Governance News

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

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Boards and Directors

Worker representation on (large) US boards? If legislated, the TEAM Act would establish a new mechanism for non-unionised workers to engage with company management, including at board level

- US Republican Senator Marco Rubio and US Representative Jim Banks have introduced a Bill - The Teamwork for Employees and Managers (TEAM) Act – which, if legislated, would provide a new engagement mechanism enabling groups of employees to engage with company management on 'workplace issues' without having to unionise/outside of the existing labour union structures/processes.
- Senator Rubio considers that this is desirable because 'current law makes it impossible for employers to have any meaningful discussion about workplace conditions with a non-unionised group of employees' and because many workers do not wish to join a labour union because they do not support 'the left's woke agenda'. Senator Rubio considers that the TEAM Act would solve these issues by 'creating a pro-worker alternative to unions, which are notoriously left-wing and almost always pit workers against management, only worsening the workplace environment.'

Key Takeaways: What would the proposed legislation do?

Among other things, the legislation would:

- Enable employees and employers to establish voluntary Employee Involvement Organisations or EIOs for the purposes of discussing 'workplace issues'. Importantly, the proposed new EIOs would be separate from (and are positioned by Senator Rubio as an alternative to) existing labour unions. As such:
  - EIOs would not be authorised to engage in/negotiate collective bargaining agreements with employers
  - EIO members would not be precluded from forming a labour union
  - an EIO could be established and dissolved by mutual consent between employers and employees
  - any 'violations of EIO-related provisions shall be adjudicated in the U.S. court system, and not by the National Labor Relations Board'.
- Enable an elected EIO worker representative to be appointed to the company's board (where the company has more than $1bn in annual gross revenue) as a non-voting board member.

According to Senator Rubio's statement, the TEAM Act is based on the Employers and Management Act, which was vetoed by then President Clinton in 1996.

Senator Rubio states that the TEAM Act has the support of a number of 'conservative labour experts' including: former Acting Assistant Secretary for Policy at the US Department of Labor Jonathan Berry, Executive Director of American Compass Oren Cass and Senior Labor and Employment Counsel at the HR Policy Association G Roger King.

[Sources: Senator Marco Rubio media release 03/02/2022; Teamwork for Employees and Managers (TEAM) Act of 2022]

Diversity

Top Story | 'Many watersheds' and 'many silver bullets': Key takeaways from an expert panel discussion on D&I issues

An expert panel reflected on the shift in the conversation around gender equality in the workplace as well as Diversity and Inclusion (D&I) issues more broadly, the barriers to progress, key change drivers and the role of leaders in this context. Our key takeaways are below.

The Governance Institute, together with Women on Boards recently hosted an expert panel discussion on Diversity and Inclusion (D&I) issues, including insights into the actions/strategies that have proven to be effective in driving progress and the many recent 'watershed' events/reports that are adding to the existing pressure on organisations to shift their approach. You can find a recording of the session here.

A high level summary of some of the key themes raised in the discussion is below.

Clarifying the difference between diversity and inclusion

Broadly, the panellists agreed that where diversity is about representation – representation of people with a range of different characteristics eg gender, ethnicity/race, etc – inclusion focuses on the behaviours that enable and support diversity – the culture that enables, values and supports diversity within organisations.

Women on Boards Executive Director, Claire Braund summed this up as follows: 'diversity is the what and inclusion is the how'.

Reflecting on her own experience as a woman, a woman of colour and an engineer, Sydney Water Corporation Non-executive Director, Dr Marlene Kanga observed that in a sense the diversity piece is 'the easy part'. She reflected that in order to gain traction, there also needs to be understanding and acceptance across the organisation around why diversity is important and valuable in a business context – an appreciation of why diversity is key to business success. She suggested that firms need to think about diversity 'as the reason' (ie business success) and that this will then drive inclusion.

'Gender fatigue'

The discussion touched on the challenge of what is sometimes called 'gender fatigue' or the perception (particularly among some men) that gender inequality in workplaces is not a problem, despite evidence to the contrary including for example, the persistent gender pay gap, the underrepresentation of women in leadership positions and recent reports into the culture in Australian workplaces.

> [Note: Panellists referred to a recent report from FINSIA highlighting this issue. The report referred to appears to be FINSIA's 2021 report: Gender Divide in Financial Services 2021]

The discussion also touched on the related challenge for organisations in dealing with the 'backlash' toward D&I initiatives and the gap between reality – measures being implemented to address structural inequality – and perception among some groups that they are being unfairly disadvantaged.

Despite the fact that the 'business case' for diversity has so far not delivered change or changed (some) minds, a key theme to emerge from the discussion was the important role that strong, focused leadership. combined with a data-driven approach can play in this context.

What works? The power of a data driven, systematic approach combined with focused, committed leadership

Dr Kanga spoke about the important role that business leaders – the board, the CEO and the executive team – play in countering a 'we've done this already' mindset and driving concrete progress.

Reflecting on her own experience, she said that some boards have been successful in closing their gender pay gaps 'within a couple of years' through taking a data-driven, systemic approach to the issue - calling for analysis of the pay gap within their organisation, identifying the reasons for it, implementing actions to address it, and then monitoring progress. Dr Kanga emphasised that sustained leadership focus on the issue, and monitoring/oversight of the effectiveness of measures being implemented, is key to progress.

Later in the discussion, and again reflecting on her own experiences in the engineering sector, Dr Kanga described how 'borrowing' from the approach taken to lifting standards of workplace safety had been effective in driving progress in the D&I context. Dr Kanga said that this had the advantage of rendering the desired systemic changes concrete as opposed to 'esoteric' – similar changes and reporting requirements had been implemented already in the safety context – and meant that managers accorded them the same high level of importance.

On a similar note, Governance Institute of Australia CEO Megan Motto described the data-driven approach to addressing the loss of women in the leadership pipeline, which has been used successfully by some engineering firms, to illustrate the power of data in changing otherwise fixed mindsets. Ms Motto explained that the firms in question knew that the number of women decreased as they progressed up the organisational hierarchy starting a graduate level. In an effort to address this, the firms paid female graduates 3% more than their male peers. However, a closer look at the data showed that after 12 months at the firm, female graduates were actually earning 5% less than their male peers.

Ms Motto said that this realisation highlighted the existence of a 'a structural impediment' to women's progression and prompted investigation into its causes and the adoption of an interventionist approach to address it.

However, despite the power of data to highlight the problem and enable assessment of the effectiveness of actions to address it, Ms Motto reflected that it is still not being utilised by nearly enough firms.

Quotas?

Ms Motto opined that implementing targets is 'more difficult to implement than people think' but seemed to suggest that 'targets with teeth', combined with interventionist strategies to level the playing field, could be valuable as a means of forcing a change in the way things are done.

Panel Chair, journalist and author Catherine Cox appeared to be in agreement, querying how, without data, people can be convinced of a need for change.

Pressure is mounting on organisations to make progress

Though there is no 'one thing' or 'silver bullet' that is an answer in itself to addressing the lack of progress on D&I issues, the panel agreed that there are a number of actions, or a number of known silver bullets, that used in combination, have proven to be effective.

On the issue of whether any one of the recent watershed events or recent reports will prove to be a tipping point, the panellists reflected that it is unlikely that any one event/report will trigger a shift (though there was optimism that this would be the case). It was suggested instead there have been a number of 'watersheds' in recent years and that in combination these are adding to the existing pressure on organisations (from the community and from investors who increasingly view D&I as a key governance issue) to achieve progress.

> [Source: This post is based on notes from a Governance Institute and Women on Boards Webinar: Diversity is half the circle. Culture, equity and inclusion are the other half, 04/02/2022. You can find a recording here]

New research links gender diverse leadership to a higher chance of business success

Research from ESG Directory Purpose Bureau tracking the performance of Australian businesses over the 2021 calendar year has identified that businesses with boards made up of one gender are 37% 'more likely to fail' (ie to be deregistered) than businesses with boards with a mix of male and female directors.

Interestingly, Purpose Bureau found that this was particularly marked in the Education and Training businesses, with single gender led businesses in these sectors 78% more likely to fail.

Commenting on the findings, Purpose Bureau CEO Nick Kamper said that they suggest that gender diversity 'leads to better business outcomes'.

> 'The research requires further analysis to fully understand the dynamics at play, but it's further evidence that Australian businesses benefit greatly from a diversity of views and experience at the leadership level…Gender diversity is not just 'a nice to have', it is actually linked to superior business performance.'
>
> [Source: Purpose Bureau media release 05/02/2022]

In Brief | Joint analysis from the 30% Club and Deloitte looking at representation of women on boards globally has confirmed that progress is being made (though it remains slow). According to the report, globally women remain underrepresented in top roles, holding an average of 19.7% of board seats (up 2.8% since 2018), only 6.7% of board Chair positions and 5% of CEO roles

> [Source: 30% Club media release 01/02/2022; Full text report: Women in the Boardroom: A Global Perspective]

Shareholder Activism

Follow This has called on shareholders to back its climate resolution at Chevron ahead of the May AGM

- In May 2021, 61% of Chevron's shareholders voted in a support of a FollowThis coordinated resolution calling on the company to decrease emissions. FollowThis considers that Chevron has not adequately responded to shareholder concerns following that majority vote.
- For example: Follow This has previously raised concerns that the emissions reduction targets set by the company are not Paris-aligned and fall short of investor expectations. FollowThis also points to Chevron's Q4 2021 results (Chevron's press release here) as evidence that the company is not doing enough, noting that:
  - The results highlight that Chevron has both increased oil production and 'added proved reserves'.
  - Chevron makes only brief reference to 'progress to advance its lower carbon future', continues to underinvest on transition plans and has not set targets to reduce its Scope 1, 2 and 3 emissions 'in the near future'.
- In light of this, FollowThis has called on shareholders to again support its emissions-reduction resolution at the May AGM (pending Securities and Exchange Commission (SEC) approval). Specifically, the resolution calls Chevron to set and publish medium- and long-term targets to reduce the greenhouse gas (GHG) emissions of the Company's operations and energy products (Scope 1, 2, and 3) consistent with the goal of the Paris Climate Agreement: to limit global warming to well below 2°C above preindustrial levels and to pursue efforts to limit the temperature increase to 1.5°C.
- Mark van Baal of Follow This comments:

  > 'Chevron is reporting as if there is no Paris Climate Agreement, and no shareholder majority that both request emissions reductions…There's no room for growing fossil fuel production in the Paris Accord.'
  >
  > [Source: FollowThis media release 28/01/2022]

Meetings and Proxy Advisers

'Boards need to appropriately manage their directors' increasing time commitments': State Street has signalled a shift in approach to the issue of director 'overboarding'

Following a program of direct engagement with boards, State Street Global Advisors (SSGA) has said that it is updating its voting policy and guidelines on director 'overboarding' including its expectations around how Nominating Committees monitor directors' external time commitments as well as disclosure expectations on the issue.

Changes to SSGA guidance on director external time commitments

- SSGA has flagged that it is updating its proxy voting guidelines on director commitments to reflect its expectation that Nominating Committees are responsible and accountable for 'evalutat[ing] their directors' time commitments, regularly assess director effectiveness, and provide public disclosure on their policies and efforts to investors'.
- SSGA comments that

  'Rather than investors holding individual directors with excessive external commitments accountable, we believe well-governed boards are responsible for establishing, enforcing and disclosing their director commitment policies.'
- SSGA 'hopes' that this approach will enable other topics to be prioritised in engagement discussions with companies.

Changes to voting guidelines - New 'disclosure waiver'

From March 2022, SSGA states that it may 'vote in support of a director' (despite the fact that they otherwise 'hold excessive commitments' by reference to SSGA's existing policy) if the company publicly discloses its director commitment policy.

This director commitment policy would need to include:

- A 'numerical limit on public company board seats a director can serve on'. This limit must not exceed SSGA's own policy 'by more than one seat'
- 'Consideration of public company board leadership positions (eg Committee Chair)'
- 'Affirmation that all directors are currently compliant with the company policy'
- 'Description of an annual policy review process undertaken by the Nominating Committee to evaluate outside director time commitments'

SSGA makes clear that the director commitment policy for named executive officers (NEOs) of public boards who hold seats on more than two public boards is 'not subject to the disclosure waivers'.

SSGA states that from 2022, in light of feedback provided through engagement with boards, it 'will not consider service on a SPAC board when evaluating directors for excessive commitments. However, we do expect these roles to be considered by Nominating Committees when evaluating director time commitments'.

Reasons given for revisiting existing guidelines and voting policy

- Being an effective director entails a bigger commitment than it has done in the past: SSGA states that engagement with board members highlighted that the challenges posed by the COVID-19 pandemic, together with various other strategic challenges (eg transition planning) has increased directors' workload. For example:
  - Globally, the frequency of formal board meetings has increased: According to State Street, in 2021, S&P 500 boards formally met an average of 9.4 times, (up 25% on the previous year), while FTSE 150 boards held an average of 11.6 meetings in 2021 (up 50% on the previous year).
  - The frequency of internal and external stakeholder engagement has also increased
  - There is an expectation that board are across emerging risks and are 'conversant in material, company-specific ESG issues and actively engaged in relevant oversight'.
- Overcommitted directors are a risk: According to SSGA's analysis, boards with over-committed directors are 'slower to adopt leading corporate governance practices and to offer robust shareholder rights to their investors'. To illustrate, ISS observes that in 2021, 60% of S&P 500 companies assessed (by SSGA) as 'governance

laggards'- which is to say, companies with a 'low level of compliance with their country specific governance codes' - had boards that included overboarded directors.

- **Appointing directors from the existing over-committed pool contributes to the lack of progress on board diversity:** SSGA also suggests that failure on the part of boards to ensure directors are not over-committed/able to devote the necessary time to their role can also

  > 'contribute to "tokenism" among the director community, nominating already over-committed directors who are considered to be diverse based on their gender, race and/or ethnicity, or other dimensions of diversity'. SSGA suggests that 'more rigorous director commitment policies can help ensure that broader candidate pools from these communities are considered'.

[Sources: Harvard Law School Forum on Corporate Governance and Financial Regulation 03/02/2022]

Disclosure and Reporting

California is a step closer to legislating minimum climate disclosure requirements for large companies: The Climate Corporate Accountability Act has passed the Senate

- California is potentially one step closer to imposing minimum climate emissions disclosure requirements on large firms doing business in the State following the passage of Senate Bill 260, the Climate Corporate Accountability Act (CCAA), through the Senate.

- Broadly, assuming the passage of the legislation through the Assembly and assuming it is signed into law, the CCAA would require:
  - reporting entities (ie United States-based partnerships, corporations, limited liability companies, and other business entities with total annual revenues in excess of $1bn that do business in California) to report annually on their Scope 1, 2 and 3 emissions
  - disclosure to be 'independently verified by a third party auditor approved by the state board, with expertise in greenhouse gas emissions accounting'
- Announcing the passage of the Bill through the Senate, Senator Scott Weiner (Bill co-author) described in the Bill as 'the first of its kind in the country' and an important step towards improving transparency around the emissions being generated by major corporations. He states:

> 'Corporate transparency and accountability are critically important when it comes to addressing our climate crisis…Corporate emissions are a huge contributor to climate change, but frankly, we don't yet know the scope of the problem. That's why we need to act quickly and decisively to ensure corporations are reporting their emissions. This is a landmark bill, and today's vote is a big step forward for California's fight against climate change'.

[Sources: Senator Scott Weiner media release; Senate Bill 260, the Climate Corporate Accountability Act]

In Brief | Greenwash? New report assessing the integrity of net zero climate pledges made by 25 major global companies found no company merited a 'high integrity rating' and the majority pledges were of low or very low integrity

[Sources: New Climate Institute media release 07/02/2022; Full text report: Corporate Climate Responsibility Monitor 2022]

Institutional Investors and Stewardship

New report finds a majority of Climate Action 100+ investors continued to support directors of climate laggard companies in 2021

- A report from Majority Action analyses how the largest 75 investor signatories to the Climate Action 100+ coalition voted on director elections and shareholder proposals at the 45 United States-based Climate Action 100+ focus companies in 2021.
- For context, Majority Action takes as its starting point the fact analysis from Climate Action 100+ had previously identified that none of these 45 companies was fully on track to reach net zero emissions ahead of the 2021 US proxy season. For example: only 10 of the 45 companies had set a net zero by 2050 ambition and no company had met all the benchmark indicators for capital allocation or climate policy engagement.

The voting decisions of some investors are 'undermining' efforts to hold directors to account

The headline conclusion the report draws is that despite the poor progress being made by focus companies, some Climate Action 100+ investors failed to exercise their voting power to support the goals of the initiative. The report states:

> 'the efforts and effectiveness of this initiative and its leading investors to hold the boards of high emitting companies accountable are being systematically undermined by the proxy voting behaviour of many of its largest investor-signatories'.

For example, the report found that:

- a majority of Climate Action 100+ investors (including BlackRock, Fidelity International and others) continued to support incumbent directors at 23 companies of the 45 companies
- Four Climate Action 100+ investors (Fidelity International, HSBC Asset Management, Janus Henderson Investors, and Lord Abbett) voted for every director at the seven companies that failed to set a 'net-zero ambition' or issue TCFD-aligned emissions disclosures
- Majority Action considers that shareholder resolutions at Chevron, Dominion Energy, Duke Energy, and Caterpillar, which were 'flagged' by Climate Action 100+, would have passed, but for some Climate Action 100+ investors voting against them. According to Majority Action, BlackRock voted against all four of these flagged resolutions, and State Street voted against three of the four.

Majority Action's report also takes issue with what it considers to be a lack of transparency on the part of some Climate Action 100+ investors around their voting decisions. According to the report, 21 Climate Action 100+ investors reviewed failed to 'disclose their firm-level proxy voting performance in a way that would allow their performance to be analysed and evaluated'.

Recommended actions

To address these issues, the report urges Climate Action 100+ investors to implement the following four recommendations:

- 'Adopt and implement proxy voting policies that enable voting against directors at companies that fail to align their targets, capital expenditures, and policy influence to 1.5ºC pathways'
- 'Leverage resources like the vote flagging process and the Climate Action 100+ Net-Zero Company Benchmark to drive proxy voting to hold directors accountable'
- 'Announce their intention to vote in advance of annual meetings, and disclose all votes at Climate Action 100+ companies within six months of the AGM date'
- 'Ensure that any asset managers or service providers for which an investor-signatory is a client are also voting for climate-critical shareholder proposals and against directors at misaligned companies. Include a review of managers' proxy voting track record on climate change in the due diligence process for all asset manager mandate renewals and RFPs'.

The report further recommends that the Climate Action 100+ initiative should:

- 'Flag key votes on directors at companies that demonstrably fail to achieve the Climate Action 100+ Net-Zero Benchmark, and ensure that all key climate resolutions at Climate Action 100+ companies are flagged for Climate Action 100+ members'
- 'Establish proxy voting performance expectations for investor members, and uplift best standards for proxy voting policies and practices'
- 'Require prompt and comprehensive public disclosure of proxy voting from all Climate Action 100+ signatories'.

[Sources: Majority Action media release; Majority Action full text report: Fulfilling the Promise: How Climate Action 100+ Investor-Signatories Can Mitigate Systemic Climate Risk]

Ceres has released a guide to assist investors in engaging with US companies on material climate risks ahead of the 2022 proxy season

Ceres has released new guidance to guide investor engagement with US companies on governance and climate risk ahead of the 2022 proxy reason. Ceres suggests that the guidance could be used to help inform decision making in the context of director elections – that is decision around whether to support the election of directors with climate risk oversight responsibility.

Ceres further suggests that the guidance may be of use to proxy advisers as well as to companies (as a resource to help them prepare for stakeholder engagements).

The table below provides a brief snapshot of the key takeaways.

ISSUE	WHAT CERES CONSIDERS INVESTORS SHOULD BE LOOKING FOR
Ceres offers the following guidance (based on the TCFD 'Governance' recommended disclosures and the Net-Zero Company Benchmark)	
▪ Is there effective board oversight of climate-related risks/opportunities and GHG emissions reduction targets?	▪ Boards should exercise and publicly disclose (eg in the board committee charter) 'independent board oversight' of climate related risks/opportunities including monitoring the company's science-based greenhouse gas (GHG) emission reduction targets. ▪ Where a board committee has oversight responsibility, the committee should: – 'ideally' be composed of 'only independent directors' – committee members should have attended at least 75% of the committee's and full board's meetings over the past year (unless an acceptable reason for absences is disclosed in an SEC filing)
▪ How effectively is management assessing and managing climate related risks/opportunities?	▪ Companies should have in place and 'disclose the existence' of a 'cross-functional senior management committee', with responsibility for company-wide management of climate related risk/opportunities. ▪ This committee should have a direct reporting line to the CEO and a 'dotted line' to the full board and the board climate committee.
▪ Does the board have the necessary capabilities/competencies to oversee climate-related risks/opportunities?	▪ The guidance makes clear that 'no one director will make a "climate competent" board'. ▪ Instead, boards should assess and disclose how each board member's experience contributes to 'thoughtful discussions and meaningful connections with the long-term strategy, given the unique climate risks and opportunities the company faces'. ▪ From a practical perspective, Ceres suggests that companies should disclose 'sufficient information' on their board's 'climate competency' eg through disclosure of board matrices with

ISSUE	WHAT CERES CONSIDERS INVESTORS SHOULD BE LOOKING FOR
	further detail (supporting the expertise listed in board matrices) provided in director biographies.
▪ How has the board and senior management responded to majority supported resolutions?	▪ Companies should disclose the company's response to a majority supported proposal (eg a shareholder climate resolution or a resolution to elect/re-elect a director that failed to receive majority support on climate grounds) and 'address investor concerns behind the vote' 'within a reasonable time' after the vote. ▪ Ceres also suggests that proposals that received between 20% and 50% also warrant 'outreach to investors after the vote'.
▪ Has there been sufficient board/senior management response to climate related controversies/failures?	▪ Companies should disclose the reasons for 'any climate-related controversy or failure' that has occurred over the past year, as well as any 'mitigating actions' taken in response
▪ To what extent are independent directors available to engage with shareholders on climate issues?	▪ One or more independent directors should be available to engage with 'significant shareholders' on material climate risk issues (ie issues listed for the company's industry in the SASB materiality finder). ▪ Ceres suggests that the measure of 'significance' 'should be determined not only with respect to assets under management, but also by other factors, such as a shareholder's recognised leadership in the climate space'.
▪ Is there 'sufficient' audit committee oversight of climate related risks and disclosures?	▪ Audit committees should direct the company's internal audit department and its independent auditors to conduct both: – 'sufficient testing of the impacts of climate change risk on the company's operations'; and – a 'review of the related disclosures in the company's audited and interim financial statements (including, for example, whether any asset valuation write-downs are appropriate), with clear disclosure of assumptions used in their testing'.
Ceres offers the following further guidance (based on Climate Action 100+ Net-Zero Company Benchmark Indicators)	
▪ What is the board's role in overseeing the company's Science-Based GHG Emission Reduction Targets and Decarbonization Transition Plans?	▪ Ceres considers that boards should have oversight of the development, implementation and disclosure of 'comprehensive transition plans that include science-based GHG emission reduction targets, including annual progress toward meeting these goals and independent verification'.
▪ Paris-aligned lobbying – what role does the board play in ensuring any lobbying activity is aligned?	▪ Boards/board committees should 'have explicit oversight responsibility for reviewing company policies and practices to determine whether their companies lobby–directly or indirectly (through each of their trade or other associations)–for public policies that support the transition to a low-carbon economy consistent with the goals of the Paris Agreement'. ▪ Should an inconsistency between the company's direct or indirect lobbying activity and the goals of the Paris Agreement (or progress towards those goals) be identified, the Board/Board Committee should: ensure a public explanation of the reasons for the misalignment is given and outline the 'mitigating steps the company is taking to address 'legal, financial, or reputational risks resulting from this misalignment'.

ISSUE	WHAT CERES CONSIDERS INVESTORS SHOULD BE LOOKING FOR
Does the company provide TCFD aligned disclosure (including disclosure in relation to the two Governance Recommendations?	▪ Ceres considers that companies should disclose the two TCFD 'Governance' recommendations. ▪ These disclosures should explain how the company has integrated climate risks and opportunities into company strategy and operations. ▪ If a company's TCFD reporting does not include disclosures for all 11 recommendations, Ceres considers that the company should publicly disclose a timeframe for when this will occur.

Withholding support for directors

Where investors consider that companies have not met the expectations set out above and/or are considered not to have taken appropriate steps/made sufficient progress on climate issues, Ceres suggests that investors could elect to 'withhold support' for the director or directors responsible for overseeing specific aspects of climate-related risk, governance or board composition, depending on the circumstances.

Ceres suggests that in situations where there is no specific committee climate committee oversight responsibility directors could consider voting against one or more of the following:

- Audit Committee Chair (or all Audit Committee members)
- Nominating/Governance Committee Chair (or all Nominating/Governance Committee members)
- Public Affairs/Sustainability Committee (or equivalent committee) Chair (or all Committee members)
- Independent Chair or Lead Independent Director; and/or
- All members of the Board of Directors
- Directors with problematic or insufficient experience or expertise

The guidance further suggests investors who are signatories to the Climate Action 100+ Initiative 'should consider focusing more attention in their company engagements with Climate Action 100+ focus companies on how company reporting aligns with both the Net-Zero Company Benchmark and the TCFD Recommendations. Gross misalignment could also inform voting against directors'.

[Sources: Ceres media release 02/02/2022; Full text report: 2022 Ceres Guidance for Engaging on Climate Risk Governance and Voting on Directors]

Markets and Exchanges

ASX is consulting on proposed rule changes to facilitate the listing of CCIVs

- The Corporate Collective Investment Vehicle Framework and Other Measures Bill 2021 was introduced in the House of Representatives on 25 November 2021 and subsequently referred to the Senate Economics Legislation Committee for review. Among other things, the Bill proposes to establish the tax and regulatory frameworks for corporate collective investment vehicles (CCIVs).
- The Senate Economics Legislation Committee has recommended that the Bill 'be passed as soon as practicable in order to provide certainty to stakeholders working towards the 1 July 2022 deadline for implementation of the CCIV and the retirement income covenant'.
- The Bill has yet to pass either the House of Representatives or the Senate.

ASX Consultation on proposed changes to ASX Listing Rules and ASX Operating Rules

In preparation for the passage of the Bill, the ASX has released a consultation paper seeking stakeholder views on proposed changes to the ASX Listing Rules and the ASX Operating Rules to facilitate the listing of Corporate Collective Investment Vehicles (CCIVs) and certain other collective investment vehicles on the ASX market and the quotation of their products on the ASX AQUA market.

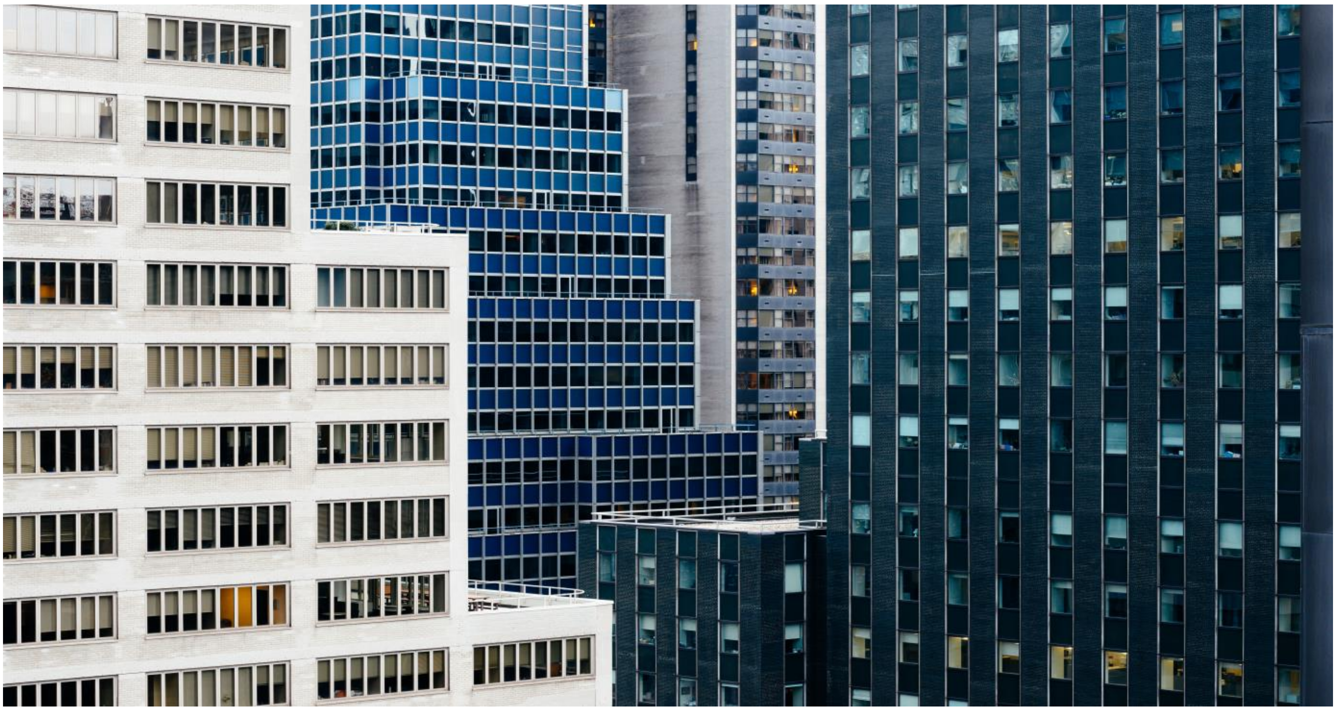
- The proposed amendments to the ASX Listing Rules are intended to facilitate the listing of CCIV sub-funds, NFPFs and recognised NZ schemes on the ASX market. Annexure A of the consultation paper is a mark-up of the proposed changes.
- The proposed amendments to the ASX Operating Rules are intended to facilitate the admission of CCIV sub-fund products, NFPF products, and securities issued by recognised NZ schemes pursuant to a 'recognised offer of securities' as AQUA products. Annexure B of the consultation paper is a mark-up of the proposed changes.

Annexures A and B each include drafting notes explaining the purpose of the proposed amendments.

Proposed timing

- The due date for submissions on the proposed rule amendments is 18 March 2022.
- ASX writes that 'subject to the receipt of the necessary regulatory approvals, ASX is aiming to have the amended rules in force on, or as soon as practicable after, 1 July 2022, the government's target date for the introduction of its CCIV legislation' (assuming the Bill is passed).

[Source: Listed@ASX Update no. 01/22: 08/02/2022]



Regulators

Labor led Senate Committee backs expansion of proposed CSLR, raises 'serious concerns about the performance of ASIC'

Key Takeouts

- The (Labor controlled) Senate Standing Committee on Economics Inquiry into Sterling Income Trust Final Report makes 11 recommendations including: expanding the scope of the planned Compensation Scheme of Last Resort (CSLR) to include managed investment schemes; tougher penalties for breach of Corporations Act obligations; and expanded powers for ASIC eg a directions power.
- The report is also critical of ASIC's regulatory approach, suggesting that the regulator should have been more proactive in acting on 'red flags' in this instance (and going forward)

Context

The Senate Standing Committee on Economics Inquiry into Sterling Income Trust (which is Chaired by Labor Senator Anthony Chisholm) was tasked with inquiring into:

- 'the Australian Securities and Investments Commission's [ASIC's] oversight of the Sterling Income Trust'
- 'the need for legislative and regulatory reform to prevent such losses in the future'
- 'access to justice and redress for victims of the Sterling Income Trust Collapse'
- 'the novelty of the products of the Sterling Income Trust'
- 'why the scheme collapsed and where the money went'
- any related matters'.

The Committee released its final report on 4 February 2022. A high level overview of some of the key issues raised with respect to ASIC's role, the broader financial services regulatory regime and recent legislative reforms is below.

Regulatory oversight

Chapter 4 of the report sets out the Committee's view on the regulatory oversight of the Sterling Group including ASIC's regulatory response, and more particularly whether ASIC could and should have acted more quickly.

Among other things, the report raises concerns that ASIC failed to take a sufficiently 'proactive' stance in this case as well as broader concerns about the adequacy of existing consumer protections more generally, about the effectiveness of the existing penalty regime.

ASIC's response

The Committee makes clear that it considers ASIC should have taken action more quickly in this case.

> …'the committee also has serious concerns about the performance of ASIC with respect to the Sterling Group matter, including its under-assessment of the gravity of the risks, the timeliness of its response, and its failure to act proactively. The committee is mindful of the requirements for ASIC to obtain proper evidence and follow due process before undertaking investigations and enforcement actions. The committee is also conscious that ASIC's regulatory role does not involve preventing all consumer losses or ensuring compensation for consumers in all cases where losses arise. However, in this instance the committee believes that ASIC had sufficient evidence and grounds for concern in 2017 to refer the matter to its enforcement division for investigation. In fact, the issues identified in ASIC's Statement of Concerns were serious and appeared to establish possible contraventions of the Corporations Act 2001(Corporations Act)'.

The report calls on ASIC to take a more 'proactive' approach going forward.

> 'The committee also emphasises that having suitable regulatory tools must be accompanied by a willingness of the regulator to use them appropriately. In a risk-based regulatory framework, being proactive in assessing risk and acting on any adverse assessments is paramount. In the Sterling Group case, there were obvious signs that this was a high-risk structure with potentially devastating consequences for investors who were not experienced and could ill afford for the scheme to fail. Accordingly, the committee encourages ASIC to take

the wheel and not a be a passenger until it is too late in the oversight of managed investment schemes and other financial products where there are obvious "red flags".'

A need for tougher penalties?

The Committee also raises concerns that the existing penalty regime (under the Corporations Act 2001 (Cth)) may not provide sufficient deterrence. The report states that:

> '…the financial products were offered by directors and key executives with a history of failed business ventures. Given that the buyer assumes the risk of such products, those responsible for the products should correspondingly face penalties commensurate with any harm caused when these products fail. While the introduction of director identification numbers may be of assistance going forward, it may not help existing consumers if historical records are not included.
>
> Clearly, the current penalty regime is insufficient to deter high-risk schemes, such as the SIT, being marketed to retail investors. Indeed, the director of the Responsible Entity for the SIT was banned for only four years while the victims of the Sterling New Life Lease (SNLL) scheme face insecure housing for the rest of their lives. As such, the committee considers that the penalty regime associated with contraventions of Corporations Act ought to be amended to sufficiently deter the creation of high-risk financial products that have a significant risk of failure'.

Snapshot: Report Recommendations

The report includes 11 recommendations, the bulk of which are aimed at strengthening protections for consumers. Government Senators delivered a dissenting report outlining their responses to each of the recommendations.

The recommendations in the report are as follows.

Recommendations specific to the collapse of the Sterling Group

Recommendations 1-3 are relate specifically to the collapse of the Sterling Group. These are as follows.

- Recommendation 1 recommends that the government 'take all necessary action to support investors in the Sterling Group of companies…being able to access the Compensation Scheme of Last Resort'.
- Recommendation 2 recommends that 'tenant-investors should be supported to access appropriate and affordable housing given that they lost this security with the failure of the 'rent-for-life' scheme'.
- Recommendation 3 recommends that ASIC investigate and, if appropriate, commence legal proceedings against Australian Financial Services licence holders (current and former) that are alleged to have breached section 917B of the Corporations Act 2001 but have not consented to participate in relevant Australian Financial Complaints Authority processes.

The remaining recommendations are broader in scope.

- Expansion of the CSLR: Recommendation 4 recommends that the government expand the scope of the proposed Compensation Scheme of Last Resort (CSLR) to include managed investment schemes.

  The Committee considered that there is a 'strong case' for the expansion of the scheme 'given the evidence of uncompensated losses that have occurred due to failed management investment schemes, such as the SIT'.

  In their dissenting report, government senators disagreed with the recommendation, stating that the 'government has introduced legislation proposing a CSLR consistent with the Royal Commission's recommendations and the Ramsay Review'.
- Tougher penalties for breach of obligations under the Corporations Act? Recommendation 6 recommends that the government 'review the penalty regime associated with contraventions of the Corporations Act 2001 to deter the creation of high-risk financial products that have a significant risk of failure'.

  In their dissenting report, government senators observed that:

  > 'At the outset, it should be noted that the penalty regime is designed to deter and penalise misconduct, not necessarily to prevent the creation of high risk financial products which may be sold in accordance with law.
  >
  > Further analysis of penalties given under the existing regime should inform any review. Given the scope of this inquiry and the limited time, we have not had the benefit of being able to review the data in this regard.
  >
  > We agree that consumers need to be protected from those who have engaged in egregious unlawful conduct which has caused financial devastation'.

- **A review of the implementation of the recommendations of previous financial services regulation inquiries:** Recommendation 5 recommends that a parliamentary review of the implementation of recommendations from 'all relevant parliamentary and government inquiries in relation to financial service regulation since the global financial crisis and an evaluation of the government responses' including the Hayne Commission, should be undertaken. The report further recommends that the Minister Table in their response to this report, 'all recommendations from all relevant parliamentary and government inquiries since the global financial crisis and the government responses'.

  In their dissenting report, government senators did not reject this recommendation stating:

  > 'We understand that the government undertakes regular reviews of implementation programmes. However, there is of course always merit in a consolidated review process to be undertaken'.

- **Stronger powers and an additional focus area for ASIC:**
  - **Directions power:** Recommendation 7 recommends that the government 'expedite the development of legislation' to grant ASIC a directions power 'in relation to financial services and credit licensees as recommended by the Australian Securities and Investments Commission Enforcement Review Taskforce, noting that an exposure draft was already issued in 2020'.
    In their dissenting report, government senators noted that ASIC has recently been granted new powers and that 'law makers should take time to assess the impact' of these before contemplating whether further reforms are required.
  - **Extension of ASIC's 'public warning power':** Recommendation 8 recommends that the government 'consider extending the Australian Securities and Investments Commission's public warning power to include situations where the Australian Securities and Investments Commission has reasonable grounds to suspect a financial product or credit product (or a class of such products) has resulted, will result or is likely to result in 'significant consumer detriment'.
    In their dissenting report, government senators noted that ASIC ;already has the ability to issue to the public a written notice for a wide range of reasons' and commented that 'whilst there is merit in considering further initiatives and enhancements', there is also a need to take time to consider the practical impact of recent reforms'.
  - **'Framework' for promoting greater consumer awareness:** Recommendation 11 recommends that ASIC 'develop a framework to promote greater awareness and understanding among retail investors and financial consumers in relation to buying financial products and services'.
    In their dissenting report, government senators acknowledged the 'continuing need for raising awareness and understanding in relation to these matters' and noted that ASIC has a number of initiatives already in place. They observed however that 'there is always merit in reviewing the performance of such initiatives and making enhancements'.

- **Marketing review**: Recommendation 10 recommends that the government 'review the marketing of, and financial advice for, investment products which deal in real property interests and whether or not sufficient protections are available for investors in these products'.

- **Address 'jurisdictional overlap':** Recommendation 9: The committee recommends that the government 'work with state and territory governments to clarify the jurisdictional overlap between Commonwealth and state regulation of financial products. In particular, the Australian Government should review investment schemes that include real property rights, including accommodation, leases and tenancy rights under state and territory laws'.

  [Sources: Senate Standing Committee on Economics Inquiry into Sterling Income Trust: Final Report]

In Brief | ASIC Q4 2021 update: ASIC has released a recap of work undertaken between 1 October and 31 December 2021

[Sources: ASIC media release 03/02/2022; REP 717 ASIC quarterly update: October to December 2021]

Financial Services

Bill proposing to establish the planned cyclone and flood damage Reinsurance Pool introduced

- Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022 was introduced into the House of Representatives on 9 February 2022.
- Broadly, the Bill proposes to establish the necessary framework for the Australian Reinsurance Pool Corporation (ARPC) to implement a cyclone and related flood damage reinsurance pool. According to the explanatory memorandum, the reinsurance pool is intended to improve the accessibility and affordability of insurance for households and small businesses in cyclone prone areas.
- In a statement flagging the government's intention to introduce the Bill, the government said that changes have been made to the proposed scheme in line with feedback received through consultation on the draft legislation. According to the statement, these changes include: a) expanding the pool to provide coverage for small business marine property insurance from 1 July 2023; and b) 'adjustments to ensure that more strata properties will benefit from the pool'.
- The statement adds that the establishment of a reinsurance pool will ensure those living in cyclone prone areas have access to affordable insurance. According to the government's statement:
  - over 880,000 insurance policies in northern Australia are expected to be eligible to be covered by the reinsurance pool
  - the pool is expected to reduce insurance premiums by up to $2.9bn for eligible household, strata and small business insurance policies over ten years.
- The Australian Competition and Consumer Commission (ACCC) has been directed by the government to undertake price monitoring to ensure the benefits of the scheme flow through to policy holders.

[Source: Joint media release Prime Minister Scott Morrison (and others) 07/02/2022]

Unfair contracts reform: Treasury Laws Amendment (Enhancing Tax Integrity and Supporting Business Investment) Bill 2022 proposes to (among other things) introduce a civil penalty regime prohibiting the use of unfair contract terms in standard form contracts

Treasury Laws Amendment (Enhancing Tax Integrity and Supporting Business Investment) Bill 2022 Unfair contract terms was introduced into the House of Representatives on 9 February 2022.

Among other things, Schedule 4 of the Bill (if legislated) would amend the Competition and Consumer Act 2010 (Cth), the Australian Consumer Law as set out in Schedule 2 to the Competition and Consumer Act 2010 (Cth) and the Australian Securities and Investments Commission Act 2001 (Cth) to (in the words of the explanatory memorandum):

> 'reduce the prevalence of unfair contract terms in consumer and small business standard form contracts. The amendments introduce a civil penalty regime prohibiting the use of and reliance on unfair contract terms in standard form contracts. The amendments also expand the class of contracts that are covered by the unfair contract terms provisions'.

According to the explanatory memorandum, Schedule 4 implements a commitment to reform unfair contract terms protections announced by the Assistant Treasurer on 10 November 2020.

Proposed implementation date: Assuming the passage of the Bill as currently drafted, these amendments would commence the 'day after the period of 12 months after the Bill receives Royal Assent'.

[Source: Treasury Laws Amendment (Enhancing Tax Integrity and Supporting Business Investment) Bill 2022]

Senate Committee backs Bill proposing to establish the CCIV framework and introduce the retirement income covenant

- The Corporate Collective Investment Vehicle Framework and Other Measures Bill 2021 was introduced in the House of Representatives on 25 November 2021.

- Broadly, the Bill proposes to:
  - establish the tax and regulatory frameworks for corporate collective investment vehicles (CCIVs)
  - amend the Superannuation Industry (Supervision) Act 1993 (Cth) (SIS Act) to include a new retirement income covenant that would require trustees to develop a retirement income strategy for beneficiaries who are retired/approaching retirement.
- The Bill was referred to a Senate Economics Legislation Committee, for report by 3 February 2022.

The Committee has recommended that the Bill be passed

- The report recommends that the Bill 'be passed as soon as practicable in order to provide certainty to stakeholders working towards the 1 July 2022 deadline for implementation of the CCIV and the retirement income covenant'.
- The report makes clear that the Recommendation is made on the understanding that:

  'that there would be ongoing conversations about proposed improvements and enhancements if the Bill were to pass to ensure the CCIV remains a competitive corporate structure and the retirement income covenant provides flexibility for trustees assisting their members'.

Views on the proposed regulatory framework for the CCIV regime

- According to the report, there was 'overwhelming support' from stakeholders for the proposed CCIV regime, though some submissions suggested enhancements relating to the proposed taxation framework (which the Committee did not consider needed to be included).
- Broadly, the Committee's view is that the intent of the proposed CCIV regime would be met - 'the intent of the bill, to increase the international competitiveness of Australia's managed fund industry, would be met as CCIVs share the characteristics of other internationally recognised investment structures'.

Views on the proposed Retirement Income Covenant

- On the retirement income covenant, the Committee also noted the 'strong support' from stakeholders for the introduction of the proposed covenant (though several submissions suggested 'improvements').
- The report appears to dismiss concerns about potential implementation challenges:

    'Regarding issues raised by submitters when formulating and giving effect to their strategy, the committee is confident that trustees can fulfil the requirements of the covenant and create effective retirement income strategies without providing financial advice or breaching anti-hawking laws.
    Further, the committee understands that Treasury's Review of the quality of financial advice consultation process will explore the issue of whether financial advice concepts could be simplified'.

  [Source: Senate Standing Committee on Economics Inquiry: Corporate Collective Investment Vehicle Framework and Other Measures Bill 2021 [Provisions] Final Report]

CALC has called for the expansion of the draft terms of reference for the planned Quality of Advice Review to include consideration of conflicted remuneration

Context

- On 16 December 2021, the government commenced consultation on proposed draft terms of reference for the planned 'Quality of Advice' Review which is due to be completed in 2022. You can find a brief overview of the draft Terms of Reference in Governance News 25/01/2022 at p21
- The review proposes to implement the government's response to three Hayne recommendations: Recommendations 2.3, 2.5 and 2.6. In addition, it's proposed that the review will also consider recent reforms which introduced annual renewal for ongoing fee arrangements (Recommendation 2.1).
- The government identifies ensuring access to affordable, high quality financial advice as the key aim of the review. Streamlining regulatory requirements/lessening the existing costs/compliance burden on advisers is presented as an important aspect of achieving this aim. Announcing the review, Minister for Superannuation, Financial Services and the Digital Economy Jane Hume said:

  'the Quality of Advice Review aims to identify opportunities to streamline and simplify regulatory compliance obligations to reduce cost and remove duplication, recognising that costs of compliance by businesses are ultimately borne by consumers.

- The due date for submissions was 4 February 2022.

Call for the terms of reference to be expanded

The Consumer Action Law Centre's (CALC) submission queries whether the draft terms of reference, as currently drafted, respond to Hayne Recommendations 2.3, 2.5 and 2.6 given they do not explicitly reference consideration of conflicted remuneration. The submission states:

> 'the Advice Review cannot be said to be meaningfully implementing these recommendations without considering Commissioner Hayne's commentary on the conflicts between interest and duty in financial services. These findings, and the evidence at the Royal Commission of atrocious sales behaviour motivated by commissions and incentives, appear to have been forgotten in the drafting of the TOR, which make no reference to these issues. Treasury's landing page for the Advice Review makes no reference to 'conflicted remuneration' or even 'insurance'. A casual reader may not discern that the Advice Review purports to implement Commissioner Hayne's recommendations to review conflicted remuneration in life and general insurance'.

The submission argues that in order to 'properly implement' the Hayne Recommendations, the Terms of Reference for the Review 'must have regard to the evidence for the Royal Commission and the commentary in its reports'.

To address these , the submission calls for the Review to both:

- 'have regard to the findings and commentary of the Financial Services Royal Commission regarding conflicts between duty and interest in financial services and advice, and the benefits of removing all forms of conflicted remuneration'; and
- 'have regard to the need to ensure good consumer outcomes and preventing misconduct and harm'.

[Sources: CALC media release 03/02/2022; CALC Submission: Quality of Financial Advice Review – Draft Terms of Reference]

SAFAA has called for the draft terms of reference for the planned Quality of Advice Review to be revised to focus on the 'full range' of financial advice services

The Stockbrokers and Financial Advisers Association (SAFAA) submission on the draft terms of reference for the planned Quality of Advice review is 'supportive' of the draft terms of reference (TOR), which it describes as 'both comprehensive and broad'.

However, the submission raises concerns that as currently drafted, the draft TOR may lead to the review placing too much focus on financial planning, rather than the full financial advice process.

The submission states:

> 'We consider that regulators and government have often applied a financial planning lens to the financial advice process to the disadvantage of stockbrokers and investment advice firms and their clients, as well as other specialised advice services. Consumers want different advice for different needs and the regulatory environment must accommodate consumer preferences and requirements. It is important that regulators and government understand the way the stockbroking and investment advice industry works and don't seek to shoehorn all consumers into the one advice service.
>
> The issues resulting from a 'one-size-fits-all approach' to financial advice have created undesirable and unintended consequences'.

In illustration, of this, the submission points to the issues with the approach taken by the Financial Adviser Standards and Ethics Authority (FASEA) to the education standards and Code of Ethics (which were administered by FASEA until 1 January 2022).

In light of these concerns, SAFAA recommends that:

- the TOR be expanded to include 'consideration of how the regulatory framework could better enable the provision of the full range of financial advice, not just financial planning advice'
- references in the TOR to 'retail clients' be replaced with the term 'retail investors'. SAFAA considers that this clarification will ensure that 'the full range of clients are considered in the review'. ensure that the review

[Source: SAFAA submission: Quality of Financial Advice Review – Draft Terms of Reference]

Danske Bank to cut its fossil fuel lending by 50% by 2030

- Danske Bank has announced interim 2030 targets for CO2 reduction across the three highest emitting sectors in its loan portfolio – shipping, energy utilities and oil and gas production - as a stepping stone to meeting its net zero 2050 ambition.
- A key commitment is the commitment by the lender to reduce its lending to oil and gas production businesses by 50% (across the loan portfolio as a whole, as against a 2020 baseline) by 2030.
- The 2030 target for shipping is a 20-30% reduction in emissions per unit transported. The bank plans to provide 'transition finance' to shipping customers to enable them replace old vessels with more efficient ones eg vessels that run on 'alternative fuel technologies'.
- For energy utilities companies, the 2030 target is a 30% reduction in carbon emissions per kWh of power and heat generation has been set.
- Danske Bank has said that it intends to introduce targets for other sectors eg agriculture, housing and heavy industry one 'the data quality for these sectors improves'. The bank expects to be able to publish some targets later in the year.

[Source: Danske Bank media release 02/02/2022]

In Brief | Hayne case study: RI Advice Group Pty Ltd has been ordered by the Federal Court to pay a $6 million penalty for failing to take reasonable steps to ensure that its authorised representative provided appropriate financial advice, acted in his clients' best interests; and put clients' interests ahead of his own. ASIC Deputy Chair Sarah Court commented that the penalty 'sends a strong message to financial services licensees to properly monitor the advice given by their advisers to make sure consumers are protected.'

[Source: ASIC media release 03/02/2022]

Risk Management

Top Story | Report finds ASX 300 companies are 'lagging' on modern slavery, suggests investors are crucial to driving improvement

Joint Monash University Centre for Financial Studies (MCFS) and ISS ESG analysis of mandatory reporting under the Modern Slavery Act 2018 (Cth) by ASX 300 companies highlights three key areas where disclosure is 'lagging'. The report also emphasises the crucial role that investors can play in driving improvement through their engagement with companies on the issue.

Key Takeouts

- The report pinpoints three key areas where ASX 300 companies need to 'make progress to bring their modern slavery response in line with the government's best practice guidance, and to move beyond compliance to leading practice'. Namely: 1) disclosure of operational risks; 2) disclosure of risks in their extended supply chains (below Tier 1); and 3) disclosure around their approach to remediation.
- In addition to flagging weaknesses in current reporting, the report flags the critical role that investors could play in driving improvements in corporate practice (and ultimately in tackling modern slavery) – especially in the absence of fines for non-compliance - through pushing for progress on the three issues identified in the report.
- The report suggests investors consider using the three areas for improvement identified, to inform their forthcoming engagements with companies.

Overview: New report pinpoints key areas for improvement in MSA disclosure

Joint analysis from Monash University Centre for Financial Studies (MCFS) and ISS ESG has identified that modern slavery reporting by ASX 300 companies under Modern Slavery Act 2018 (Cth) (MSA) is 'lagging' in three key respects (outlined briefly below). The report urges investors, as 'the main mechanism for driving improvements in corporate practice' in this context, to focus on these areas in their forthcoming engagements with companies to lift standards.

Three key areas for improvement

A comprehensive review of MSA reporting across ASX 200 companies released by the Australian Council of Superannuation Investors (ACSI) in 2021, concluded that companies are essentially engaged in a 'race to the middle' when it comes to MSA reporting – that is, while most reports are technically 'compliant', the majority do not include meaningful information about modern slavery risk and how it is managed in their supply chains.

This report, which looks at reporting across the ASX 300, adds to the broader picture of MSA reporting and pinpoints three key areas for improvement.

1. Operational-level risks 'tend to be overlooked'

- The report found that operational level modern slavery risks 'tend to be overlooked' by companies, with a 'significant discrepancy' between companies' own assessment of their risk (as disclosed in MSA statements) vs the external assessment of their risk by ISS ESG. For example, ISS ESG concluded that 41% of the ASX 300 companies assessed have operations in countries considered at high risk of modern slavery, but only 4% of companies self-described their risk as high in their MSA statements.
- This gap was found to be particularly marked in the professional services sectors (eg Financial and Communication Services sectors). For example it's suggested that operational risks in areas such as cleaning/security, offshored services etc are being overlooked.

2. Lack of transparency around the risks in 'extended supply chains'

- The report observes that vast majority (76%) of modern slavery issues occur in global supply chains. However, the researchers found that reporting by companies on their extended supply chains remains limited.
- Specifically, the report found that while the majority of MSA statements reviewed provided details of Tier 1 suppliers (direct suppliers), 59% of statements did not disclose whether the company's supply chain disclosure extended beyond Tier 1, to include indirect suppliers (where research indicates that modern slavery risks could be higher).

- In terms of the steps/actions companies can take to improve their limited visibility in this context, the report suggests that companies adopt a 'systematic approach to supplier risk assessments and management'. This could include, it's suggested, implementing a supply chain risk management framework geared toward the identification, assessment and mitigation of risk across the extended supply chain (a suggested model is briefly outlined at page 9 of the report). It's also suggested that companies monitor their management of supply chain risks through the introduction of modern slavery specific key performance indicators (KPIs). The report observes that of the 18% of companies currently using KPIs for this purpose, the most common metrics used included (among others): supplier auditing, 'modification of supplier contracts', 'supplier survey response rate', 'reported incidents', and 'corrective actions'.

3. Comprehensive disclosure of remediation processes

The report found that

> 'typically, companies are hesitant to admit responsibility, invest resources, and build strong relationships with suppliers, expert stakeholders, workers, and their representatives – all elements of effective remedy'.

For example, the report found that almost half of ASX 300 companies do not describe remediation processes in their modern slavery statement.

Of the 51% of ASX 300 companies that do so, the disclosure provided was found to be less than comprehensive. For example, 80% of MSA disclosures that described remediation processes referenced whistleblower policies, but only 32% described grievance mechanisms/how grievance mechanisms had been implemented.

The report considers that 'substantive remediation' may need to go further than this to also include for example: a public apology, compensation for loss of income/opportunities, and a guarantee that there will be no recurrence.

Investors could play a key role in pushing companies to lift standards

Consistent with ACSI's previous findings (flagged above), the report argues that rather than driving a 'race to the top' in terms of improved practices, Australia's mandatory disclosure regime has in practice resulted in a 'race to the middle approach' – that is, companies are 'ticking the box to meet the legal requirements of the MSA without seeking to take the lead in addressing modern slavery'. This leads the researchers to query the effectiveness of the design of existing regime.

> 'The key gaps in modern slavery reporting and performance outlined in this report…call into question the effectiveness of the mandatory disclosure legislation model. Not only do these gaps challenge the MSA's intention to incentivise best practice, they also suggest that most S&P/ASX 300 companies are not taking their responsibilities to rights-holders seriously in their operations and supply chains. Without transparent disclosure on the effectiveness of mechanisms to address the root causes of exploitative labour, simple disclosure can provide a sense of "action" at the same time as undermining meaningful progress on modern slavery'.

The report argues that investors have a key role to play in improving corporate practice under the current regime in Australia – especially in the absence of fines for non-compliance - through pushing for improvements in practice. With this in mind, the report suggests that investors use the three improvement areas highlighted in the report to inform and focus their engagements with companies.

The report observes that globally, the issue is becoming a focus area for investor engagement with companies, and that there are signs that it is also gaining traction in Australia. For example, the Investors Against Slavery and Trafficking Asia-Pacific Initiative aims to exert pressure on companies to ensure that their MSA reporting is effective.

[Sources: Driving Improvements in Modern Slavery Reporting: The Role for Australian Investors]

In Brief | 'We say sorry': Formal apologies have been made in both Houses of Parliament to people who have experienced bullying, sexual harassment or sexual assault while working for the federal government. The statement also confirmed that 'We are fully committed to working across the Parliament to implement all of these recommendations within the timeframes proposed by Commissioner Jenkins'

[Sources: House of Representatives: Statement of Acknowledgement – Statement by the Speaker (Live Minutes 12:01:52pm); Senate: Statement by President—Independent Review into Commonwealth Parliamentary Workplaces]

Other News

Productivity Review: Productivity Commission tasked with identifying an 'actionable roadmap' to boost Australia's productivity

Treasurer Josh Frydenberg has announced that the Productivity Commission has been tasked with completing the second five yearly review of Australia's productivity performance and with providing the government with 'an actional roadmap to assist' in making 'productivity enhancing reforms' within 12 months.

According to the Terms of Reference, every recommendation is expected to 'qualitatively and quantitatively estimate the benefit of making the reform and identify an owner for the action and a timeframe in which it might occur'.

Terms of Reference

The Productivity Commission has been tasked with:

- Analysing 'Australia's productivity performance in both the market and non-market sectors, including an assessment of the settings for productive investment in human and physical capital and how they can be improved to lift productivity'.
- Identifying 'forces shaping Australia's productivity challenge as a result of the COVID-19 pandemic and policy response'.

- Considering 'the opportunities created for improvements in productivity as a result of Australia's COVID-19 experience, especially through changes in Australia's labour markets, delivery of services (including retail, health and education) and digital adoption'.
- Identifying 'priority sectors for reform (including but not limited to data and digital innovation and workforce skills) and benchmark Australian priority sectors against international comparators to quantify the required improvement'.
- Examining 'the factors that may have affected productivity growth, including domestic and global factors and an assessment of the impact of major policy changes, if relevant'.
- Prioritising and quantifying 'the benefit of potential policy changes to improve Australian economic performance and the wellbeing of Australians by supporting greater productivity growth to set out a roadmap for reform'.
- Revisiting key recommendations and themes from the 2017 Shifting the Dial report, in light of the above, 'where relevant.'

In addition, the Productivity Commission is expected to 'have regard to' other reviews commissioned by Australian governments 'relating to Australia's productivity performance' as well as include 'comparisons of Australia's productivity performance with other comparable countries'.

Process and Timing

- The Productivity Commission is expected to 'undertake appropriate public consultation processes' including inviting 'public submissions'.
- 'Initial submissions' are due by 23 March 2022.
- The Productivity Commission is expected to provide its final report to the government 'within 12 months' ie by February 2023.

[Source: Treasurer Josh Frydenberg media release 07/07/2022; Productivity Commission, Productivity Inquiry, Terms of Reference]

In Brief | Treasury has released a working paper highlighting that Australian firms are slower to adopt 'cutting edge technologies and processes' and to catch up to world-leading 'frontier firms' than they have been in the past. The paper suggests that the slowdown may 'reflect weaker incentives and imperatives for firms to improve…[indicating that] policies to address barriers to business dynamism and competitive pressures can improve Australia's productivity performance, by increasing incentives for firms to adopt, innovate and improve'.

[Source: Treasury working paper: Reaching for the stars: Australian firms and the global productivity frontier]

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