 Ethics Index and some points of comparison with the 2020 Index.

Key Takeouts

- The Governance Institute's latest Ethics Index has found that public perceptions of Australia as an ethical society have dropped compared with last year, and this is reflected in overall drops across sectors, organisations and roles.
- The financial services sector is no longer ranked as the least ethical sector overall, though public perceptions of the financial services and corporate sectors remain low
- Consistent with the 2020 Index, CEOs, Chairs, Managing Directors, senior executives and directors of foreign companies operating in Australia and mortgage brokers were ranked among the top ten least ethical occupations.
- Climate risk was ranked in the top three ethical challenges facing Australia

Some interesting findings

The Governance Institute's sixth annual Ethics Index tracks changes in public attitudes to the importance of ethics generally and also changes in public perceptions around the extent to which certain groups can be trusted to behave ethically.

The findings are based on a survey of 1000 people conducted during 10-20th September 2021.

Australian society is perceived as overall less ethical than last year

- Overall the 2021 Index found that public perceptions of how ethical Australian society is decreased compared with 2020, with the Governance Institute's overall metric for measuring this dropping from a record high of 52 in 2020 to 45 in 2021.
- All sectors saw a dip in perceptions of their ethical behaviour (to varying extents) compared with 2020. However, consistent with 2020, the education, health and charity sectors remained the top three most ethical sectors. The sharpest drops were in the government/public service sector (which saw a 10 point drop from 56 to 46) and the media sector (which fell 20 points from 22 to 2).
- Governance Institute CEO Megan Motto attributed this overall decline to the additional uncertainties and lack of consensus around pandemic management that have come into play in 2021.

> 'Last year, we placed vast amounts of trust in our governments, scientists and health and emergency service workers during the initial waves of lockdown – and our trust was rewarded as we saw, in many cases, COVID-19 numbers settling, lockdown lifting and the resumption of most activities. The Ethics Index skyrocketed to a five-year high of 52.
>
> However, 2021 has been a very different year. We have seen major fluctuations in approaches to managing the virus, stronger debate around when to lockdown – and when to open up, and we were all thrown by a new variant of the virus. It has been a tumultuous and anxious locked down year with greater uncertainty. It seems this is reflected in a dip in the latest Ethics Index'.

Climate action is ranked among the top ethical challenges facing Australia

Top five greatest short term ethical challenges: Respondents nominated the following issues as the top five greatest ethical challenges facing Australia in the next 12 months.

- 1. balancing personal freedoms with COVID control 54% (up from 44% in 2020);
- 2. reducing our reliance on global supply chains 33% (unchanged from 2020);

- 3. ensuring climate change and environmental issues continue to receive attention and action 32% (up from 28% last year).
- 4. executive remuneration: 'greater scrutiny, transparency and oversight of board and executive remuneration, ensuring economic conditions of the day are accounted for and reflective in senior pay rates' 27% (up from 24% last year)
- 5. increased surveillance of the population via CCTV, apps, QR check ins to monitor public health or reduce crime 23% (up from 15% last year)

Interestingly, aged care reform which ranked third on the list of top concerns in 2020 does not appear in the list of 12 priorities included in the 2021 Index. Likewise, the need to balance fire reduction with hazard reduction and conservation which ranked fifth last year is also not included.

Climate risk: When asked to nominate who has an ethical obligation to tackle climate change the majority respondents indicated that the Federal and State governments as well as multinational corporations have an urgent ethical obligation to act. 71% of respondents consider the Federal government has an urgent ethical obligations, and 68% of respondents consider that State governments and multinational corporations also have an urgent ethical obligation.

Corporate and financial sectors still have work to do?

The 2020 Ethics Index (summarised) found that financial services sector and the corporate sector more broadly had work to do to improve perceptions of their behaviour. For example the 2020 Index found that:

- the financial services sector was rated the least ethical of all sectors
- financial services and social media organisations dominated the list of the most unethical organisations overall
- CEOs, Chairs, Managing Directors, senior executives and directors of foreign companies operating in Australia and mortgage brokers were ranked among the top ten least ethical occupations.

The 2021 Index shows some movement.

Least ethical organisations overall

- Fewer financial services organisations are included in the list of ten least ethical organisations in 2021 as compared with 2020.
- The 2021 Index lists the ten (perceived) least ethical organisations overall as (ranked from most ethical to least ethical) as follows: 1) Journalists; 2) Life insurance companies; 3) Magazine; 4) Federal Parliament; 5) Instagram; 6)Foreign companies operating in Australia; 7) Twitter; 8) Facebook 9) TikTok; and 10) Pay Day Lenders
- 'Other insurance companies', investment banks and retail banks which were included in the 2020 list, no longer appear, replaced by Journalists, Magazine and Parliament.

Perceptions of the financial services sector slipped further backwards

- In 2020, the financial services sector was rated the least ethical of all sectors with the lowest ethical score of all sectors (18, up from just -11 in 2019).
- The 2021 Index found that public perceptions of the sector have slipped backwards, with the score dropping from 18 to 11 (though not back to 2019 levels).
- However, despite this, the sector is no longer ranked as the least ethical sector overall – the media sector has replaced it with a score of just 2, down from 22 in 2020
- Consistent with the 2020 survey, industry superannuation funds are perceived to be the most ethical of all organisations in the sector. Pay day lenders are perceived to be the least ethical. Life insurance companies ranked in second last place above pay day lenders with a score or -8 (down from 1 in 2020)
- Accountant remains the occupation with highest ethical score in the banking and finance sector. Mortgage broker remains the occupation with the lowest ethical score in the sector.

Softening in perceptions of the Corporate sector

- Consistent with the 2020 Index, CEOs, Chairs, Managing Directors, senior executives and directors of foreign companies operating in Australia and mortgage brokers were all ranked among the top ten least ethical occupations.

- The 2021 index found that the ten least ethical occupations overall were (ranked from most ethical to least ethical): 1) mortgage brokers; 2) senior executives; 3) CEOs/Managing Directors; 4) Chair of companies; 5) Lawyers; 6) State politicians; 7) Local politicians; 8) Directors of foreign companies operating in Australia; 9) Real estate agents; and 10) Federal politicians.
- At an organisational level, perceptions of:
  - foreign companies operating in Australia dropped from -4 in 2020 to -16 in 2021
  - Australian unlisted and private companies also declined slightly from 16 in 2020 to 11 in 2021
  - listed public companies was almost flat: 27 in 2020 to 28 in 2021.
- Company secretary remains the occupation with highest ethical score in the corporate sector. Directors of foreign companies operating in Australia remains the occupation with the lowest ethical score in the corporate sector.

Top five ethical issues for corporate Australia

- Corruption remains the top issue facing corporate Australia(57%), followed by company tax avoidance (47%), misleading and deceptive advertising (45%), discrimination (44%) and executive pay (43%).
- Environmental responsibility ranks sixth in the list (40%).
- Treatment of suppliers ranked lowest on the list (21%).

Attitudes to COVID-19 measures

- Some COVID-19 workplace safety measures had strong support from respondents eg 60% of respondents supported employers requiring employees to wear mask in the office. In contrast, others eg monitoring employees working from home using surveillance technology were not generally supported (30%). The Index attributes this difference to the extent to which respondents perceived the measure to be ethical (or not).
- More broadly, support for certain other pandemic-related measures decreased compared with 2020. For example support for curfews dropped from 41 in 2020 to 15, and support for continued international border closures fell from 67 to 42.

[Sources: Governance Institute media release 17/11/2021; Governance Institute Ethics Index 2021]

FTSE350 boards rank climate ahead of cyber risk as the top risk facing firms

The Chartered Governance Institute UK and Ireland has released its latest FTSE 350 Boardroom Bellweather survey monitoring changes in board attitudes to various challenges including (among other things) a range of governance issues such as board diversity, stakeholder engagement and risk.

The respondents to the survey are company secretaries at FTSE 350 companies. The report explains that this is because 'their pivotal position at the heart of the boardroom gives them a unique perspective on how boards are responding to external pressures'.

Key Takeaways

Board Diversity

- Overall, the survey found that boards perceive themselves to be diverse. For example:
  - 87% of respondents consider their boards is diverse in terms of business experience
  - 80% of survey respondents consider their boards is gender diverse (down from 84% in the December 2019 survey)
  - 55% of respondents consider their board is ethnically diverse (up from 29% in the December 2019 survey)
- Most respondents (71%) also considered that their policies on ethnicity and diversity in the workplace are fit for purpose.
- The survey found that boards are divided when it comes to the perceived diversity of their executive pipelines: 41% of respondents consider their pipeline is insufficient and 51% believe the opposite. Drilling down, larger companies appear slightly more confident on the issue than smaller companies: 43% of FTSE 100 companies believe their pipeline to be insufficient vs 57% of FTSE 250 companies.

Pay Gap reporting

- Gender pay gap – intention is there….

- According to the report, 59% of survey respondents indicated that their company intends to take action to reduce the gender pay gap.
- Interestingly, only 27% of companies reported reporting their company's gender pay gap had resulted in changes to pay policies/strategy.

- Most survey respondents (57%) consider it will be difficult or very difficult to report on their company's ethnic pay gap. A further 16% of respondents consider reporting on the issue will be 'somewhat difficult', and 16% are neutral.

Employee engagement

- Respondents were divided on the question of whether their approach to 'workforce voice' had changed over the period of the pandemic with 53% indicating that it had changed and 43% indicating that it had not.
- Getting the 'workforce voice' into the boardroom: The UK Corporate Governance Code 2018 includes a requirement (on an if not/why not basis) for companies to explain how the board is engaging with/aware of the views of the workforce.
  - 68% of survey respondents considered that their board was more aware of worker views as a result of their efforts to meet this requirement.
  - The survey found that consistent with the December 2019 survey, the most the most common option for ensuring that workers have a voice in the boardroom is having a designated non-executive director (NED) to represent worker interests on the board. 43% of companies have adopted this approach.
  - The least common option remains having an employee director on the board. Only 2% of respondent indicated their company had adopted this approach.

Attitude to Risk

- 67% of respondents consider that their risk is increasing (up from 49% in the December 2019 survey).
- Of the companies that consider their risk to be increasing, climate change was considered the biggest risk ahead of cyber risk and global economic risk.

Climate Change

- 96% of survey respondents indicated that their company has discussed climate change at least once over the last year.
- 69% of survey respondents have published plans to tackle climate change. Of these companies, the majority (62%) are FTSE 100 companies and 39% are FTSE 250 companies.
- Published climate plans cover a range of timespans:
  - 39% focussing on five to ten years
  - 25% cover up to five years
  - 17% covering a 10-15 year time span
  - 19% plan for more than 15 years
- 57% of companies have published a net zero ambition.
- Despite the increasing investor interest in ESG issues, only 16% of companies hold an ESG investor day. The report suggests that this may indicate there 'is a potential appetite for such an event, although restrictions on movement during the pandemic might have been a factor in this result'.

Cyber risk

- 88% of companies believe that their exposure to cyber risk is increasing. Of this group, 89% are spending more mitigating the risk.
- Only 50% of boards have discussed the NCSC's Cyber Security Toolkit for boards. Actions taken by those boards which have reviewed the toolkit include training, identification of a lead director, as well as regular review and oversight by the audit committee and the board.
- Although artificial intelligence (AI) has the potential to disrupt business models, just 3% of companies consider it to be a major risk.

Culture

- Culture continues to be a major focus for all boards: 100% of survey respondents said their companies have discussed culture at least once during the year and 37% indicated they had discussed it four to six times

Executive pay

- Executive pay remains a key focus for boards. The report points to boards taking into account various factors in this context:
  - 94% of survey respondents indicated that consideration of the impact of the pandemic was a factor in executive remuneration discussions.
  - 72.5% of companies take the pay ratio between the CEO and average employee into consideration (broadly in line with the December 2019 survey which found 74% of companies did so)
  - 69% of companies now consider the gender pay gap as part of their executive pay considerations, but only 16% of companies consider the ethnic pay gap.
- The report also found that companies are (fairly) responsive to investor feedback on the issue. For example, 35% of companies have made changes to their remuneration policy following feedback from investors (down from 61% in the December 2019 survey)
- The report flags that the level of concern about the detrimental impact of 'increasing rules and scrutiny' is having in terms of attracting talent has increased considerably from 38% in December 2019 to 53% in this survey.

Corporate governance wishlist

- The report includes a 'corporate governance wishlist' listing the 'one regulation' respondents would 'most like to see the government bring in or reform'.
- Among other things, the list includes:
  - 'Removal of the requirement to consult with the workforce on executive pay' ranked third on the list.
  - The introduction of 'a new regime in relation to authentication of documents/ requirements for signatures to allow for electronic signatures'.

  [Source: Chartered Governance Institute UK and Ireland media release 08/11/2021; Full text report: FTSE350 Boardroom Bellweather Survey 2021]

ASIC reiterates calls for companies to review their whistleblower policies and supporting processes

Key Takeouts

- ASIC has reminded reporting entities of the need to review existing whistleblower policies to ensure compliance with legal requirements and address gaps/weaknesses identified in ASIC's recent review of whistleblowing policies
- Conducting a review of whistleblower programs with a focus on: a) 'how entities are handling whistleblower disclosures'; b) 'how entities use the information from disclosures to address issues or misconduct or change their operations'; and c) 'the level of board and executive oversight of whistleblower programs' will be a priority for the regulator in 2022

- Australian Securities and Investments Commission (ASIC) Commissioner Sean Hughes has given a speech - Whistleblower policies and the compliance gap – outlining the importance/benefits of the whistleblowing regime; recapping the findings of ASIC's recent review of whistleblower policies and reiterating calls for companies to prioritise reviewing their existing policies and supporting processes to ensure compliance with existing laws (see: Governance News 20/10/2021 at p27).
- Mr Hughes said that 'strong whistleblower systems, processes and procedures are – and always will be – a vital element of good corporate culture' and a key focus for ASIC.

The introduction of the whistleblower reforms has seen a spike in reports to ASIC:

- Mr Hughes said that as the 'conduct regulator' ASIC is benefiting from the information being provided by whistleblowers about corporate misconduct and is able to perform this role more effectively as a result. For example he said that there has been sharp spike in the number of whistleblower reports made to ASIC in recent years:
  - In RY2018–19, (before the 2019 reforms commenced), ASIC dealt with 278 whistleblower reports.
  - The following year, this had increased to 644 whistleblower reports. This number increased again to 817 reports in FY2020-21.

- Mr Hughes said that from an enforcement perspective, ASIC has investigations on foot into alleged breaches of whistleblower protections.
- Mr Hughes called on anyone who has 'suffered detriment for making a whistleblower disclosure or because something thinks you have' to contact ASIC as the regulator 'may be able to take action against the company or individual for their detrimental actions'.

Recap of the findings of ASIC's review of whistleblower policies

- Mr Hughes provided a brief recap of the purpose and key findings of ASIC's review of 102 whistleblower policies which was conducted in FY2020–21. Mr Hughes said that the purpose of the review was to: a) understand how entities are implementing the new requirements; b) understand/benchmark the standard of policies across entities; and c) 'refine ASIC's regulatory approach to the requirements'.
- Broadly, Mr Hughes said that though some policies met some of the minimum legal requirements the 'majority of policies…reviewed did not fully address' them. The three 'most prevalent and concerning deficiencies' ASIC identified were:
  - **Inaccurate/incomplete information:** Mr Hughes said that 'around of third' of all policies sampled provided incomplete/inaccurate information about the protections available for whistleblowers which he flagged as being of particular concern because it may dissuade/discourage whistleblowers from speaking out. Mr Hughes said that 'policies that did well in this area' provided clear information, in 'positive terms' about the protections available for whistleblowers.
  - **Obsolete information:** Mr Hughes said that 40% of policies reviewed contained obsolete or out of date information. For example policies: included references to obsolete/outdated legislative requirements; almost half of all policies reviewed did not fully/accurately describe who a whistleblower can report to instead listing only the company's preferred internal reporting channels; and others encouraged whistleblowers to discuss concerns with their managers before making a report 'without clarifying that

those discussions may not qualify for whistleblower protections'. On the positive side, Mr Hughes said two thirds of policies reviewed 'acknowledged that whistleblowers could disclose anonymously and qualify for protections'.

  - **Oversight mechanisms:** Mr Hughes said that close to a third of policies did not mention whether the entity had in place oversight arrangements to monitor the effectiveness of the policy. Though acknowledging that this is not a legal requirement, Mr Hughes said that it is of concern to the regulator because it 'suggests there is an attitude of "set and forget" which is not good enough'. Mr Hughes said:

    > 'ASIC wants to see entities treating their whistleblower programs as an important governance function which supports robust and timely escalation of important information and cultural warning signs to an organisation's leadership. This includes review mechanisms to monitor their effectiveness. We also encourage entities to integrate insights from their whistleblower programs with other information sources for boards to make decisions'.

- Mr Hughes said that these issues are of 'particular concern because they 'suggest that many entities do not fully understand the enhanced whistleblower protection regime, or worse still, have chosen to ignore them'.

Call to action for Australian CEOs

- Reminder to review existing whistleblower policies:
  - Mr Hughes noted that following the review, ASIC wrote to the CEOs of public companies, large proprietary companies and corporate superannuation trustees urging them to review their whistleblower policies to ensure compliance with current legal requirements. Mr Hughes reiterated the importance of CEOs acting on this.
  - Mr Woods said that in the new year, ASIC will continue to monitor compliance and plans to conduct another review of whistleblower policies 'in the future'. Mr Hughes said that where non-compliance is identified, ASIC will 'draw upon the full suite of regulatory tools we have available to us, which includes enforcement action'.
- Review internal systems and processes: Mr Hughes said that 'one of our priorities in the coming year' is to conduct a review of whistleblower programs to assess how 'practices are evolving to address the reforms'. Specifically, Mr Hughes said that ASIC plans to focus on: a) 'how entities are handling whistleblower disclosures'; b) 'how entities use the information from disclosures to address issues or misconduct or change their operations'; and c) 'the level of board and executive oversight of whistleblower programs'.

ASIC's own approach to whistleblowing

- Mr Hughes briefly described some aspects of ASIC's approach. This includes:
  - the recent launch of a new reporting platform to encourage/make it simpler for people to raise issues/report. The new platform also makes it easier to those who wish to remain anonymous to raise issues anonymously and to remain anonymous throughout the assessment and investigation process.
  - processes/resources to ensure prospective whistleblowers have confidence that: a) any issues raised will be assessed confidentially; b) they will be protected from retaliation; and c) that 'they will be treated fairly, professionally and respectfully'
  - processes have been designed to ensure that immediate issues flagged in reports are actioned and that the information is analysed to identify trends/address emerging risks 'before they become systemic'
  - ASIC's approach is expected to evolved/improve over time.

Moving in the right direction

- Mr Hughes concluded by observing that despite the issues identified in ASIC's review of whistleblower policies, 'Australia's corporate sector whistleblower regime is moving in the right direction'. Mr Hughes opined that:

  > 'Once companies have caught up to the new requirements I believe we will see even greater benefits to the health and sustainability of the culture within Australia's corporate sector'.

- Referencing the ISO 37002 Guidelines for Whistleblowing, and developments in the EU (eg implementation of the standards in the Whistleblower Protection Directive (EU 2019/1937), Mr Hughes flagged that 'ASIC may consider some of the broader practical guidance in these guidelines in our next review'.

[Source: Speech by ASIC Commissioner Sean Hughes at the 3rd Australian National Whistleblowing Symposium, 11/11/2021]

Governance Theory/Principles

The problem with 'stakeholder supremacy'? Elliott Management's Paul Singer reflects on the role of 'owners'

Key Takeouts

- Elliott Management's Paul Singer writes that ultimately, accountability to owners (including activist investors) is key to driving improved company performance and ensuring accountability. This benefits both activist investors and shareholders as a whole.
- Mr Singer considers that taking into account the views/interests of stakeholders is not inconsistent with the prioritisation of shareholder returns. However, he argues that claims by companies of the need to give equal weight to 'stakeholder' interests can too easily be used as an excuse for poor returns.

Elliott Management's Paul Singer has written an article reflecting on the important role that investors as the ultimate owners of companies play in driving improvements in companies' performance and ensuring management is held accountable. Mr Singer raises concerns about the various pressures being brought to bear on shareholder rights, and in particular the rise of 'stakeholder supremacy'.

Mr Singer takes as his starting point the position that public ownership is 'the essence of modern capitalism — which, along with the rule of law, has been responsible for the spectacular growth in global living standards over the past 200 years.'

He argues that accountability to shareholders in general, and the ability of activist investors in particular to provide constructive critique/feedback is fundamental to this.

> 'Activist investors do not just analyse and select securities and companies in which to invest. They also interact with company managements, publicly and/or privately, in a dialogue that the activist hopes will validate its analysis (or show why it is wrong) and lead to improvements in the company's performance. Activists aim to influence outcomes and "make something happen" to cause a company's share price to increase and hold its gains'.

Mr Singer writes that in his experience, 'most public company management teams do not like being told what to do, and they really do not like their performance to be critiqued by outsiders who have the temerity to call themselves "owners"' and for this reason, tend to dismiss outside criticism, no matter how valuable/constructive it may be. Mr Singer gives various examples of this including: companies lobbying for regulations to make it harder for activists to build positions and/or attempting to shift the focus away from their own performance to the holding period of activists.

On this last point, Mr Singer comments that the critiques levelled at activists often do not take into account the broader benefits that activist campaigns deliver to owners as a whole.

> 'While activists are the owners of the shares in which they invest, the largest activists represent millions of direct and indirect beneficiaries who receive most of the value from the activism as well as from other trading activities…These people and institutions are among the real owners of interests in shares held by activist investors. The narrative of a battle between rich-guy investor and beleaguered but beneficent management is just phony. Activists often represent "the people" much more than do the executives and directors on the other side of the table, many of whom own little or no stake in their company other than free options (heads they win, tails the shareholders lose)'.

Mr Singer considers that 'stakeholder supremacy' is essentially another technique being adopted by some companies, to avoid accountability for poor performance. He states:

> 'what the "stakeholder supremacy" theory of capitalism is designed to do…is allow weaker corporate management teams to justify poor shareholder returns by citing a need to serve some higher corporate purpose. The fact that it is largely gibberish is disguised by the air of moral superiority with which it is presented, leaving all too many investors uncomfortable challenging its logic, its purposes or its impact on corporate performance and rates of return'.

In putting forward this view, Mr Singer does not suggest that stakeholder views should not be considered/have no place. Indeed, he makes clear that:

> 'In reality, the prioritisation of shareholder returns is perfectly consistent with the goal of balancing the needs and competing interests of all of the company's other stakeholders. The best leaders constantly adjust to maintain equilibrium among stakeholders' competing interests — and indeed, they must serve the needs of stakeholders in order to keep the company healthy and profitable for the shareholders'.

Mr Singer also acknowledges that some shareholders are 'oddly' applying pressure on companies to adopt 'shareholder supremacy'. He attributes this to investors' misplaced assumption of high returns.

> 'having become 'so used to high and consistent returns from stocks that they now assume that such returns — the returns on which so many important social goods depend — must be easy to generate, and that no harm will come to shareholders from encouraging corporate executives and boards to take their eyes off that particular ball' he writes.

[Source: Harvard Law School Forum on Corporate Governance and Financial Regulation 15/11/2021]

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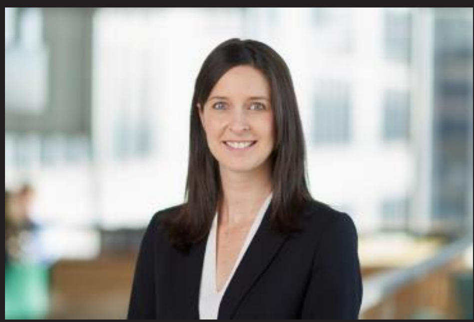

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