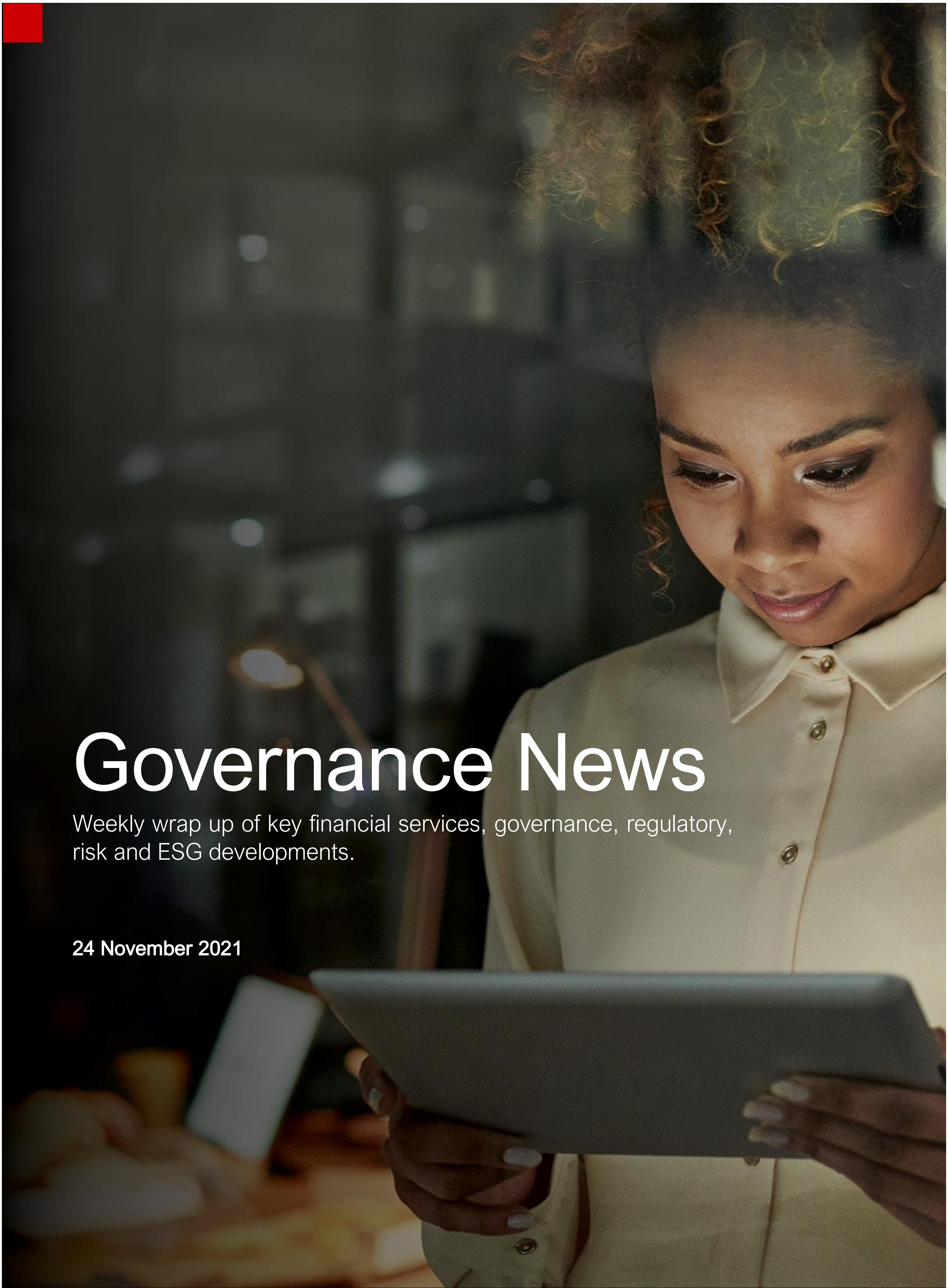


Governance News

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

24 November 2021

Contents

Boards and Directors

Top Story | APRA calls on boards to be proactive in their oversight of cyber-risk

Three areas where APRA would like to see improvement in board-oversight of cyber risk

Key Takeouts

- APRA has reiterated its expectation that boards adopt a proactive approach to oversight of cyber-risk. The regulator has said that it expects boards to 'have the same level of confidence in reviewing and challenging information security issues as they do when governing other business issues'.
- APRA considers boards need to be more proactive in the following three areas: 1) 'reviewing and challenging' management reports on cyber issues generally; 2) ensuring organisations are in a position to recover from cyber-attacks (including recovering lost data); and 3) ensuring the effectiveness of information security controls across the supply chain.

APRA calls on boards to step up their oversight of cyber risk

The Australian Prudential Regulation Authority (APRA) has released an article outlining its expectations of boards with respect to oversight of cyber-risk. The key message for boards is that:

> 'APRA expects boards to have the same level of confidence in reviewing and challenging information security issues as they do when governing other business issues'.

Further, APRA expects boards to adopt a proactive approach. APRA states that it is

> 'ultimately the board's responsibility to ensure that management is fully across the cyber threat they face and, where necessary, takes appropriate action to ensure its entity remains cyber resilient'.

Three areas for improvement

APRA states that the insights gained from two pilot initiatives - a technology resilience data collection and an independent assessment of a pilot set of entities' compliance with Prudential Standard CPS 234 Information Security - have served to 'reinforce APRA's view that boards need to strengthen their ability to oversee cyber resilience' and 'play a more active role in' the following three areas.

1. Reviewing and challenging cyber information

APRA states that the CPS 234 assessment and other supervisory activities have identified two key issues of concern:

- 'little evidence of boards actively reviewing and challenging the information that senior management has provided on cyber topics'
- 'that management reporting on information security to the board is not fit-for-purpose and unlikely to facilitate meaningful discussion'.

APRA makes clear that boards are expected to 'regularly seek assurance from and as appropriate, challenge management the effectiveness of the information security controls'. APRA points boards towards Prudential Practice Guide CPG234 for guidance on its expectations around this, and also suggests a number of questions that may assist boards in this context. These include:

- 'What are the information security vulnerabilities and threats faced by our entity?'
- 'Is our entity's current information security capability sufficient?'
- 'What is the overall health of the entity's information assets and the information security control environment?'
- 'How much of the information security control environment is regularly tested?'
- 'What are the most severe but plausible security compromise scenarios that management considers the entity cannot currently withstand?'

2. Resilience: Ensuring organisations are in position to recover from cyber attacks

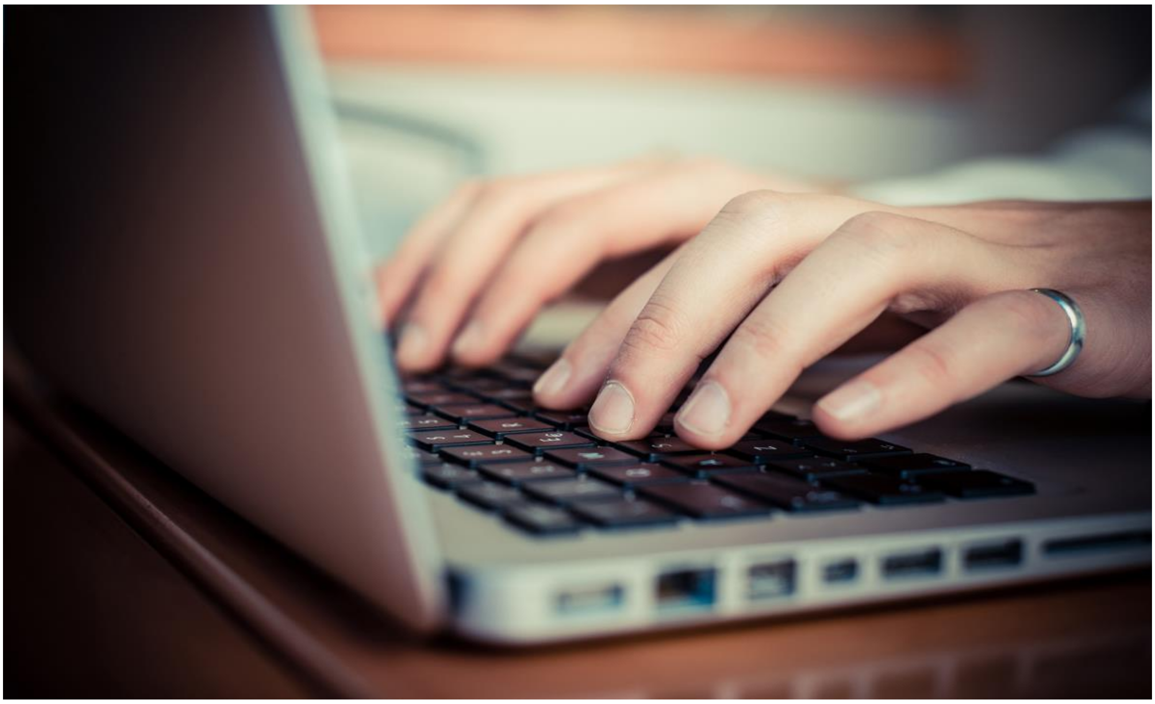
APRA is concerned that some entities may not be in a position to recover critical data in the event of a ransomware attack or other 'high-impact cyber compromise'. For example, APRA states that the pilot data collection identified that:

- 'more than one third' of respondents had not tested their backups for critical systems in the past 12 months; and
- 22% of entities had not tested their cyber incident response plans in the past 12 months.

APRA calls on boards to 'regularly seek assurance in this area by communicating with management'. APRA suggests that the following questions may assist in this:

- 'What backup and recovery testing has been conducted for critical information assets, and is the testing coverage sufficient?'
- 'What plausible disruption scenarios have been considered and tested to ensure the backup and recovery capability is effective – including recovery from a successful ransomware attack where protection of backups is key?'

3. Ensuring the effectiveness of information security controls across the supply chain



APRA states that the results of its CPS 234 assessment and supervisory reviews demonstrate that entities are 'not applying sufficient rigour in testing the design and operating effectiveness of their service providers' information security controls'. Among other things, APRA flags some entities' heavy reliance on self-assessments or surveys completed by their service providers (in the absence of independent verification of their effectiveness) as an area of concern. APRA considers that this is of particular relevance in light of the fact that cyber-attacks frequently target suppliers in order to identify a 'weak link'.

APRA called on boards 'to play a more active role in challenging management's assumptions' around the effectiveness of security controls. APRA suggests that the following questions could assist in this context:

- 'What controls are in place to protect our business and minimise customer impact when the information security of one (or more) of our suppliers is compromised?'
- 'What blind spots do we have on the end-to-end supply chain of our business which could challenge our resilience to a cyber-attack?'

Next steps

APRA's pilot CPS 234 assessment involved a small sample of banking, insurance and superannuation entities undergoing an independent assessment against CPS 234 requirements. APRA plans to continue to roll out the CPS 234 independent assessment to remaining APRA-regulated entities 'over the next couple of years' and to 'share relevant insights' with industry.

[Source: APRA media release 23/11/2021]

Diversity

Diversity is on the agenda of most US boards, but less than half of companies are setting DEI targets

Key Takeouts

- The report highlights that Diversity, Equity and Inclusion (DE&I) has been a priority for 60% of boards for a number of years and is now a topic of discussion for the vast majority of organisations (92%)
- This is reflected in the increasing sophistication of the methods being employed to monitor progress, in the increased internal communication and public disclosure on the issue, and is beginning to be reflected in executive pay.
- However, the survey found that less than half (46%) of organisations have yet to set DE&I goals.

A director survey (respondents were Women Corporate Director (WCD) members at US-based organisations) conducted in July 2021 has identified that boards are increasingly tracking progress on Diversity Equity and Inclusion (DE&I), are stepping their communication and increasingly are holding leaders to account for progress on the issue.

Key Takeaways

- **A long-term area of focus:** 92% of boards are having DE&I discussions. In 60% of cases, this is not a new development but something they have been 'doing for years'. The report points to this as evidence that board discussions are 'not a knee-jerk reaction to the events of the past 18 months, but rather than important trend that follows a culmination of decades long societal pressures'.
- **Organisations are expanding the metrics they use to track DE&I**:
  - The most commonly used measures to track progress on DE&I were: reporting on management diversity and leadership diversity (98%), reporting on overall workforce diversity (92%), workforce engagement scores (84%) and turnover rates (76%).
  - The report also identified that organisations are beginning to expand the range of metrics used. For example 75% of directors indicated they track new hire diversity, and 56% indicated they track diversity in leadership promotions. Fewer respondents indicated that they track diversity in promotions more broadly (44%).
  - Inclusion initiatives and potential bias were ranked the least commonly tracked data.
- **Less than half of organisations have DE&I goals:** According to the report, of the organisation that track DE&I metrics, only 46% set goals. The report suggests that this may be partly attributable to 'to the difficulty in setting quantitative goals to track against'. The report also highlights the collection of consistent and accurate DE&I data as a challenge. Also, despite the focus on DE&I issues generally, the report highlights addressing the gender pay gap and pay equity as a 'missed opportunity'. Only 54% assessed pay equity and only 40% have examined pay gap.
- **Increased disclosure:** The report observes that as measurement and tracking of DE&I has increased, and potentially in response to external stakeholder pressures, there has also been an increase in both public disclosure and internal communication on the issue. According to the report:
  - 65% of directors cited targeted internal communication to employees as their company's primary communication method on DE&I.
  - In terms of external disclosure/communication, ESG and sustainability reports have become the most frequently used method of communicating progress with 58% of directors indicating that their company includes DE&I within their ESG scorecard (and a further 28.8% indicating that their company intends to include it in future) and 56% indicating it is included in their company's sustainability report (with a further 16.7% indicating that it will be included in future).
  - Going forward, the survey found that companies expect to expand the channels through which they communicate about DE&I. For example: 19.2% of directors indicated that they expect their company's annual letter to shareholders to include DE&I in future (for context 32.9% of directors indicated that their company's annual letter to shareholders currently includes DE&i).
- **DEI is increasingly being included in executive incentive plans:**

- According to the report, 39% of organisations currently include DE&I in their executive annual incentive plan and 41% indicate that they are likely/very likely to do so in future. As such, the report suggests that the practice of 'how and where to account for DE&I in executive incentive plans is still emerging'.
- The report identifies the 'strategic importance' of DE&I as the top reason given by respondents for including DE&I in incentive plans
- The top reason given for not including DEI metrics, nominated by 36.7% of respondents, was that DE&I is 'a baseline expectation for executives and does not need to be further reinforced'. 23.3% were reluctant to reduce the value of financial metrics in order to include DE&I metrics.

[Sources: WEB Peal Meyer media release 16/11/2021; Full Text WCB Peal Meyer report: Directors prepare for more: tracking, reporting and incentivising DE&I]

In Brief | According to Bloomberg the percentage of ASX200 directorships held by women increased to 34.1% in October 2021 from 34% in the previous month. Bloomberg attributes this increase to the departure of male directors

[Source: Bloomberg 17/11/2021]

In Brief | Pandemic pause on diversity at an end? A global report analysing the background/experience of newly appointed CEOs at the1095 largest listed public companies across 24 markets has identified that the share of women appointed to CEO roles jumped to 13% in H1 2021 (up from just 6% in H2 2020). Likewise the proportion of CEOs with C-suite experience beyond CFO and COO roles (ie with experience in roles such as Chief Risk Officer, Chief Technology Officer, Chief Strategy Officer) increased

[Source: Full text report: Route to the Top 2021]

Meetings and Proxy Advisers

Committee paves the way for the passage of the Corporations Amendment (Meetings and Documents) Bill 2021

Context

- Temporary relief (details here) 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 – is now before parliament. Importantly, the proposed changes are not identical to the temporary measures now in place. It's planned that the permanent changes introduced by the Bill will take effect immediately after temporary relief measures expire. You can find an overview of the proposed measures in the Bill, and discussion of how they differ from those currently in place, here.

Senate Committee recommends the Bill be passed

The Senate Standing Committee on Economics has paved the way for the passage of the Corporations Amendment (Meetings and Documents) Bill 2021 (Bill) recommending that it be passed.

According to the Committee's report, the majority of submissions were supportive of the Bill, generally agreeing that the changes would 'benefit the sector and allow greater flexibility and efficiency in managing the flow of documents and the undertaking of meetings while delivering savings through the greater use of electronic communications'.

Having said this, the report acknowledges that though many submissions 'advocated their support for making the amendments permanent', a number also raised concerns about specific elements of the Bill or suggested amendments/improvements to it. The main concern raised was in relation to virtual-only meetings, and more particularly the ability of stakeholders to engage effectively with boards of companies.

In response to this concern, the Report states:

> 'The committee is cognisant of these concerns and notes that companies will continue to have face-to-face meetings or hybrid meetings (a combination of face-to-face and virtual) unless the constitution of the company provides otherwise. Hence, members (and peak organisations representing them) would be able to engage in a debate regarding whether the constitution should be amended to provide for solely virtual meetings. Accordingly, the shareholders of a particular company will be able to determine the meeting arrangements appropriate for that company subject to the safeguard discussed below. The committee notes that the bill stipulates that for any virtual meeting the technology must be reasonable and allow members, as a whole, to exercise their rights to ask questions and make comments either in writing or orally. This is an important safeguard to ensure that shareholders as a whole have an opportunity to participate in a solely virtual meeting'.

Accordingly, the Committee recommended that the Bill be passed without amendment.

Dissenting views

- In light of the concerns raised by stakeholders around virtual meetings and the ability of shareholders to participate, Labor Senators recommended that 'an independent review of the Bill be conducted within two years of its implementation date, with particular attention paid to the ability of shareholders to participate in meetings and hold directors to account'.
- Greens Senators recommended that provisions in the Bill allowing for entities to conduct wholly virtual AGMs 'be opposed' in light of the concerns raised in submissions. They consider that:

  > 'Allowing hybrid AGMs should be the limit of current reform in respect of company meetings. This will provide an opportunity for all of the issues associated with virtual meetings to be sorted out and for there to be real-world confirmation of the purported benefits. But until then, wholly virtual AGMs should not be allowed, and shareholders should retain the opportunity to sit in the same room as the executive and the board to bear witness to exactly what they are up to'.

The Bill is currently before the House of Representatives.

[Source: Corporations Amendment (Meetings and Documents) Bill 2021 [Provisions] Report]

SEC mandates use of universal proxy cards

- The US Securities and Exchange Commission (SEC) has voted (Commissioner Hester M Pierce dissenting) to adopt final rules requiring parties in a contested election - usually the parties are company management and an activist investor - to use universal proxy cards listing all director nominees standing for election at the meeting (as opposed to listing only each parties' preferred candidates).
- SEC states that the change will give shareholders the ability to vote by proxy for their preferred combination of board candidates, as they would be able to do if they attended the meeting in person/virtually. SEC Chair Gary Gensler explained the rationale for the change as follows.

  'These amendments address concerns that shareholders voting by proxy cannot vote for a mix of dissident and registrant nominees in an election contest, as they could if voted in person…Today's amendments will put these candidates on the same ballot. They will put investors voting in person and by proxy on equal footing. This is an important aspect of shareholder democracy.'
- The rules will apply to all non-exempt solicitations for contested elections other than those involving registered investment companies and business development companies.
- Compliance with the rule will be required for any shareholder meeting involving contested director election held after 31 August 2022.

Not universally supported within SEC

- SEC Commissioner Hester M Pierce issued a statement explaining her reasons for voting against the rule change. In it, Commissioner Pierce makes clear that she is not opposed in principle, stating:

  'Shareholders voting by proxy should be able to split their vote among company and dissident nominees. Allowing shareholders a straightforward way of choosing a mixed slate through a universal proxy card can facilitate sensible changes to board composition. Universal proxy makes sense for both operating companies and investment companies.'
- Her concern is instead around the potential for the rule, as drafted, to 'facilitate changes to the company that advance special interests rather than enhancing corporate value by serving as a tool for frivolous, as well as serious, activists' because of what Commissioner Pierce considers to be the unacceptably low bar for accessing a company's proxy card.

ISS and CII have welcomed the reform

- The Council of Institutional Investors (CII), which has advocated for the adoption of universal proxy cards, has welcomed it. CII states:

  'Imagine if, in a political election, you could vote only for Democrats or only for Republicans. That has been the dilemma facing most investors voting in a proxy contest at US companies. To have real choice in a contested election, shareholders generally have had to vote in person at the annual shareholder meeting. But that is costly and time-consuming for many institutional and retail investors. By mandating universal proxies in contests for board seats, the SEC is simply giving investors who vote by proxy the same choice they would get if they voted in person'.
- Institutional Shareholder Services (ISS) has also welcomed the change, stating that it 'represents a significant milestone in efforts by institutional investors and others who champion shareholder rights to ensure corporate elections are fair, transparent, and efficient'.

  [Source: SEC media release 17/11/2021; Commissioner Caroline A Crenshaw: Statement on Universal Proxy 17/11/2021; Commissioner Elad L Roisman: Statement on Universal Proxy 17/11/2021; Commissioner Allison Herren Lee: Statement on Universal Proxy 17/11/2021; Council of Institutional Investors media release 17/11/2021; Commissioner Hester M Pierce Dissenting Statement on Universal Proxy 17/11/2021; ISS media release 17/11/2021]

SEC consults on the proposed repeal of 2020 proxy adviser rule-changes

- The US Securities and Exchange Commission is conducting a 30 consultation on proposals to rescind certain changes to proxy rules adopted in 2020, including requirements for proxy advisers to:
  – provide their voting advice to the companies that are the subject of the advice in a 'timely manner; and

– ensure their clients' are provided with a means of becoming aware' of any written responses by companies to proxy voting advice.

- Announcing the consultation, SEC states that 'investors and others have expressed concerns that these conditions will impose increased compliance costs on proxy voting advice businesses and impair the independence and timeliness of their proxy voting advice'.
- SEC also proposes to rescind the changes made to the proxy rules' liability provision after investors (and others) 'expressed concerns that the 2020 changes have created confusion, increased proxy voting advice businesses' litigation risks, and potentially impair the independence and quality of the proxy voting advice'.
- Though these requirements were adopted in 2020, they have yet to come into effect.

Not all SEC Commissioners are supportive of the proposed changes.

Both Commissioner Elad L Roisman and Commissioner Hester M Pierce (both of whom were appointed under the previous Administration) dissented.

- Pointing to the extensive consultation/development process behind the 2020 rules, Commissioner Roisman argues that the decision to reopen consultation sets 'a poor precedent'.

  'In sum, I cannot support this proposal and remain firm in my belief that the Final Rules should be allowed to take effect. They still offer the important investor protections the Commission aimed to achieve when they were adopted, and they would level the playing field for proxy advisory firms to compete in a transparent and improved manner. Moreover, I urge the Commission to rethink this rulemaking process. Whereas the Final Rules were developed based on years' worth of information and deliberation, and support for their requirements was clearly delineated in a transparent administrative process, this proposal's rationale is not so well-supported and the process through which it was developed raises questions about its thoroughness. Offering such little transparency into our process or reasoning for considering dramatic changes to recently adopted rules can lead people to worry about the efficacy and longevity of our rulemakings. This is poor precedent for our Commission to overturn thoughtfully developed regulation so lightly. Thus, I respectfully dissent'.

- Similarly, Commissioner Pierce questioned the rationale for reopening the consultation.

  'I cannot support today's proposal. The Commission lacks a sound basis for seeking to amend a brand new rule. Nothing has changed since we adopted the rule, and we have not learned anything new. The release takes a stab at justifying the rewrite, but we might as well simply acknowledge that the political winds have shifted.'

CII and ISS have each welcomed the consultation

- The Council for Institutional Investors (CII) has expressed 'general' support for the SEC's proposed changes and reiterated its opposition to the 2020 rule-changes. CII states:

  'CII had opposed these aspects of the rules when they were adopted criticizing them for possibly causing significant delays in the already constricted proxy voting process, increasing the costs of the advice to investors, and jeopardizing the independence of proxy advice. CII believes that it is critical that any final rule resulting from the proposed amendments promotes, rather than hinders, the availability of timely, high-quality, cost-effective, and independent advice and analysis of issues subject to shareholder votes.'

- Similarly, Institutional Shareholder Services (ISS) has welcomed the consultation. ISS also called for the proposed amendments to go further. ISS states:

  'While a significant step in the right direction for those who champion shareholder rights, we do believe the scope of the amendments should have gone further and look forward to engaging with the Commission on ensuring the provision of proxy advice remains independent and unfettered.'

  [Source: SEC media release 17/11/2021; SEC Fact Sheet; Proposed Rule; Commissioner Elad L Roisman: Too Important to Regulate? Rolling Back Investor Protections on Proxy Voting Advice 17/11/2021; Commissioner Hester M Pierce: Dissenting Statement on Proxy Advice Proposal 17/11/2021; CII media release; ISS media release 18/11/2021]

Markets and Exchanges

Investigation into ASX November 2020 outage: No breach of ASX licence conditions found, ASIC imposes additional licence conditions on ASX

The Australian Securities and Investments Commission (ASIC) has concluded its investigation into the November 2020 market outage at the ASX.

Broadly, though ASIC's investigation identified 'serious deficiencies in ASX's and market participants' ability to limit the impact' of the outage, it did not conclude that ASX breached its licence conditions.

Rather the review (the findings of which are included in: REP 708 ASIC's expectations for industry in responding to a market outage) found that:

> 'ASX broadly adhered to its procedures for incident management, including its communications protocol, during the 2020 market outage.'

However, in light of the 'minimal level of liquidity and trading' that was able to continue, ASIC considers that 'further work is required' to enable sustained trading to continue on alternate trading venues in the event of a market outage. Accordingly, ASIC has imposed additional licence conditions on ASX.

Additional licence conditions imposed

- ASIC has imposed additional licence conditions on three licences held within the ASX Group: Australian market licence of ASX Ltd; Australian CS facility licence of ASX Clear Pty Ltd; and Australian CS facility licence of ASX Settlement Pty Ltd.
- ASIC states that the licence conditions are 'directed at mitigating risks for future upgrades, with specific emphasis on the oversight of the CHESS Replacement Program, due to go live in April 2023'. ASIC Chair Joe Longo said that the new conditions will 'confirm that remedial actions are implemented appropriately and efficiently to address these operational issues - including for the critical rollout of the CHESS Replacement Program'.

Details

- ASIC states that the additional licence conditions imposed on ASX's Australian market licence require:
  - remediation of underlying issues with ASX operations that led to the November 2020 market outage
  - assignment of accountability to the ASX board and senior executives for the implementation of the remedial actions
  - attestations on behalf of the ASX board that adequate controls, procedures, skills, and resources are in place.
- ASIC states that the additional conditions imposed on the licences of ASX Clear Pty Ltd and ASX Settlement Pty Ltd require an independent ASIC-approved expert to be appointed to assess and provide regular reports to ASIC on whether ASX's assurance program for the replacement of CHESS is fit for purpose.
- ASIC states that the ASX did not oppose the imposition of the additional licence conditions.

Success of the remediation actions tied to executive pay

In addition to the conditions outlined above, ASIC states that the ASX board will

> 'provide attestations specifying individual executive accountability, with clear links to remuneration consequences. The relevant executives' interests will be appropriately aligned with the success of any remedial actions, avoidance of any further outage and with any failure to comply with their accountability obligations'.

ASIC's expectations of market operators and participants going forward

- As flagged above, the findings of ASIC's review into the outage and the 16 other 'operational incidents' that impacted the operation of the ASX equity market in the week of 16 November 2020 are outlined in: REP 708 ASIC's expectations for industry in responding to a market outage. ASIC comments that the findings are 'particularly disappointing in circumstances where some of these deficiencies had previously been raised by ASIC in Report 509 Review of the ASX equity market outage on 19 September 2016'.

- In addition, REP 708 sets out ASIC's expectations for market operators and participants to address the concerns identified with the aim of supporting the 'resilience' of the market going forward.
- ASIC has provided separate summaries of the issues identified and ASIC's expectations of market operators, participants and institutional investors at p5-7 of the report.

Next steps

- ASIC plans to send letters to 'a number of market operators and participants requesting them to develop a response' to the expectations outlined in the report. ASIC will monitor progress towards implementation of its expectations in 2022.
- ASIC comments that some expectations will require ASX (and other market operators where appropriate) to consult with stakeholders and seek feedback from a broad range of market users before implementing changes. ASIC's expectation is that these consultations occur in 2022. ASIC also called for operators to engage on proposals for 'additional mechanisms'. ASIC states:

  > 'Industry is encouraged to consider if there are additional mechanisms (such as a re-opening auction to aggregate liquidity, incentives for liquidity providers or additional volatility controls) that may support liquidity and price formation on alternative trading venues during market outages, and engage with ASIC once proposals are well formed'.

- ASIC previously consulted on new market integrity rules (Consultation Paper 314 Market integrity rules for technological and operational resilience (CP 314)). The regulator expects that these new rules will be made 'early in 2022'. ASIC states that 'these market integrity rules implement our expectations for market operators and market participants to ensure the resilience of critical business services, including change management, outsourcing, risk management, incident management, business continuity planning, governance and resourcing'

ASX response

ASX Managing Director and CEO Dominic Stevens said that ASX is 'pleased that ASIC's investigation into the market outage is closed and that no breach of ASX's licence conditions was found' and that ASX will 'continue to invest to strengthen the quality of our infrastructure and reduce operational risk.'

ASX has indicated that:

- work to address the recommendations has commenced and is expected to be completed 'over the next 12 to 18 months'. Mr Stevens described the additional licence conditions as 'practical' and 'aligned with the action ASX is taking to improve the way we operate our business'.
- it is 'considering' report 708 outlining ASIC's expectations for industry in responding to a market outage and will 'engage with ASIC and market users on our response to these expectations'.

[Sources: ASIC media release 24/11/2021; ASIC Report 708: ASIC's expectations for industry in responding to a market outage; ASX media release 24/11/2021]

Regulators

Top Story | ASIC clarifies its stance on EUs

ASIC has released updated guidance on its approach to enforcement

On 22 November 2021, the Australian Securities and Investments Commission (ASIC) released updated regulatory guidance on its enforcement approach generally - Information Sheet 151 ASIC's approach to Enforcement (INFO 151) – and its use of court enforceable undertakings (EUs) - Regulatory Guide 100 Court Enforceable Undertakings (RG 100). The changes were not announced via media release.

In a speech, ASIC Chair Joe Longo said that ASIC's updated guidance clarifies the regulator's stance on the use of court enforceable undertakings (EUs). Mr Longo stated that the guidance:

> 'highlights that court-enforceable undertakings are a flexible enforcement tool that will be used to improve compliance with the law. They are one of the options that allow us to take targeted, proportionate action. We will only use court enforceable undertakings where it is in the public interest. Offenders should be held accountable for their poor conduct, and publicly acknowledge that accountability, regardless of which enforcement tool we use against them'.

The focus on use of the full range of regulatory tools available, and the focus on targeted and proportionate action, is consistent with Mr Longo's previous comments on ASIC's enforcement approach more generally, with the narrative in the regulator's latest Corporate Plan, and with ASIC's recently released 'Statement of Intent' published in response to the government's Statement of Expectations for the regulator.

Use of enforceable undertakings: Revisions to RG 100

RG 100.12-18 sets out ASIC's approach to accepting an EU. RG 100 states that:

- ASIC will only consider accepting and EU 'when we consider it will achieve an effective and appropriate regulatory outcome that is in the public interest'.
- ASIC 'will generally only consider accepting a court enforceable undertaking after we have weighed up the effectiveness of the regulatory outcome offered by the undertaking compared to outcomes offered by other available enforcement remedies'.

The Revised RG 100 makes clear that ASIC will not 'usually accept' an EU from a party: 'instead of referring a brief of evidence to the Commonwealth Director of Public Prosecutions (CDPP) for potential criminal prosecution; where the misconduct is deliberate or involves a high level of recklessness; after a matter has been referred to an ASIC delegate or other specialist body; or as an alternative form of relief if conditional relief has not been complied with'.

RG 100 also makes clear that 'when ASIC accepts a court enforceable undertaking in final resolution of a matter, we will generally require that it contains admissions that the promisor contravened specific legislative provisions'. Further, ASIC will 'generally' not accept EUs that do not include details of the conduct that gave rise to the undertaking.

Importantly, a key concern around ASIC's use of EUs made by the Hayne Commission, was the lack of acknowledgement of wrongdoing. Commissioner Hayne stated that:

> 'When an entity fails to acknowledge that it has done wrong the risk is that it considers the promises made in the EU as no more than the cost of doing business or the cost of placating the regulator'

ASIC's enforcement stance post-Hayne

In response to Hayne Recommendation 6.2, ASIC adopted a 'why not litigate?' approach to enforcement which entailed a shift away from 'negotiated outcomes'.

This shift is reflected in ASIC's reported enforcement outcomes post-Hayne. For example, ASIC's enforcement update for the January to June 2018 period (REP 585), reports that ASIC agreed to 12 court enforceable undertakings, decreasing slightly to nine for the July to December 2018 period (REP 615).

A review of all subsequent enforcement reports up to the latest report covering the January to June 2021 period (REP 699) shows an apparent move away from the use of EUs – for the whole of 2019, ASIC reports that there were no EUs (REP 625, REP 660), for the July to December 2020 period (REP 688), there were two EUs reported and for the January to June 2021 period there was only one (REP 699).

The shift is further confirmed by a table prepared by ASIC setting out the results of ASIC's enforcement activity over the period 1 July 2011 to 30 April 2021. According to ASIC's table, in the 2018-19 financial year, ASIC completed 25 civil proceedings, and secured 10 EUs. In 2020-21, the number of civil proceedings completed had spiked to 43 while the number of EUs had decreased to just two.

A recalibration of ASIC's approach

The release of ASIC's updated enforcement guidance, consistent with the shift away the term 'why not litigate?' to describe its enforcement approach, and consistent with the government's revised expectations of the regulator is arguably further confirmation of a recalibration in ASIC's enforcement stance under ASIC Chair Joe Longo. More particularly, it underlines ASIC's renewed focus in ASIC Chair Joe Longo's words on use of the full suite of tools available to regulate 'in a way that both supports legitimate business activity *and* allows for the independent discharge of our key regulatory and enforcement responsibilities'.

[Source: Information Sheet 151 ASIC's approach to Enforcement (INFO 151) Regulatory Guide 100 Court Enforceable Undertakings (RG 100)]

In Brief | SEC enforcement update: SEC reports an 3% decrease overall in enforcement actions filed in fiscal year 2020, but a 7% jump in the number of new enforcement actions including against emerging threats in the crypto and SPAC spaces. SEC Chair Gary Gensler said that the results show that SEC is 'the cop on the beat for America’s securities laws…As these results show, we go after misconduct wherever we find it in the financial system, holding individuals and companies accountable, without fear or favour, across the $100-plus trillion capital markets we oversee'

[Source: SEC Media release 18/11/2021]

Financial Services

Responsible lending: New regulations made to further extend the 'small business exemption'

Key Takeouts

- New regulations are now in force that retrospectively reinstate the small business exemption – ie temporary measures exempting Australian credit licensees from certain responsible lending obligations where the lending is partly for a small business purpose – which was first introduced in April 2020 and subsequently extended to 3 October 2021, to facilitate the flow of credit to small business.
- The Regulations apply retrospectively from 3 October 2021 and will remain in force until the relevant parts of the National Consumer Credit Protection Amendment (Supporting Economic Recovery) Bill 2020 commence or if this does not occur, for a period of three years.

The temporary small business exemption

In April 2020, the National Consumer Credit Protection Amendment (Coronavirus Economic Response Package) Regulations 2020 (summarised) came into force. The Regulations temporarily exempted Australian credit licensees from certain responsible lending obligations in order to facilitate the flow of credit to small businesses (the small business exemption). The measures were introduced in response to the COVID-19 pandemic as a temporary measure but were subsequently extended and ceased to apply on 3 October 2021.

Broader planned reform of responsible lending obligations

- On 9 December 2020 the National Consumer Credit Protection Amendment (Supporting Economic Recovery) Bill 2020 (the Bill) was introduced into the House of Representatives. The Bill is currently before the Senate, the Senate Committee having recommended that the Bill be passed without amendment (read more about the Bill here)
- Relevantly, Schedule 1 of the Bill proposes to permanently remove existing responsible lending obligations relating to the unsuitability of credit contracts, except in relation to small amount credit contracts (SACCs), SACC-equivalent loans by authorised deposit-taking institutions (ADIs), and consumer leases.
- On 19 March 2021, the Treasurer announced that the small business exemption would be extended until the Bill is passed.

Further extension of the small business exemption

- The National Consumer Credit Protection Amendment (Small Business Exemption No. 2) Regulations 2021 (the Regulations) – are now in force. The Regulations apply retrospectively from 3 October 2021 to align with the repeal date of the previous Regulations of 3 October 2021.
- In line with the Treasurer's 19 March statement, the purpose of the Regulations is to ensure that the small business exemption continues to apply until the relevant parts of the Bill commence or if this does not occur, for a period of three years.

[Sources: National Consumer Credit Protection Amendment (Small Business Exemption No. 2) Regulations 2021]

Hayne implementation: Senator Hume rejects criticism that the proposed CSLR is too narrow in scope

Context

- Following consultation, on 28 October 2021, the government introduced three Bills that if legislated will establish a CSLR and the industry funding framework to support it, in line with the government's response to Hayne recommendation 7.1.
- Broadly Schedule 3 of the Financial Sector Reform (Hayne Royal Commission Response No. 3) Bill proposes to amend the Corporations Act 2001 (Cth) and other Commonwealth Acts to establish a CSLR. The Bill sets out the proposed scope, operation, administration and oversight of the scheme.

- The Financial Services Compensation Scheme of Last Resort Levy Bill 2021 and the Financial Services Compensation Scheme of Last Resort Levy (Collection) Bill 2021 propose to implement the industry levy framework to fund the scheme.
- If legislated, the proposed CSLR would fund unpaid 'relevant' determinations made by AFCA that have been made since 1 November 2018 (the date of the commencement of the AFCA scheme) where the determination is in relation to a financial product or service within the scope of the scheme and where the application meets certain eligibility requirements. You can find a brief overview of the proposed scheme in Governance News 3/11/2021 at p25

Well-targeted: Senator Jane Hume has defended the proposed scope of the CSLR

In her address to the AFR Super and Wealth Summit, Minister Financial Services, Superannuation and the Digital Economy Jane Hume spoke about recent developments and planned reforms in the superannuation sector, the proposed Compensation Scheme of Last Resort (CSLR) and touched briefly on the 'incredible opportunities' that de-centralised finance underpinned by blockchain technology presents.

On the proposed CSLR, Ms Hume said that the scope of the proposed scheme, which will not cover managed investment scheme (MIS) or 'other high risk financial products', is appropriate in light of the fact that it is 'not an insurance scheme designed to pay compensation to any consumer who has lost money on an investment' but rather intended to 'cover unpaid compensation awarded because of misconduct relating to a targeted range of financial products and services'.

With respect to the exclusion of MIS from the scheme, Ms Hume said that: a) banks will be required to contribute to the establishment of the CSLR so they are not 'off the hook'; and b) there are to her knowledge no examples of banks that have failed to pay an AFCA determination.

With respect to the exclusion of 'other high risk financial products' Ms Hume said that the exclusion is warranted because the government considers that losses resulting from the choice to 'punt' on 'speculative' investments should be borne by the individual (not by the proposed CSLR). Ms Hume said:

> 'Now, if you want to punt a portion of your savings on something speculative - knock yourself out. No government should stand in your way. But you should be prepared to wear it when it goes wrong. And no government should pick up the tab with taxpayers money nor force industry - and thereby ultimately other savers - to underwrite any and every investment that consumers choose to make'.

Ms Hume labelled calls by Labor to expand the scope of the scheme as 'irresponsible' and 'paternalist'. Ms Hume also observed that:

> 'expanding the CSLR to provide compensation for any and every bad investment would essentially give a Government backed guarantee to every Ponzi scheme - paid for by suppressing the returns of all other Australian investors. It would be a green light to fraudsters and charlatans. Come in spinner'.

Ms Hume also pointed to the UK approach/experience as evidence that a broader based scheme would result in huge costs over time.

[Source: Minister for Financial Services, Superannuation and the Digital Economy Jane Hume media release 22/11/2021]

ASIC has commenced proceedings against the largest registered debt administrator in Australia over alleged use of threats/coercion to induce payment

- The Australian Securities and Investments Commission (ASIC) has commenced civil proceedings in the Federal Court against a registered debt agreement administrator, A&M Group Pty Ltd over alleged 'misleading, threatening and coercive conduct against debtors who had missed payments under their debt agreements' in contravention of ss 12DA and 12DJ of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act).
- A&M Group is the largest registered debt administrator in Australia.
- Broadly, ASIC alleges that A&M Group made 'misleading or deceptive representations' to six debtors during the period 30 January 2018 to 19 February 2020 about the current status of their debt agreements, and the consequences of defaulting under these agreements in order to pressure them into contacting A&M Group/making payments. For example, A&M sent texts/emails to six debtors that:
  - threatened them with fraud charges/imprisonment if they failed to make payments
  - threatened to contact friend/family/work colleagues/landlords if debtors failed to contact A&M group

Annexure A of ASIC's concise statement includes full details of the alleged misrepresentations made by A&M Group.

- ASIC states that it is concerned that the alleged conduct could cause additional harm/place additional stress on consumers already experiencing financial difficulties.
- ASIC is seeking civil penalties and declarations.

[Source: ASIC media release 17/11/2021]

Regional Banking Taskforce commences consultation on the impacts of regional branch closures

On 22 October 2021, the government announced the establishment of a regional banking taskforce to assess the impact of bank branch closures on regional communities.

The Taskforce has released an issues paper seeking feedback on the following 11 questions.

- 'How are Australians changing the ways they are accessing banking services? What are driving these changes?
- What banking facilities, services and products are used in regional bank branches?
- Are there particular banking products or services that need to be delivered face-to-face or have support provided face-to-face? Are any of these particularly important for regional customers?
- What are the impacts of regional bank branch closures on the banking needs of individuals?
- What are the impacts on the banking needs of businesses, community organisations and communities?
- Are there particular issues in the provision of banking services in regional Australia for specific vulnerable groups?
- What more could banks do to help customers transition to alternative banking services that would enable them to do their banking in a timely, efficient and cost-effective way?
- Are there facilities, services and products provided in bank branches that are not available through alternatives like ATMs, Bank@Post, phone banking, mobile banking, the telephone and the internet?
- What are alternatives to bank branch models that would maintain or improve banking services and accessibility in areas where branches have been closed?
- Are there any alternative models for the provision of banking services that could be considered for adoption by banks in Australia?
- What are the lessons from Australian and international experiences that can help improve banking services and accessibility in regional communities where bank branches have been closed?'

The due date for submissions is 18 December 2021.

[Source: Treasury consultation: Regional Banking Taskforce - Issues Paper 18 November 2021 - 18 December 2021]

ASIC Chair Joe Longo's speech to the AFR Super and Wealth Summit focused on: enforcement, superannuation and the challenges of regulating cryptoassets

In his speech to the AFR Super & Wealth Summit, Australian Securities and Investments Commission (ASIC) Chair Joe Longo spoke about the regulators' approach to enforcement, the 'evolving regulatory landscape over superannuation' and reflected on the 'crypto phenomenon'.

Key Takeaways

Enforcement

- Mr Longo said that in the 20 years since he was head of enforcement at ASIC, the regulator's 'strong commitment to targeted, credible corporate law enforcement…has not changed'. Mr Longo described the need for ASIC to 'maintain and enhance a strong reputation in the market and the general community' and 'essential' to ensuring confidence in the financial system.
- Mr Longo said that ASIC 'must regulate in a way that both supports legitimate business activity and allows for the independent discharge of our key regulatory and enforcement responsibilities. These outcomes are not mutually

exclusive. By enforcing the law against those who break the rules, we support those who want to do the right thing'.

- Mr Longo emphasised that 'ASIC is not here to eliminate risk', which is an 'essential part of Australia's financial system and economy'. However, where 'industry has neglected to take its share of responsibility, ASIC will not hesitate to deploy the powers in our regulatory toolkit' – from 'supervisory work through to litigated enforcement matters' - to deter the misconduct, hold individuals/corporations to account and 'drive a culture of better corporate behaviour'.
- Referencing the updated regulatory guidance (Regulatory Guide 100 Court Enforceable Undertakings (RG 100) and Information Sheet 151 ASIC's approach to Enforcement (INFO 151) released on 22 November 2021, Mr Longo said that the updated guidance

  > 'highlights that court-enforceable undertakings are a flexible enforcement tool that will be used to improve compliance with the law. They are one of the options that allow us to take targeted, proportionate action. We will only use court enforceable undertakings where it is in the public interest. Offenders should be held accountable for their poor conduct, and publicly acknowledge that accountability, regardless of which enforcement tool we use against them'.

Superannuation

- Mr Longo said that ASIC is focused on how superannuation trustees 'deal with consumers'. That is, ASIC is focused on questions such as: 'is it fair? Does it meet the needs of members? Does it promote confidence?'
- Mr Longo said that ASIC has observed 'plenty of examples', as illustrated by ASIC's recent enforcement actions, where it considers 'industry has not delivered the outcomes consumers should expect' . Mr Longo said that ASIC will 'continue to act against misconduct of this kind'.
- Mr Longo offered his comments on 'three issues' – performance, distribution and retirement focus - which 'trustees are thinking about currently'.
  - On the issue of performance, Mr Longo said that ASIC is 'focusing on communications made around performance by those trustees who recently failed APRA's performance test. Where we identify misleading or deceptive conduct, we will intervene to achieve corrective disclosure or take enforcement action, if appropriate'
  - On the issue of distribution, Mr Longo said that ASIC is 'proactively surveilling the industry' to monitor whether consumers 'get into products that are suitable for them' and whether the 'plethora' of superannuation products available are 'good and useful'. Mr Longo cautioned that where ASIC finds 'trustees breaching the law and not acting in good faith or where their conduct causes actual harm, enforcement action is likely'.
  - On the question of 'retirement focus' Mr Longo called on trustees to focus on the 'overall retirement needs of their members not just the accumulation of a superannuation balance'.
- Mr Longo issued a 'challenge' for every trustee to consider how their operations compare to an asset manager of similar size.
- Mr Longo called on trustees to ensure, that as they move investment management functions in-house, they have appropriately 'robust risk management, compliance and governance arrangements' in place, that are 'specifically focused on their obligations as market participants'.
- Mr Longo also flagged 'widespread poor conflict management arrangements' as an area of concern for ASIC.
- Touching briefly on reforms that provide for 'stapling of accounts' Mr Longo questioned whether some criticisms of the measure eg that it may mean members are 'stuck with a poor performing fund' are helpful, observing 'surely the real issue there is that the fund is performing so poorly in the first place?'

The rise of the 'crypto-universe'

- Mr Longo commented briefly on the rise of the 'crypto-universe' and on the recommendations in the report recently released by the Senate Select Committee on Australia as a Technology and Financial Centre.
- Mr Longo described the recommendations as a 'very challenging set of policy questions for Parliament to consider'. In illustration, Mr Longo suggested that the regulation of decentralised autonomous organisations (DAOs) presents a 'policy challenge for traditional forms and methods of regulation'.
- Mr Longo commented that from a policy perspective the Committee was 'right to highlight the fact that crypto is on our doorstep here and now and being driven by extraordinary consumer and investor demand'.

- From a regulatory perspective, Mr Longo said that ASIC 'will always enforce the law as it stands, using the many means available' but that 'we need to be careful those laws keep pace with change, and with the community's realistic expectations and demands'. Commenting on the present situation with respect to crypto-assets Mr Longo said:

  > 'The demand-driven nature of the rush into crypto has thrown up some unique challenges. At present many crypto-assets are probably not "financial products", making it difficult for financial advisers to offer counsel. So, what can they do when clients are banging down the door wanting to divert their savings into Ethereum or Dogecoin, a currency originally conceived as a joke? ASIC has already provided some guidance on exchange traded funds linked to crypto-assets – they at least are financial products, and traded on a licensed exchange, so there will be some protections there – but for the most part, for now at least, investors are on their own'.
  >
  > [Source: Speech by ASIC Chair Joe Longo at the AFR Super & Wealth Summit, Responsibility amid change, 22/11/2021]

An opportunity for industry: APRA calls on the superannuation industry to step up its focus on post-retirement planning

In her address to the AFR Super and Wealth Summit, Australian Prudential Regulation Authority (APRA) Deputy Chair Helen Rowell spoke about the need for the superannuation industry to step up its focus on post-retirement planning.

A gap in the market

- Ms Rowell observed that 'Australians might be transitioning into retirement in ever-growing numbers and with increasingly higher balances, but the availability of a wide range of quality products to help them manage and ultimately use their savings, potentially over decades, has failed to keep pace'.
- Referencing the findings of the Retirement Income Review, Ms Rowell said that many people are 'more frugal than needed' during their retirement for fear of outliving their savings, with many people dying with the bulk of their nest egg intact. Ms Rowell said that this is an indication that they 'often lack the necessary guidance or options to help them effectively manage their nest egg'.
- Ms Rowell said that this 'gap in the market' is a space that is 'ripe for good innovation'.
- Ms Rowell emphasised the need for industry to ensure that 'the challenge to innovate is undertaken in a thoughtful and considered way' that avoids 'creating the legacy issues we have seen in the past' in other contexts. Ms Rowell observed:

  > 'We do not want retirement income products to head down the same path as we have seen in relation to individual disability income insurance products, for example, where the product design, terms and conditions and pricing have proved unsustainable, and caused significant losses for insurers that the industry has not been able to adequately address on its own. Nor do we want to see the proliferation of high cost, poorly performing products that we have seen in the choice sector of the superannuation industry, where consumers are bamboozled by having too many (often not very different) products to choose between'.

Changing the community's mindset

Ms Rowell said that the 'biggest challenge' for industry may be 'changing Australia's mindset when it comes to retirement savings – from one where outcomes are judged solely by the size of an account at retirement to one that equally values helping retirees manage that money for the rest of their lives'.

The (proposed) retirement income covenant

- Ms Rowell also touched on the government's 'retirement income covenant' which (if legislated) would require superannuation trustees to develop a retirement income strategy for their members. Ms Rowell said that the development of covenant 'demonstrates growing recognition that trustees must focus on the retirement income needs of members and build the capacity and capability to service those needs'.
- Ms Rowell said that APRA expects that, if introduced, the 'covenant will start to drive the demand for, and development of, new solutions for retiring members'. Again, she suggested that this represents an opportunity for

trustees to 'collaborate with other providers to develop a (simple) suite of options that could be made available to help retirees make sound choices in managing the longevity and other risks they face through retirement'.

- Ms Rowell said that though the covenant is not proposed to come into effect until mid-2022, 'trustees don't have to wait until then to start developing or offering innovative income products to their members', observing that APRA has already observed 'movement among some leading super funds, life insurers and other providers to bring new products to market'. In saying this, Ms Rowell acknowledged that 'plunging into a market that is yet to really take off in Australia also carries risks' and that 'some entities have launched retirement income products over recent years, only to be so underwhelmed by consumer demand that the projects were quickly abandoned'. She observed,

  > 'From this vantage point, simply doing the same thing and hoping for a different outcome, notwithstanding the growing number of retirees and the imminent commencement of the retirement income covenant, doesn't seem the wisest strategy'.

- Ms Rowell said that they key to a different outcome is innovation – 'to somehow both design and offer retirement product options that meet retirees' needs and persuade them that they need them'.
- Ms Rowell identified understanding customer needs as 'the first step' in this process.

APRA will engage with industry

- From a regulatory perspective, Ms Rowell said that APRA is increasing its focus on the provision of 'better retirement income solutions as a key aspect of delivering quality outcomes to retirees'.
- Ms Rowell said that APRA has had feedback from industry that they're 'reluctant to put products on the market until they have a better sense of the direction regulators are heading'. Ms Rowell said that

  > 'APRA is already thinking about potential changes to the regulatory framework that may be required, however it's difficult to make informed judgements about the types of risks that would demand APRA guidance until we see what types of products are coming to market – another chicken and egg-type impasse!'

- In light of this, APRA intends to 'continue to engage with the wealth management industry on these issues'. Ms Rowell said that APRA does not plan to issue extensive or detailed guidance on the covenant in the short term to allow time for industry thinking and approaches to develop. In the meantime, APRA will leverage its improved data collections to support industry through sharing examples of better practice to assist the development of new products,

  [Source: APRA Deputy Chair Helen Rowell, speech to the Australian Financial Review Super and Wealth Summit, Hatching a plan for better post-retirement outcomes, 22/11/2021]

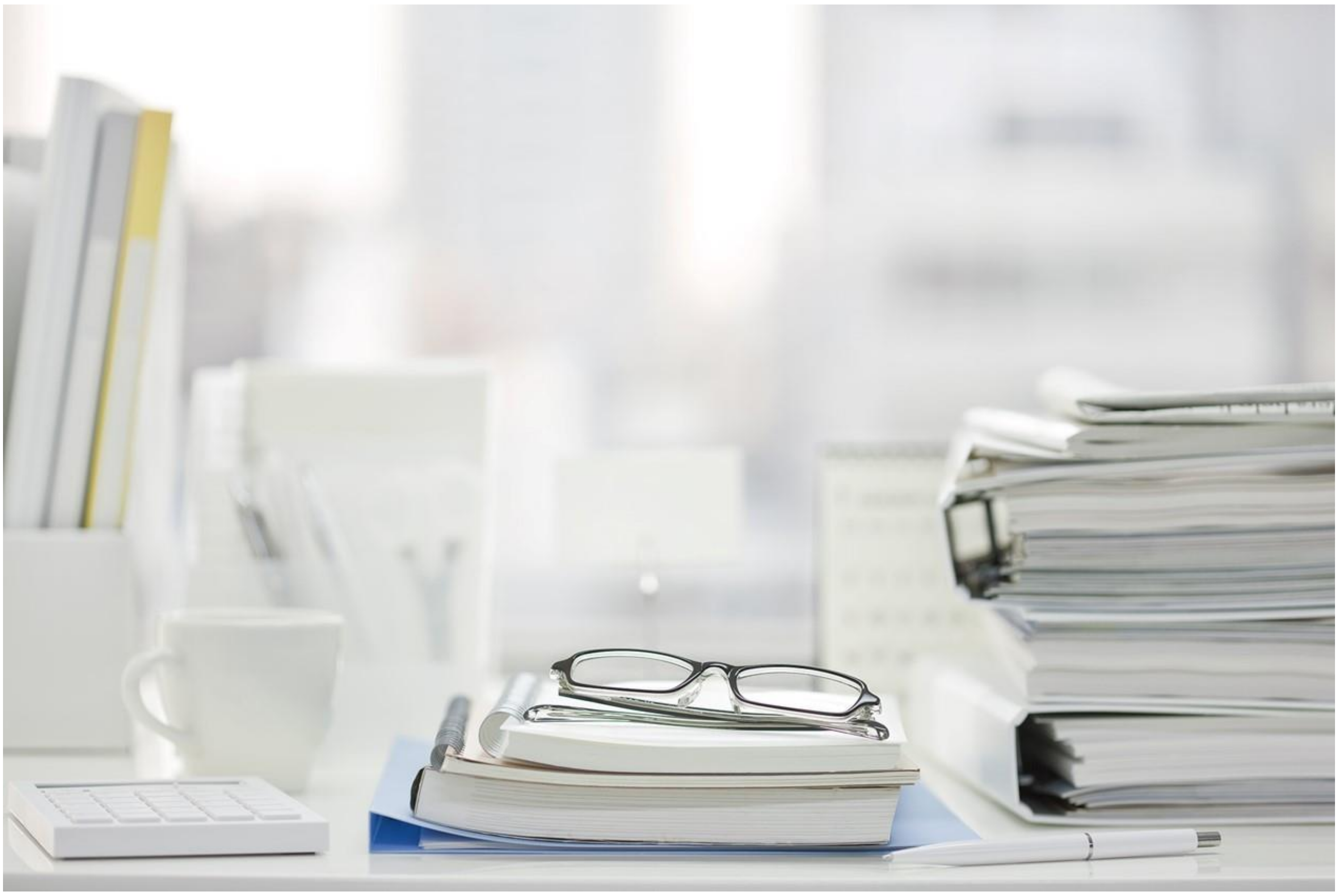
Accounting and Audit

In Brief | The FRC's latest annual audit assessment flags 'deficiencies relating to lack of professional scepticism by auditors, including failures to sufficiently challenge management's assumptions, as well as evidence of the poor application of professional judgement' as ongoing issues. The FRC considers that 'quality across firms was more mixed' than last year, with 'evidence that some firms had successfully implemented improvement measures' since the last review. Of the 147 audits reviewed, 33% required improvement or significant improvement (down from 38% in 2019/20).

[Sources: FRC media release 18/11/2021; Developments in Audit 2021]

Insolvency and Reconstruction

ALRC supportive of a comprehensive review of Australia's insolvency laws



In a speech to the Australian Restructuring and Insolvency Turnaround Association (ARITA), President of the Australian Law Reform Commission (ALRC) Justice Sarah Derrington said that the ALRC is supportive of a 'call to government to conduct a comprehensive review of Australia's insolvency laws to ensure they are "simple, efficient and effective"' in light of the time that has elapsed since the last review and the changes that have occurred during that time.

A potential review of Australia's insolvency laws: room to apply learnings from previous and current reviews

- Justice Derrington said that there is 'a significant opportunity for the ALRC to apply its learnings from the Financial Services Inquiry to a review of insolvency laws to achieve greater simplicity and effectiveness in the law'. In particular, she said that the principles underpinning the approach that the Harmer Report took to its inquiry so many years ago, 'capture the underlying approach of the ALRC to its current Inquiry into financial services and corporations and, remain relevant for a future insolvency inquiry.
- Justice Derrington observed that the 'technical' focus of the ALRC's current review of the Legislative Framework for Corporations and Financial Services Regulation (Chapter 7 Review), with its strong emphasis on improving the mechanics/navigability of the law, rather than on recommending changes to/improvements to the content of obligations imposed under the law, is 'not dissimilar to the type of inquiry being sought by ARITA'.
- Justice Derrington opined that the 'novel analysis' methods used in the Chapter 7 inquiry could be helpful in the context of a future review of insolvency law as well as in the context of future inquiries more generally. For example: she said that coding software developed for use in the Chapter 7 review has identified a number of 'trends' in the length and complexity of the existing legislative regime. This data, she suggested, can now be used to identify

  > 'how insolvency provisions both within the Corporations Act and outside the Act rank in terms of their "complexity". The data can also be used to identify hotspots of complexity within the insolvency provisions. This data can assist the ALRC to identify where simplification is needed'.

- Justice Derrington also emphasised the importance of consultation in the context of the ALRC's work and underlined that this would be an important part of any future review of insolvency laws. She stated:

  > 'Like the process followed this year, the ALRC would hold public webinars, arrange targeted consultations, and attend industry and professional events all around the country to elicit as many views as possible to aid its reform process'.

Early insights from the Chapter 7 Review

Ahead of the release of the first Interim Report on 30 November 2021, Justice Derrington said that the review has identified six 'general problems with the law' that together have led stakeholders to 'generally feel that the law is "too complex" and in need of simplification'.

These 'problems' are:1) 'incomplete understanding of legislative complexity'; 2) 'complex use of definitions'; 3) difficulties navigating definitions'; 4) 'overly prescriptive legislation'; 'obscured policy goals and norms of conduct'; and 6) 'difficulties administering complex legislation'.

Justice Derrington observed that a 'general finding' of the data undertaken as part of the Chapter 7 review is that corporate law is

> 'regularly modified, amended and applied, and this contributes to the overall complexity of the system. There is also a large mass of "secret" law, contained in legislative instruments made by bodies like ASIC, which unsophisticated users of the legislation struggle to find. This makes finding the law and applying it particularly burdensome for unsophisticated or less well-resourced users'.

Again, she suggested that these findings have broader relevance to the way in which laws, including insolvency laws, are drafted/operate.

The ALRC acknowledges ARITA's concerns

Justice Derrington said that ARITA has already provided feedback to the Chapter 7 Review which 'identify instances of definitional uncertainty and legislative complexity in the existing insolvency regulatory scheme, the supporting Regulations, and the Insolvency Practice Rules'. Justice Derrington highlighted that:

> 'in particular, the ALRC is on notice that ARITA considers that: there is inconsistency between the terminology used in the Act and ancillary legislation; and the Corporations Act is structured in a problematic way'.

She said that 'The ALRC supports these key points and hopes that the Interim Report addresses some of ARITA's concerns in this regard'.

Next steps

Justice Derrington said that the ALRC 'supports' ARITA's concerns that: a) 'there is inconsistency between the terminology used in the Act and ancillary legislation'; and b) that the 'Corporations Act is 'structured in a problematic way'. She expressed the hope that the ALRC's first interim report as part of its review of the Legislative Framework for Corporations and Financial Services Regulation (Chapter 7 Review) would address some of ARITA's concerns in this regard.

Justice Derrington said that the ALRC's first interim report would call for stakeholder submissions on the proposals for reform relating to definitions, concepts and standards in financial services legislation. Feedback received would be used by the ALRC to develop its recommendations.

> [Sources: Speech by the Hon Justice S C Derrington, The changing face of law reform in Australia: Commentary on the ALRC's inquiry into insolvency, its contribution to the current legal framework and the need for a review given the passage of over 30 years, ARITA Expert Series: Insolvency – Season 1, 11/11/2021; Presentation Slides]

Risk Management

In Brief | The Security Legislation Amendment (Critical Infrastructure) Bill 2021 passed both Houses on 22 November 2021. The Bill introduces new mandatory cyber incident reporting requirements for 'owners and operators of critical infrastructure' as well as new powers for the government to step in to 'assist' in the event of a 'significant' cyber attack

[Source: Security Legislation Amendment (Critical Infrastructure) Bill 2021]

In Brief | Expansion of the CDR: The government has released Treasury's final sectoral assessment report which recommends telecommunications be the third sector designated for the Consumer Data Right (CDR). The government is consulting on a draft designation instrument setting out the scope of datasets and data holders proposed to be designated. The due date for submissions is 13 December 2021.

[Sources: Consumer Data Right: Telecommunications sectoral assessment; Treasury Consultation: Consumer Data Right - Telecommunications draft designation instrument 23 November 2021 - 13 December 2021]

In Brief | NSW Modern Slavery Act (finally) set to commence: The NSW Modern Slavery Amendment Bill 2021 (NSW) passed both Houses on 19 November 2021

[Source: Modern Slavery Amendment Bill 2021 (NSW)]

Corporate Misconduct and Liability

How has corporate law been enforced in Australia? Melbourne University Study sheds light on enforcement activity in the decade leading up to the Hayne Commission

A University of Melbourne study provides an overview of 10 years of corporate law enforcement activity in Australia over the 2009-2018 period. Our key takeaways are below.

Key Takeouts

- The study identified (among other things) that in the decade leading up to the Hayne Commission: a) the level of criminal enforcement activity under the Corporations Act and the ASIC Act was 'arguably limited'; b) prosecutions against corporations were relatively low; and c) court imposed penalties were 'limited in their severity'.
- The authors consider that this is evidence that there 'may have been underenforcement' during the period.
- The authors consider that the research 'provides a baseline to facilitate future analysis of criminal prosecutions of misconduct, post the publication of the final report of the Hayne Inquiry' and the impact of ASIC's 'why not litigate' approach to enforcement (which was adopted in response to the Hayne Commission)

Overview

University of Melbourne academics Ian Ramsay and George Gilligan have released their analysis of corporate law enforcement activity in the decade leading up to the Hayne Royal Commission.

The findings are based on analysis of the outcomes for all matters that were finalised by the Commonwealth Director of Public Prosecutions (CDPP) between 1 January 2009 and 31 December 2018 under all sections of the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) and the Corporations Act 2001 (Cth) (Corporations Act).

Our key takeaways are below.

Some interesting statistics

- A key finding is that the level of criminal enforcement activity under the Corporations Act and the ASIC Act was 'arguably limited' in light of the 'extent and pervasiveness of business misconduct' known to have taken place over the ten year period of the study with only 715 cases in total finalised by the CDPP.
- The study also identified that prosecution activity focused on a fairly small range of sections of the Corporations Act.
  - The 715 cases during the period were brought under only 86 sections of the ASIC Act and Corporations Act (combined).
  - 98% of cases were brought under the Corporations Act. The top three most commonly applied sections were: 1) s 184(2) – making dishonest use of a position in a company to gain an advantage or cause detriment to the company) (64 cases); 2) s 1043A(1) – insider trading (55 cases); and 3) s 1308(2) – making a false or misleading statement.
- The study also found relatively low levels of prosecutions against corporations: only 16.5% of all cases prosecuted by the CDPP (or 118 prosecutions) in total brought against corporations over the period. The authors observe that a 2020 ALRC report on corporate criminal responsibility also found that prosecutions against corporations were 'extremely rare and generally against small corporations'. The authors suggest that in light of the 'succession of scandals involving misconduct by some of Australia's most significant corporate actors throughout the period under review', the findings of their own study, together with those of the ALRC review, 'raise questions about the ability of Australian regulators to ensure that Australians are sufficiently protected from dishonest and unscrupulous actors in the Australian business sector and the findings also raise questions about whether the documented levels of enforcement provide a sufficient deterrent effect to counter misconduct'.
- The study found that overall, there was a high rate of successful prosecutions. According to the study, the CDPP achieved a proven outcome in 74.7% of total cases for a total of 534 wins. Drilling down, the study found that the CDPP's highest success rate was where it alleged a contravention of s319(1) – failure to lodge annual report with

ASIC within three months – with 91.5% of the 47 cases proven. In contrast, the CDPP's lowest success rate was where it alleged a contravention of s 1043A(1) – prohibited conduct by person in possession of inside information – 58.2% of the 55 cases proven.

- The study also found that court imposed penalties were 'limited in their severity'. For example, of the 534 cases in which the CDPP was successful the court imposed:
  - no fine or prison sentence in 141 (26.4%) of cases
  - fines in 234 (43.8%) of cases
  - prison sentences in 176 (33.0%) cases. The study found that of the defendants who received a prison sentence, 72 (13.5%) were released forthwith meaning that only 104 (19.5%) actually received a custodial sentence.
  - Of those who went to prison, the minimum sentence was two months and the maximum was 174 months. The median prison sentence was 16.5 months and a large group (44.2%) received sentences of 12 months or less (while just over 20% served over three years)
- The authors consider that these figures raise questions about whether the penalties are: a) 'likely to act as a credible deterrent'; and b) are in line with community expectations.

Possible underenforcement but not necessarily a 'crisis of underenforcement'

The introduction to the article cites American scholar John Coffee's claim that there is a crisis of underenforcement of the law against companies in the United States.

Reflecting on whether the results of the study support a similar claim in the Australian context, the authors conclude that though there is evidence that there 'may have been underenforcement', more research would be required to bear out a broader claim. They state:

> 'ongoing empirically grounded scholarly research is essential to producing a mosaic of empirical evidence to inform whether such a claim may be applied more widely to how companies and their directors and officers are regulated in Australia'.

The authors suggest that the study could be used as a baseline for future research into what impact ASIC's 'why not litigate' enforcement approach (adopted in response to the Hayne Commission) has had on enforcement outcomes.

[Source: Gilligan, George and Ramsay, Ian, Is There Underenforcement of Corporate Criminal Law? An Analysis of Prosecutions Under the ASIC Act and Corporations Act: 2009–2018 (August 16, 2021). Company and Securities Law Journal, Vol. 38 No. 6, 2021, pp. 435-458, Available at SSRN: https://ssrn.com/abstract=3916720]

Other News

Consultation on further proposals to modernise Treasury portfolio laws

Key Takeouts

- Draft legislation has been released for consultation aimed at improving the technology neutrality of Treasury portfolio laws. The due date for submissions is 10 December 2021.
- The government has flagged that as part of its broader project to modernise business communications, the next phase of the project will consider 'improving technology neutrality in further contexts' including: a) communicating with regulators; b) exemptions to the Electronic Transactions Act 1999; and c) product disclosure and recordkeeping requirements

Context

Broadly, the Corporations Amendment (Meetings and Documents) Bill 2021 (Meetings and Documents Bill) proposes to: a) permanently give companies and registered schemes flexibility in their choice of meeting format (ie the Bill would permanently enable companies to elect to hold physical or hybrid meetings, or to hold 100% virtual (if expressly permitted to do so under their constitution)); and b) the option to use technology to execute company documents, sign meeting related documents and provide those documents to their members.

If legislated in its current form, the changes would apply to documents sent and meetings held on/after 1 April 2022 (ie the changes would be in place when the temporary relief currently in place expires). The changes would apply to documents executed on/after the day after the Meetings and Documents Bill receives Assent. You can find a short overview of the changes in the Meetings and Documents Bill and how they differ from temporary arrangements now in place here.

Consultation

On 19 November 2021, the government released draft legislation for consultation – [exposure draft] Treasury Laws Amendment (Modernising Business Communications) Bill 2021 and [exposure draft] Treasury Laws Amendment (Modernising Business Communications) Regulations 2021– proposing to build on the reforms in the Meetings and Documents Bill. The changes in the draft legislation are contingent on the passage of the Meetings and Documents Bill.

The due date for submissions to the consultation is 10 December 2021.

Electronic signing and execution of documents

Broadly, Schedule 1 of the draft legislation Bill would:

- enable all documents (including deeds) which are required or permitted to be signed under the Corporations Act 2001 (Cth) (the Act) to be signed electronically or in physical form. For context, if legislated in its current form, the Meetings and Documents Bill would only enable certain documents to be signed or executed electronically.
- enable all documents sent under Chapters 2A to 2M, 5 to 5D, 6-6C, 6D, 8, 8A and 9 or Schedule 2 to the Act to be sent in either hard copy or electronic form. Under the proposed reforms in the Meetings and Documents Bill, most documents with the exception of meeting-related documents must be sent in hard copy.
- allow Australian members of a notified foreign passport fund and any other person prescribed in the regulations (in addition to members of companies, registered schemes and disclosing entities) to elect to be sent documents in either hard copy or electronic form. This election may apply to all documents or a class of documents.
- remove the requirement for companies to send documents to 'lost members' ie members whose contact details are known to be incorrect, provided that certain conditions (set out in s110JA(3)-(4) of the draft Bill are met). These are that:
  - the sender has received notification, that each of the addresses held for the sender are not current
  - the sender reasonably believes that none of those addresses are current
  - the sender is unable, having taken reasonable steps, to ascertain a current address for the recipient (s110JA(4) of the draft Bill states that the sender will not have taken reasonable steps 'unless the sender has attempted to communicate with the recipience using all contact details for the recipient known'

- – the sender has taken reasonable steps to advise the recipient the sending of documents has been suspended but will be resumed if the recipient provides a current address.

Proposed timing

If legislated in its current form the changes in Schedule 1 of the draft Bill would commence on the later of the day after the draft Bill receives Assent and immediately after the commencement of Schedule 2 of the Meetings and Documents Bill. The changes would not commence at all if the changes in Schedule 2 of the Meetings and Documents Bill do no commence.

Credit and payments

Schedule 2 of the draft Bill proposes to amend the requirements for giving documents 'to allow for the greater use of electronic communication'.

Broadly, the draft Bill proposes to introduce requirements for credit providers and others covered by the National Consumer Credit Protection Act 2009 (NCCP Act) to send documents to the electronic or physical address nominated by the recipient. For context, currently credit providers and other persons covered by the NCCP must send documents to the last known postal address, unless the recipient has expressly nominated an electronic address.

The Bill also proposes to remove the requirement for nominations, changes of nomination and communications as to a preference not to receive electronic communications to be made in writing.

The draft Bill also proposes to remove what the draft explanatory memorandum describes as 'technologically prescriptive requirements relating to payments'.

More particularly, the draft Bill proposes to:

- remove the requirement for a no liability company to notify shareholders of the place of payment and to send the notice by post. According to the draft explanatory memorandum this is intended to remove 'any uncertainty that companies can provide for any method of payment, including digital methods'.
- repeal section 32 of the Small Superannuation Accounts Act 1995. This section required the deposit form accompanying the deposit paid to the Commissioner of Taxation under Part 4 of the Small Superannuation Accounts Act 1995 to include certain specifications as to the method of payment.

Proposed timing

- The amendments relating to credit (Schedule 2, Part 1 of the Draft Bill) would apply to information, notices or other documents given from one month after the draft Bill receives Assent.
- The proposed amendments relating to payments (Schedule 2, Part 2 of the Draft Bill) would apply from the day after the draft Bill receives Assent.

Notices in newspapers

- Various Treasury laws require or permit notices to be published in newspapers. Schedule 3 of the draft Bill proposes to amend these requirements to specify that notices can be published in a technology neutral manner ie 'in a manner which results in them being accessible to the public and reasonably prominent'.
- In certain circumstances, the relevant regulator would have power to determine the manner of publication.
- The proposed changes to notice requirements (Schedule 3, Part 1) would commence on a day to be fixed by Proclamation or, if this does not occur, six months and one day after the draft Bill receives Assent.

Draft Regulations

The draft regulations would support the changes in the draft Bill by making the necessary consequential amendments to requirements in various Treasury laws.

Further planned changes in prospect

The next phase of the government's modernisation project will consider further reforms to improve technology neutrality including:

- communicating with regulators

- exemptions to the Electronic Transactions Act 1999
- product disclosure and recordkeeping requirements

  [Sources: Treasury consultation: Improving the technology neutrality of Treasury portfolio laws 19 November 2021 - 10 December 2021; Joint media release Minister for Financial Services, Superannuation and the Digital Economy Jane Hume and Minister Assisting the Prime Minister and Cabinet Ben Morton 19/11/2021]

NSW Bill permanently enabling remote witnessing of documents has passed both Houses

- The NSW Electronic Transactions Amendment (Remote Witnessing) Bill 2021 passed both Houses on 16 November and now awaits Assent.
- Broadly, the legislation will make permanent the temporary measures enabling documents to be witnessed in real time over an audio-visual link (AVL) (remote witnessing), introduced in response to the pandemic.
- The list of people able to witness statutory declarations will also be extended to the broader list of witnesses permitted to do so under the relevant Commonwealth legislation – Statutory Declarations Regulations 2018 (Cth) - for a further 12 months. There are two reasons that the measures are not being made permanent: 1) the 12 month extension will allow more time for the government to evaluate the efficacy of the measures; and 2) it would be 'premature' permanently enact the change before the work of an inter -jurisdictional working group that is currently looking at the State and Commonwealth statutory declaration schemes across Australia has further progressed its work.
- Announcing the reforms, NSW Attorney General Mark Speakman said that having the option to witness documents remotely will provide flexibility for individuals and businesses and 'benefit people living in rural, regional and remote areas' and as well as 'improve access to justice for vulnerable members of the community including older people, people suffering from illness or people with a disability.'
- Traditional methods of signing and witnessing documents remain available.
- The measures will commence on the date of Assent.

  [Sources: Attorney General Mark Speakman media release 16/11/2021; NSW Electronic Transactions Amendment (Remote Witnessing) Bill 2021; Second reading speech]

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