Governance News

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

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Contents

Diversity

Five ways leaders can support gender inclusion in their workplace: New guidance from the Champions of Change coalition

The Champions of Change coalition has released a new report highlighting how power – ie both individual power and organisational/societal systems and structures – impact gender equality/gender inclusivity in the workplace.

The central message is that by understanding these structural barriers in the context of their own role as leaders, leaders have potential to accelerate progress through either harnessing or where necessary, 'disrupting systems of personal and organisation power that may be impeding progress'.

The paper states:

> 'by discussing these issues openly, we believe we can strengthen the systems of power that support inclusive gender equality, disrupt those that don't, and tap into the types of power that have traditionally been undervalued to accelerate change'.

Five practical steps for leaders

This paper provides an overview of the structural barriers to gender inclusive workplaces flagged above, and outlines five practical actions leaders can take to:

> 'better understand and use their power to help achieve inclusive gender equality in their organisations and in the community more broadly'.

These are outlined briefly in the table below.

FIVE ACTIONS TO SUPPORT GENDER INCLUSIVITY	WHY/HOW
▪ Leaders understanding their own pathway to power	▪ The report challenges leaders to consider how they attained the personal power they hold an identify the role of systemic/organisational systems of power in their advancement. This might take the form, for example of 'green lights' to advancement ie 'where doors open because of attributes like race, gender, education and networks'. Page 13 of the report includes a table setting out a number of examples of these 'green lights' in more detail. ▪ The report suggests that leaders sharing personal experiences of how they gained their position ('with or without the assistance of green lights') may have a number of benefits in terms of supporting/advancing inclusivity in the workplace including: – creating 'opportunity for discussion about real or perceived barriers to power' – helping 'others to better understand different perspectives, and constructively challenge your own views' – challenging the assumption that existing systems are necessarily 'fair' (the idea of meritocracy) by demonstrating 'that access to traditional power structures, networks and/or career trajectories are not necessarily prerequisites for leadership positions'.
▪ 'Understand how others perceive your use of power'	▪ The report encourages leaders to participate in a 'leadership shadow exercise' – to seek feedback from a range of people within the organisation 'on what they say, how they act, what they prioritise and how they measure' – to: – better understand the impact of their intentional/unintentional actions/behaviour on others; – to invite stakeholders to make leaders accountable for their actions and progress' – 'reinforce the notion that unless leaders are aware of their power and its impact, they risk unconsciously misusing it'.

FIVE ACTIONS TO SUPPORT GENDER INCLUSIVITY	WHY/HOW
▪ 'Consider how and who you are empowering'	▪ The report encourages leaders to reflect on 'on how – and with whom – you enable and share power' as a means of: – challenging 'affinity bias' – highlighting 'green lights' that may be being offered to some people over others – enhancing leaders' 'understanding of talent' or 'merit' within their organisation
▪ 'Understand the types of personal power used in your organisation and how they impact gender equality'	▪ The report comments that: 'Organisations' function, context and strategies tend to reward and reinforce the use of particular types of personal power'. ▪ The report encourages leaders to be conscious of how formal and informal power is used within their organisation as a necessary step towards understanding how it can inhibit/advance inclusive gender equality. The tables at pages 18-20 of the report give examples of how personal power could be used to advance/inhibit gender inclusivity in a range of contexts.
▪ 'Challenge organisational systems, structures, processes and cultures to ensure they empower employees equally'	▪ The report also encourages leaders to think about how barriers to gender inclusivity are 'baked into' existing processes/systems/decision making and to move towards change. The report observes these barriers may take the form of 'seemingly small decisions' on a range of issues, that nonetheless, reinforce existing inequality. Among the examples of this listed in the report are job descriptions that list 'senior, long-term experience' in male-dominated sectors. ▪ The report underlines the importance of 'applying user-centred organisational design at the outset (or through purposeful review) to advance inclusive gender equality'. ▪ In terms of the form that this might take, cites a number of examples of the steps Coalition members are taking to move away from 'overly prescriptive and unintentionally exclusionary practices to principle-based, inclusive, human-centred approaches'. These include: – adopting 'location-agnostic work' to facilitate access to a broader talent pool – increased transparency in remuneration 'which supports pay equity and enables us to attract appropriate candidates in a competitive skills market' – 'increased transparency and accountability about action to address harmful behaviour in the workplace' ▪ Importantly, the report underlines that the 'emerging practices' highlighted above 'do not necessarily constitute changes to individual employees' entitlements or create increased industrial complexity or administration' but instead 'empower' employees in a range of ways that position organisations to harness the benefits of diversity and inclusion. ▪ The report states that: 'Empowering all employees through organisational system, structure and process design will: – support the attraction, retention and promotion of a larger pool of more diverse talent – increase employee engagement and performance, and reduce organisational risks'.

[Source: Champions of Change media release 17/06/2023; Full text report: Power to create inclusive gender equality in the workplace]

Remuneration

UK executive pay debate | How should companies set executive pay?

Call to pay executives more (in line with US peers)

- A statement published on the London Stock Exchange (LSE) website in May 2023 from LSE CEO Julia Hoggett suggested that the cost of UK companies attracting and retaining gifted leaders may be to offer them larger and more globally competitive pay packets. Ms Hoggett called for a 'big tent' conversation on the issue with all stakeholders ie listed company Chairs, Founders of potentially listed companies, Asset Managers and Owners, the Financial Reporting Council, the Investment Association, other investee groups. Ms Hoggett stated:

> 'It is essential to have a constructive discussion with all stakeholders about a topic that tends to generate emotion and strong views. If the UK capital markets community chooses to remain on the current path, the consequences of that decision should be explicitly recognised and accepted….We are at a pivotal moment. We should be encouraging and supporting UK companies to compete for talent on a global basis, so we remain an attractive place for companies to base themselves, stay and grow. The alternative is we continue standing idly by as our biggest exports become skills, talent, tax revenue and the companies that generate it'.

No justification for raising pay?

- In response to Ms Hoggett's comments, the High Pay Centre issued a statement arguing there is no justification for raising CEO pay, especially given the current cost of living crisis. The High Pay Centre's position is that encouraging employers to increase spending on executive pay could in fact further exacerbate cost of living pressure on workers, as if companies increase executive wages they would have less money 'left over for their wider workforce'.
- The High Pay Centre suggests that if UK companies are finding it difficult to attract suitable leaders it may be a question of revisiting educational requirements/training, rather than increasing executive pay:

  'If UK companies really are struggling to find high calibre senior managers, that is perhaps a reflection of their training and development processes. There is certainly no shortage of people willing to work for £3.4m and there are hundreds of thousands of business and management graduates in the UK. The pipeline of potential future leaders is something boards and investors can address directly, unlike the constraints on their capacity to blow football transfer-style sums of money on their CEOs, and would be a better focus for their energies'.

Broader context

- Research from Insightia suggests that executive pay in the UK has reached record levels – according to the report, in 2022 total pay for CEOs of FTSE 350 companies averaged £3.03m (up from £2.6m in 2021). Insightia also found that the approval rate for 'say on pay' proposals during Q1 2023 has fallen from an average of 93.5% in 2020/21 to 92.5%.
- Looking at vote results so far this year, there are signs that the issue is a particular concern this year for investors. For example, Ms Hoggett's comments followed the recent 'pay revolt' at Unilever which saw 58% of shareholders vote down the company's remuneration report.
- Ms Hoggett's comments also follow recent moves to loosen the UK Listing Rules to remove barriers to companies electing to list in the UK/stem the tide of companies electing to list elsewhere.

How should companies approach setting executive pay?

Against this background, Roger Barker (Director of policy and corporate governance) at the UK Institute of Directors has released an article (through LinkedIn here) acknowledging the challenges facing UK companies in setting executive pay, and the difference between what UK executives are paid vs their US counterparts.

The article also underlines the reputational risks companies may face if they are perceived by investors to be awarding overly generous pay to executives (without sufficient justification) including 'pay revolts' by shareholders.

Though Dr Barker observes that 'best practice is largely silent when it comes to defining the appropriate amount of total remuneration', and the article offers no insight into what the appropriate amount might be, it does offer a brief precis of the 'factors' Dr Barker/the IoD considers boards should consider in this context.

These include:

- ensuring that the pay-setting process is driven by independent non-executive directors – ie 'no one should be involved in setting their own pay'
- ensuring employment contracts allow the company to claw back/withhold payments or share awards for poor performance or where 'misconduct comes to light'
- ensuring pay is aligned with the company's performance – Dr Barker observes that it may be reputationally challenging for companies if executives are branded 'fat cat bosses after banking huge rewards for failure, following an average – or worse, underperforming year for the business'
- considering executive pay in the context of both:
  - what is being awarded to the wider workforce (in line with the requirements in the UK Corporate Governance Code); and
  - with investor expectations that pay is aligned with other ESG criteria
- whether pay is incentivising the 'right kind of performance and behaviour' from the management team

  [Source: LSE media release: We need a constructive discussion on the UK's approach to executive compensation; High Pay Centre media release 09/05/2023; Dr Barker LinkedIn post: https://www.linkedin.com/posts/institute-of-directors_governance-explainer-executive-pay-activity-7076551162501459968-ij2Y?utm_source=share&utm_medium=member_desktop]

Shareholder Activism

Climate Action 100+ flagged lobbying proposal at Toyota secures 15% shareholder backing

- A shareholder climate lobbying resolution (Proposal 4 in the Notice, full text of the proposal here) – filed by three investors: Danish pension fund, AkademikerPension (US$20 bn in AUM), Norwegian financial services company, Storebrand Asset Management (US$120 bn in AUM), and Dutch pension investment company, APG Asset Management (US$600 bn AUM) – secured 15.06% support at carmaker Toyota Motor Corporation's 14 June 2023 AGM.
- The proposal called for the following provision to be added to the company's Articles of Incorporation:

  'The Company shall conduct a comprehensive, annual review and issue a report…describing if, and how, the Company's climate-related lobbying activities (direct and through industry associations), including public statements, serve to reduce risks for the Company from climate change and how they align with the goals of the Paris Agreement and the Company's goal of carbon neutrality by 2050. The report should disclose any instances of misalignment with those goals, along with the planned actions to address these.'

- Investors state that the proposal was filed after 'over two years of intense engagement' with the company failed to secure (what they consider to be) sufficient progress towards aligning both Toyota's strategy and indirect lobbying efforts (ie through business associations such as Keidanren and JAMA) with the goals of the Paris Agreement. Anders Schelde, Chief Investment Officer (CIO) at AkademikerPension commented:

  'From an investment perspective, we're concerned that Toyota is missing out on profits from soaring EV sales, jeopardising its valuable brand, and cementing its global laggard status. We welcomed the dialogue and annual disclosure but we need concrete policy changes and a better annual review drawing on independent data to calm international investors.'

- The proposal was flagged by Climate Action 100+ ahead of the meeting.
- The Toyota board issued an 'against' recommendation ahead of the meeting. In addition to pointing to the climate measures/initiatives and disclosure already in place/being provided, which the board considers to be sufficient, the board also opposed the proposal because it considers it inappropriate for the company's articles of association to be amended in the manner requested. The board states:

  '…the role of TMC's Board of Directors to address these issues is to make flexible and varying decisions according to the circumstances at the time, make agile changes as required, and swiftly turn decisions into action. Thus, the ideal state of disclosure is subject to sudden change as well. Generally, the articles of incorporation are intended to define the basic details of a corporation and its operation, and is not for stipulating matters related to specific business execution such as those in this shareholder proposal. Therefore, we would like to maintain our current Articles of Incorporation'.

How investors voted

- The proposal had the backing of a number of investors: CalPERS (a co-lead on the Climate Action 100+ Toyota Motor Corporation engagement), AP7, Anima Sgr and Local Tapiola Asset Management Ltd predeclared their intention to support the proposal Legal and General Investment Management also backed the proposal. CalSTRS also voted in support.
- However, perhaps unsurprisingly given the vote result, other larger investors do not appear to have given it their support. For example Norges Bank Investment Management (NBIM) voted against.

Chair re-election

Toyota Chair Akio Toyoda was reelected as Chair with 85% support (this is down on the 96% vote last year).

Looking at the justifications given by some investors for their 'against' votes, investors cite a range of reasons including concerns about: independence, climate action, diversity and accountability. For example:

- CalPERS pre-declared its intention to vote against Mr Toyoda's reelection. As well as against the reelection of seven other directors on independence grounds – fewer than 50% of the board is considered to be independent.

- Legal and General Investment Management (LGIM) also cited concerns about lack of overall board independence among its reasons for voting against Mr Toyoda's reelection as Chair. LGIM states:

  'A vote against is applied due to the lack of independent directors on the board. Independent directors bring an external perspective to the board. Bringing relevant and suitably diverse mix of skills and perspectives is critical to the quality of the board and the strategic direction of the company. We would like to see all companies have a third of the board comprising truly independent outside directors'.

In addition, LGIM voted against due to: 'lack of meaningful diversity on the board', and accountability – specifically that 'the company has not provided disclosure surrounding the use of former CEO as Advisor to the board'.

  'A vote against is applied due to the lack of meaningful diversity on the board. Accountability: A vote against has been applied as the Company has not provided disclosure surrounding the use of former CEO as Advisor to the Board'.

LGIM also voted against the election of four other directors on independence grounds.

- Storebrand also voted against Mr Toyoda's reelection. The justification given is that: 'the nominee is a top executive and the company is not aligned with investor expectations on net zero by 2050 targets and commitments'. Storebrand voted in support of all other directors standing for reelection.

  [Sources: Storebrand media release 10/05/2023; Results of meeting]

Scope 3 proposal at Builders FirstSource secures 21% support (following majority vote on a similar proposal last year)

- A shareholder proposal (proposal 5 in the Notice, filed by Green Century) calling on building product supplier Builders FirstSource to set short, medium and long-term science based GHG targets across its entire value chain in line with achieving net zero emissions by 2050, secured approximately 21% support at the annual shareholder meeting.
- The board recommended shareholders reject the proposal ahead of the meeting, chiefly because it considered the request to be 'unnecessary'. The board pointed to the company's existing commitment to set short, medium and long term Scope 1 and 2 targets by 'no later than 2025 in support of this. The board further submitted that committing to set Scope 3 targets as requested in the proposal is 'premature'. The board explains:

> 'the processes and methodologies for calculating Scope 3 emissions (and validating targets in respect thereof) are not well established and continue to evolve. In particular, even the GHG Protocol is developing a Land Sector and Removals Guidance to provide the needed accurate and consistent accounting standard to quantify GHG emissions from land use and land use change. Until the GHG Protocol Land Sector and Removals Guidance is finalized, it is not reasonable to expect us to "fully account for emissions linked to the harvesting and manufacturing of wood products" or to set Scope 3 targets'. .

Some success? Green Century considers that the majority vote on a similar proposal last year, coupled with further engagement/re-filing of the proposal this year pushed the company to set Scope 1 and 2 targets

- Responding to the vote outcome, Green Century acknowledged the company's commitment to set Scope 1 and 2 targets as a step toward responding to the majority vote on 'nearly identical proposal' (also filed by Green Century) at the company in 2022, but underlined the importance of the company setting Scope 3 targets.
- Douglass Guernsey, shareholder advocate at Green Century commented:

> 'While we appreciate that Builders is now taking action on a part of Green Century's 2022 proposal, the company has not yet measured, disclosed, or set targets for its Scope 3, or supply chain emissions, leaving investors in the dark for what comprises, on average, 75% of companies' climate emissions'.

How did investors vote?

- Despite the drop in the level of support for the 2023 proposal as compared with last year, the proposal nevertheless had the support of a number of investors including: NBIM, LGIM, CalSTRS and CalPERS.

Support for environmental proposals is down on last year

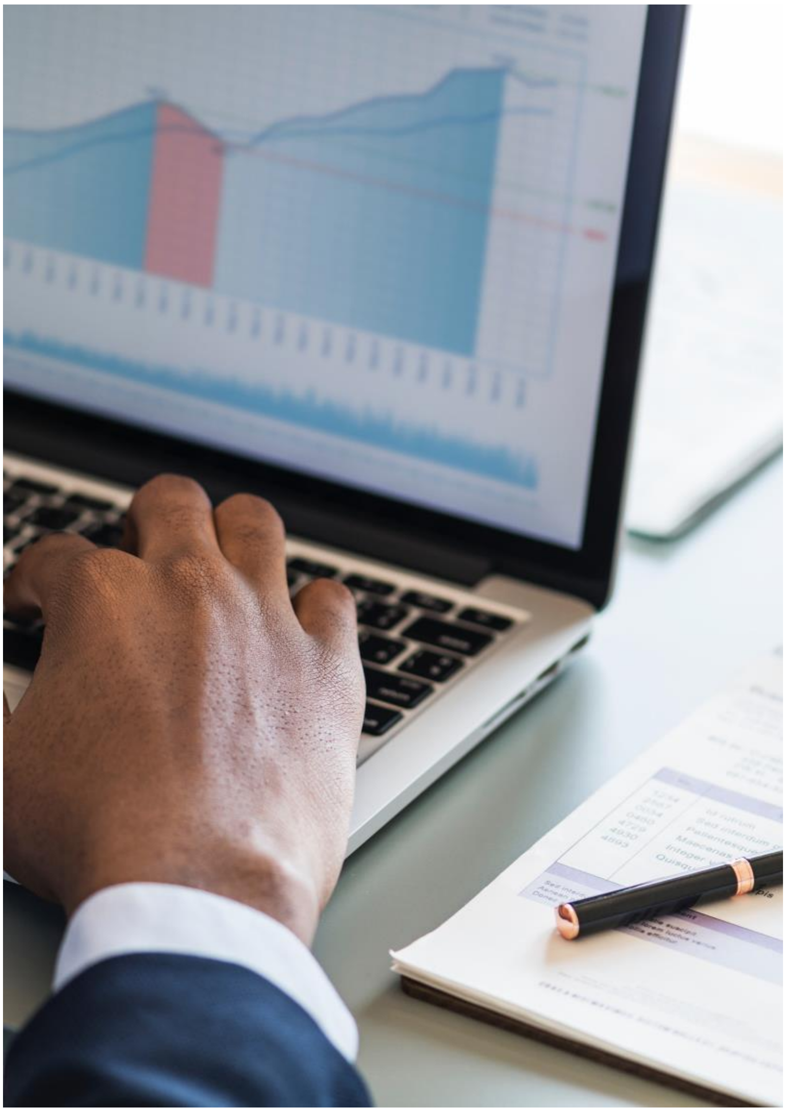
To provide some context for the vote result, research from The Conference Board suggests that support for ESG shareholder proposals is down on last year, with the support for 'environmental' proposals seeing the sharpest drop in support year on year – 34% average support in 2022 vs 21% support in 2023. The Conference Board attributes this to:

> 'the proscriptive nature of some proposals, the steps companies have already taken to address the topics raised by proposals, and major institutional investors taking a more discerning, case-by-case approach in evaluating shareholder proposals as compared to a few years ago'.

[Sources: Builders FirstSource Results of Meeting; Notice of Meeting; Green Century media release 16/06/2023]

Disclosure and Reporting

SEC Climate Disclosure Rule expected October 2023



- US Securities and Exchange Commission (SEC) Chair Gary Gensler announced the release of SEC's Spring 2023 regulatory agenda setting out the SEC's rulemaking priorities over the next 12 months, on 13 June 2023.
- The (indicative) timeline for finalising the long-awaited Climate Change Disclosure rules is October 2023.
- Separately, SEC plans to finalise its proposed Cybersecurity Risk Governance rule in October 2023.

[Sources: SEC Chair Gary Gensler media release 13/06/2023; SEC 2023 regulatory agenda]

Aligning short-term targets with 1.5°C pathways: SBTI consults on new financial sector resources

The Science Based Targets initiative (SBTi) is in the process of developing a Financial Institutions Net Zero (FINZ) Standard. It's envisaged that this will (once finalised) provide guidance to financial institutions on establishing robust short and long-term targets consistent with achieving net zero emissions by 2050.

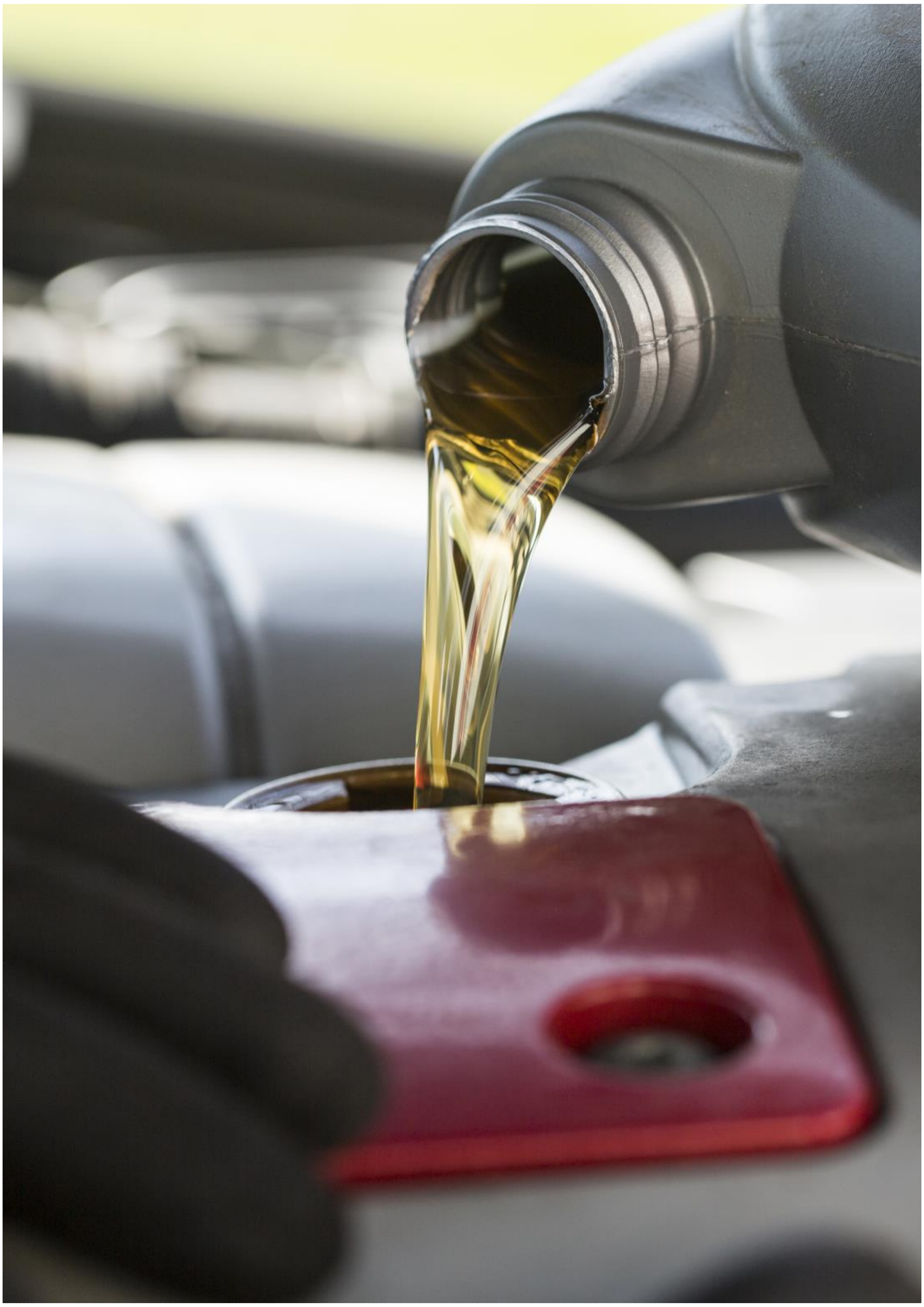
As part of this broader aim, the SBTi has opened a 60 day consultation (15 June 2023 – 14 August 2023) on the following draft resources. The due date for submissions is 14 August 2023.

DRAFT RESOURCES	
▪ [Consultation Draft] SBTi Financial Institutions Net-Zero (FINZ) Standard Conceptual Framework and Initial Criteria for Financial Institutions setting.	The proposed criteria and framework would form the basis of the FINZ standard.
▪ [Consultation Draft] SBTi Near-Term Financial Sector Science Based Targets Guidance V2 ▪ [Consultation Draft] Near-Term Criteria and Recommendations for Financial Institutions Version V2 (this is an excerpt of the full guidance above)	The updates to the guidance are intended to ensure alignment of short-term targets with 1.5°C pathways instead of with 'well-below 2°C pathways'. Appendix G of the guidance document (p193) sets out the proposed changes in detail.

[Source: SBTi media release 15/06/2023]

Institutional Investors and Stewardship

Why Vanguard did not support the shareholder climate proposal at BP



- A shareholder climate resolution (Resolution 25 in the Notice, filed by Follow This (backed by a €1.1 trillion investor coalition) calling on BP to align its 2030 Scope 3 emissions reduction targets with the goals of the Paris Agreement failed to secure the necessary support to be carried at the company's 27 April 2023 shareholder meeting. The resolution secured 16.75% support.
- On 9 June, Vanguard confirmed it did not support the proposal.
- The justification given is that the 'requested action implicated a change in company strategy'. In light of this, as Vanguard 'funds do not seek to direct company strategy…the Vanguard-advised funds did not support the shareholder proposal'.
- Vanguard emphasises that it takes a case by case approach to determining how it will vote on shareholder climate proposals. It is therefore not clear how Vanguard voted on similar proposals filed at Exxon, Chevron, Shell and TotalEnergies.

How other investors voted on the BP proposal

- Legal and General Investment Management (LGIM) also voted 'against', chiefly because of what it considered to be the overly prescriptive/inflexible nature of the demand being made. LGIM states that:

  'Although we support the principles of this proposal, a vote AGAINST is applied as in our view, the wording of the proposal imposes inflexibility on the company that is challenging to justify at the present time, and could lead to unintended consequences as we transition to a net-zero emissions economy. For example, the non-linear nature of the energy transition and the importance of achieving real-world progress to cut emissions. Our approach to such resolutions will remain dynamic given the need for companies to demonstrate clearly how they will be net zero compliant in a transition'.

- A number of other investors also voted against (though their reasons for doing so are not always clear):
  - Ahead of the meeting, Norges Bank Investment Management (NBIM) predeclared its intention to vote (in line with management's recommendation) against the resolution.
  - California Public Employees Retirement System (CalPERS) also voted against.

- In contrast, Storebrand voted in support, stating that:

  'A vote FOR this resolution is considered warranted as the proposal would further aid shareholders in understanding the company's assessment of how it could reduce its carbon footprint in alignment with GHG reductions necessary to achieve the Paris Climate Agreement goal'.

  [Sources: Vanguard voting insight 09/06/2023; BP Results of meeting 27/04/2023]

Why BlackRock recommended 'against' shareholder ESG proposals at Yum! Brands

- BlackRock has issued a vote bulletin explaining its rationale for rejecting all five shareholder ESG proposals included in the Notice of Meeting at the Yum! Brands Inc.
- This is the first time this year that BlackRock has issued a vote bulletin on its vote rationale on ESG-related proposals.
- The proposals covered a range of topics: additional disclosure around the company's plans to reduce single-use plastic packaging, additional disclosure around the company's lobbying activity/expenditure, civil rights audit, share retention by named executive officers, and paid sick leave provisions for franchisee employees.
- In the event, only three of the proposals went to a vote at the meeting and none secured the necessary support to be carried. The table below provides a snapshot of each of the proposals, the vote result and a summary of BlackRock's reasons for voting 'against' in each case.

PROPOSAL	APPROX. SUPPORT	WHY BLACKROCK VOTED AGAINST
Plastic reduction: Item 5 (filed by As You Sow) called on the company to report on 'how the Company will reduce its plastics use by shifting away from single-use packaging in alignment with the findings of the Pew Report, or other authoritative sources, to feasibly reduce ocean pollution'.	36%	BlackRock considers the company's existing disclosure is 'comprehensive and provide sufficient information to allow investors to understand the company's approach to managing the risks of plastic use'
Lobbying disclosure: Item 6 (filed by SOC Investment Group) called on the company to report annually on: '1. YUM's policy and procedures governing its own lobbying, both direct and indirect, and grassroots lobbying communications.	41%	Again, BlackRock considers the company's existing disclosure is sufficient. BlackRock states: 'Yum!'s existing disclosures already provide sufficient transparency on the company's lobbying practices'.

PROPOSAL	APPROX. SUPPORT	WHY BLACKROCK VOTED AGAINST
2. Payments by YUM used for (a) direct or indirect lobbying or (b) grassroots lobbying communications, in each case including the amount of the payment and the recipient. 3. Description of management's decision-making process and the Board's oversight of this process'.		
Civil Rights and Nondiscrimination Audit Report: Item 7 called for board to: 'commission an audit analysing the Company's impacts on civil rights and non-discrimination, and the impacts of those issues on the Company's business'.	N/A	BlackRock states that: 'In considering shareholder proposals requesting an assessment of a company's practices in relation to civil rights and non-discrimination, we take into account the costs of an assessment as well as the benefits of mitigating the economic risk of inadequate policies and practices. In our view, Yum!'s approach to these matters is proportionate to the human capital risks the company has identified. As a result, BIS determined that support for this shareholder proposal was not warranted'.
Disclosure of Share Retention Policies for named executive officers: Item 8 (filed by New York State Common Retirement Fund) called on the company to: 'disclose if, and how, it seeks to require that named executive officers retain a significant percentage of shares acquired through equity compensation programs until reaching normal retirement age'.	N/A	BlackRock's chief reason for not supporting the proposal is that it essentially considers it unnecessary. BlackRock states that it: 'did not support this shareholder proposal because, in our assessment, Yum!'s current stock ownership guidelines for their named executive officers are robust'.
Paid sick leave: Item 9 (filed by United Church Funds) called on the company to issue a report: 'analysing the provision of paid sick leave among franchise employees and assessing the feasibility of inducing or incentivizing franchisees to provide some amount of paid sick leave to all employees'.	20%	BlackRock's chief reason for not supporting the proposal is that it considers it to be 'unduly prescriptive as it seeks to direct the independent operations of the company's franchisees'. BlackRock also considers that Yum!'s existing paid sick leave policy for employees is already robust. BlackRock reiterates that: 'Generally, we are unlikely to support shareholder proposals that, in our assessment, are intended to micromanage companies. This includes those that are unduly prescriptive and constraining on the decision-making of the board or management or call for a change to the company's business model. In our view, this proposal seeks to tell the company, and indirectly the franchisees, which benefits they should offer their employees. In our assessment, Yum!'s approach is appropriate, and we determined it was not in the financial interests of our clients to support this shareholder proposal'.

[Source: BlackRock vote bulletin: Yum! Brands Inc]

IIGCC launches new Asset Owner Stewardship Questionnaire

- Following investor and stakeholder consultation, the Institutional Investors Group on Climate Change (IIGCC) has released a new Asset Owner Stewardship Questionnaire, intended for internal use by asset owners, to assist them in:

  'meeting their own individual net zero goals by incorporating climate stewardship into selection, appointment and monitoring of external asset managers'.

- Specifically, the questionnaire includes:

  'qualitative questions for due diligence when selecting an asset manager, and quantitative reporting when monitoring asset managers'.

- The questionnaire is intended to build on the IGCC's Net Zero Stewardship Toolkit and aligns with the Net Zero Investment Framework to promote consistency on engagement reporting.

  [Source: IIGCC media release 12/06/2023]

IIGCC releases new corporate bondholder guidance

The Institutional Investors Group on Climate Change (IIGCC) has released new guidance - Net Zero Bondholder Stewardship Guidance – focused on publicly listed corporate debt.

The IIGCC states that the guidance is intended to provide corporate bondholders

> 'with a foundational framework to enhance their climate stewardship practices, building on IIGCC's Net Zero Stewardship Toolkit for listed equities and practical steps aligned with the Net Zero Investment Framework (NZIF)'.

The guidance includes:

- A 'Toolkit' for bondholders covering 'debt-specific approaches to effective stewardship across the life of the bond and beyond. This is structured around the following six 'steps' (adapted from the Net Zero Stewardship toolkit):
  1. 'Undertake portfolio analysis, set portfolio alignment goals and develop a stewardship decarbonisation framework
  2. Set net zero alignment criteria, alignment levels and time-bound engagement objectives
  3. Develop an engagement strategy for priority companies
  4. Baseline engagement and voting approach
  5. Asset owner and manager alignment
  6. Transparency'
- 'Guidance on stewardship across different forms of corporate debt, including investment grade, high yield, labelled bonds, private companies (issuing public bonds), securitised issuances and emerging markets'.
- 'Guidance on stewardship across the debt ecosystem, including banks, credit ratings agencies, index providers, industry bodies and regulators'.

  [Sources: IIGCC media releases 15/06/2023; 15/06/2023; Net Zero Bondholder Stewardship Guidance]

ESG

Top Story | ACCC embeds sustainability into 2023-24 Product Safety Priorities

Key Takeouts

- The ACCC has announced its latest move towards embedding sustainability into its broader regulatory approach, announcing that 'sustainability and maintaining product safety' is included among its four product safety priorities for 2023-24
- The ACCC's sustainability taskforce is also set to consider where 'environmental and sustainability issues intersect with the application of competition and consumer law' more broadly
- This is in line with Australian (and overseas) regulators' increasing focus on ESG/sustainability. For example, in Australia:
  - consideration of climate related risk is now an explicit expectation for the Australian Prudential Regulation Authority. Climate risk is included among APRA's key supervisory priorities for 2023
  - similarly, the Australian Securities and Investments Commission (ASIC) Chair Joe Longo has identified the following as key areas of focus:
    - good governance – ensuring ESG is integrated into existing governance frameworks – in preparation for upcoming changes
    - tackling greenwashing (a key enforcement priority)
    - preparing for the growth in sustainable financing.
  - APRA, ASIC, the Reserve Bank of Australia and Treasury, through the Council of Financial Regulators Climate Working Group, have also been engaged since 2017 on 'coordinating actions in relation to understanding and managing financial climate-related risks'.

Our key takeaways from Australian Competition and Consumer Commission (ACCC) Chair Catriona Lowe's 15 June 2023 address to the National Consumer Congress are below.

'Sustainability and maintaining product safety' is included among the regulators four product safety priorities for 2023-24

Among the ACCC's four product safety priorities for 2023-24 is a new priority 'sustainability and maintaining product safety'. This includes plans for the regulator to:

- publish a 'scoping study' on the potential safety hazards associated with lithium-ion batteries, which may ('if required' include proposed risk mitigation strategies.
- consider 'ways to ensure key safety requirements in standards made under the Australian Consumer Law are sufficiently available to successive owners of products'.
- update recall guidelines to cover the circular economy (the ACCC has indicated this is planned to occur over the next 12 months)
- explore the potential development of 'best practices to reduce safety risks from reused or second-hand goods that are sold online'.

The ACCC's sustainability taskforce will coordinate this work (in addition to other sustainability-focused initiatives across the regulator)

The ACCC's other three product safety priorities for 2023-24 are:

- **product safety online including detection and prevention of unsafe product listings** and 'developing best practices to reduce the safety risks from second hand goods sold online' (the ACCC has indicated this is planned to occur over the next 12 months)
- **infant sleep products** with a focus on implementing measures to prevent injuries/deaths associated with infant sleep products
- **young children's product safety** including taking 'appropriate regulatory and enforcement action against businesses' that are not complying with regulatory requirements, improving the effectiveness of product recalls and stepping up consumer awareness activities

Why include 'sustainability and maintaining product safety'?

Ms Lowe summed up why the ACCC has prioritised this as follows:

> 'This is a new priority, reflecting the changing purchasing behaviours of consumers as they seek to be more environmentally conscious and look for more sustainable products. Our work for this priority will involve activities to support consumer confidence in the safety of sustainable products that are helping to underpin Australia's transition to net zero and a circular economy. By making sustainability and maintaining product safety a priority, we're ensuring that we do not perform our product safety functions in a way that creates unnecessary barriers to industry or governments that are pursuing environmental and sustainability objectives'.

Embedding sustainability into the ACCC's broader approach

Ms Lowe underlined that in addition to the work detailed above, the ACCC sustainability taskforce will:

> 'examine a range of issues where environmental and sustainability issues intersect with the application of competition and consumer law. It will also identify the need for competition exemptions for new technologies and maintaining product safety without impeding economic transformation'.

Greenwashing

Ms Lowe reiterated the regulator's continued focus on tackling greenwashing, stating that the ACCC is 'determined to make a real difference in this area'.

Ms Lowe observed that consumer law is only one part of the broader framework needed to address the issue.

This is in line with recent comments from Australian Securities Investments Commission (ASIC) Deputy Commissioner Karen Chester and separately, comments from ASIC Chair Joe Longo, that enforcement of compliance with existing disclosure requirements is only one aspect of the measures necessary, and being progressed, to tackle greenwashing and more broadly, to support the government's net zero by 2050 ambition.

An important development is the expected roll out of new internationally aligned, mandatory disclosure standards which importantly, will go further than the TCFD framework in a number of respects.

In a recent speech, ASIC Chair Joe Longo flagged that Treasury is expected to release a position paper on these standards 'within the next fortnight' which will outline the proposed implementation timeline.

[Source: ACCC Deputy Chair Catriona Lowe, Keynote address to the National Consumer Congress 2023 15/06/2023]

Government consults on principles/objectives proposed to underpin Australia's first health and climate strategy

- The government has announced it is developing a National Health and Climate Strategy to:

  'ensure the nation's health system can meet the needs of Australians in the face of a changing climate'.

- Broadly, it's envisaged that the strategy will establish a roadmap to prepare for the health challenges associated with:
  - more frequent and severe weather events
  - extreme temperatures
  - poor air quality.
- It's also envisaged that the new strategy will identify areas to reduce GHG emissions in the health system.
- The consultation paper seeks views on four proposed objectives and accompanying principles that are planned to underpin the strategy. The four proposed objectives are:
  - Measurement: Measure and report on health system greenhouse gas emissions, to enable progress in reducing emissions to be tracked and quantified
  - Mitigation: Accelerating 'the reduction of greenhouse gas emissions from the health system'
  - Adaption: 'Strengthening the resilience of the health system and communities to anticipate and respond to the health impacts of climate change'.
  - Health in all policies: 'Maximise the synergies between good climate policy and public health policy by working across policy areas to lessen the impact of climate change on the social and cultural determinants of health and wellbeing'.

- You can find a two page summary of the consultation here. A list of consultation questions is included at p37-38 of the consultation paper.
- The due date for submissions is 24 July 2023.

[Source: Department of Health and Aged Care media release 15/06/2023; National Health and Climate Strategy – Consultation 02/06/2023 - 24/07/2023]

Net Zero Agency Chair and Advisory Board announced

- On 5 May 2023, the government announced its plan to legislate a National Net Zero Authority (Authority) to:
  - 'Support workers in emissions-intensive sectors to access new employment, skills and support as the net zero transformation continues.
  - Coordinate programs and policies across government to support regions and communities to attract and take advantage of new clean energy industries and set those industries up for success.
  - Help investors and companies to engage with net zero transformation opportunities'.
- The government also flagged plans to establish a Net Zero Economy Agency to advise on the final design and establishment of the new Authority.
- On 14 June 2023, the Prime Minister announced that Greg Combet (Chair of IFM Investors and Industry Super Australia and former Labor Minister for Climate Change and Energy Efficiency) will chair the Net Zero Economy Agency. Mr Combet will begin the role on 10 July 2023.
- Mr Combet separately announced plans to step down as both: Chair of IFM Investors effective from the close of business on Friday 30 June 2023; and Chair of Industry Super Australia, also effective from 30 June 2023.

- Mr Combet will be supported in his role by an Advisory board. The following 10 people have been appointed as board members:
  - Professor Ross Garnaut AC - Professor Emeritus in Economics at the University of Melbourne and Professor Emeritus, College of Asia & the Pacific at ANU;
  - Professor Paul Simshauser AM – CEO of Powerlink Queensland and Professor of Economics at Griffith University;
  - Anthea Harris – CEO of the Australian Energy Regulator;
  - Nicole Lockwood – Chair of Infrastructure WA, board member of NBN and former Shire President of Roebourne;
  - Kellie Parker – CEO of Rio Tinto Australia;
  - Michele O'Neil – President of the Australian Council of Trade Unions;
  - Professor Robynne Quiggin - Pro-Vice Chancellor of UTS and part of Steering committee for the First Nations Clean Energy Network;
  - Anna Skarbek – CEO of Climateworks Centre, Director of the Green Building Council of Australia, the Centre for New Energy Technologies, Impact Investment Group, and Sentient Impact Group;
  - Tony Maher – General President of the Mining and Energy Union;
  - Laura Tyler – Chief Technical Officer, BHP.
- According to the government's announcement, the appointments were made based on each person's 'significant expertise across a range of areas including workplace relations, energy markets, regional development, First Nations engagement and economic development'.
- Stakeholder reference groups are planned to be established to guide the Agency's work with representatives to include regional experts, to engage with workers, industry and communities about the transition to net zero.

  [Sources: Prime Minister Anthony Albanese media release 14/06/2023; ISA media release 14/06/2023; IFM investors media release 14/06/2023]

New Senate Inquiry into household electrification established

- On 14 June 2023, the Senate referred an inquiry into 'the benefits and constraints of household electrification' to the Senate Economics References Committee for inquiry and report by the last sitting day of 2024
- The Inquiry will consider (among other matters):
  - how electrification can combat energy price inflation
  - the barriers to uptake of home electrification
  - the total upfront cost and longer term benefits as well as 'alternative models for funding and implementation'
  - the 'optimal timeline for household electrification accounting for the likely timing of decarbonising electricity'
  - 'solutions to the economic barriers to electrification for low income households'.
- The full terms of reference are here.

  [Sources: Senator Andrew Bragg media release 14/06/2023; Senate Economic Reference Committee Inquiry: Residential Electrification]

US regulator calls for tipoffs about potential fraud/manipulation in carbon markets

- The US Commodities Futures Trading Commission (CFTC) has called on would-be whistleblowers to report potential fraud and/or manipulation in carbon markets noting that if information received leads to successful enforcement action, whistleblowers may be eligible for monetary rewards.
- The CFTC Director of the Division of Enforcement, Ian McGinley underlined the regulator's continuing focus on ensuring the integrity of carbon credit markets stating:

  'As carbon credit markets continue to grow, we will act to foster the integrity of these markets by fighting fraud and manipulation…Whistleblowers are invaluable allies in these efforts. We will diligently investigate all credible tips and complaints from whistleblowers relating to carbon credit markets.'

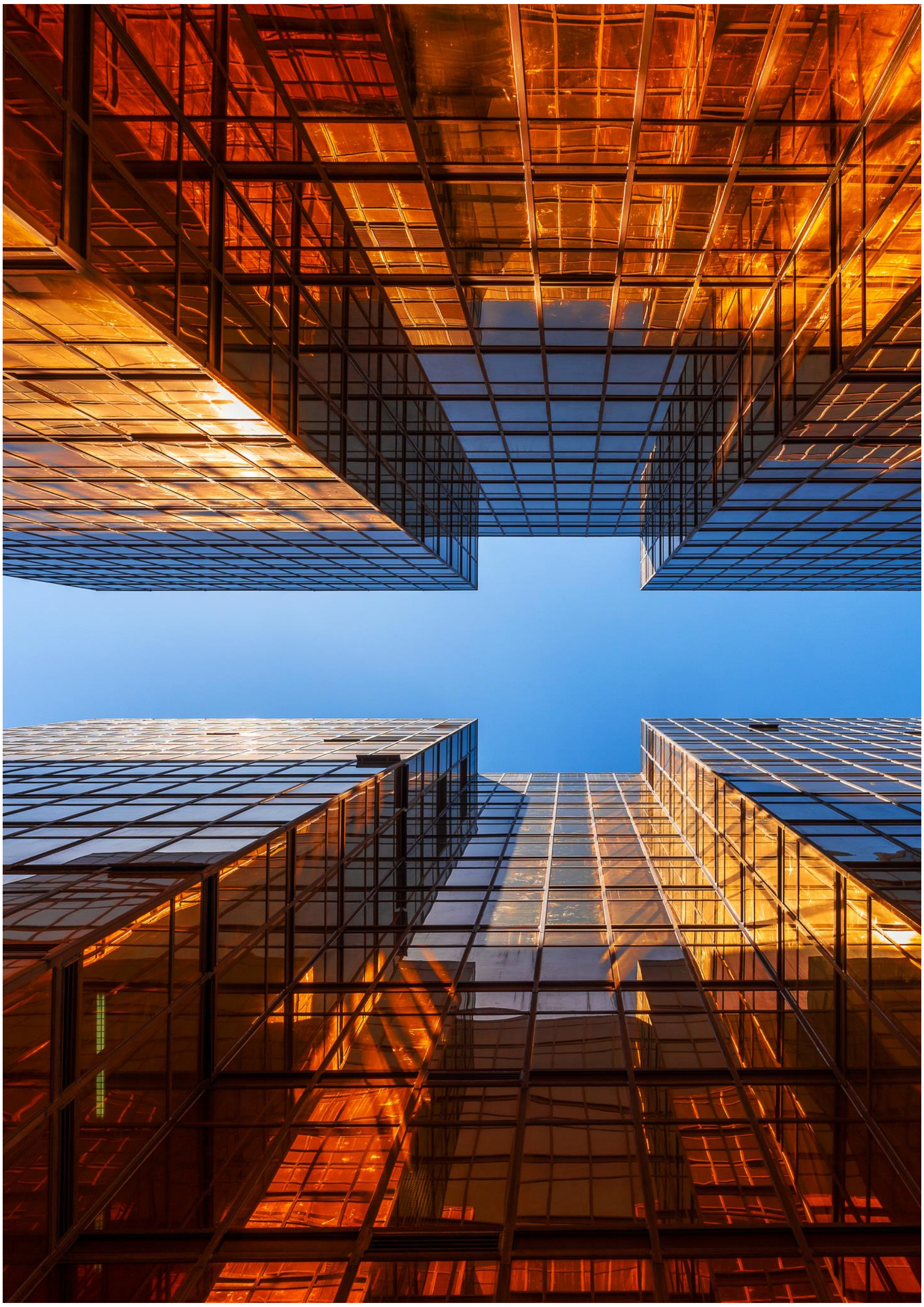
  [Source: CFTC media release 20/06/2023]

Regulators

FRAA consults on draft 'enduring metrics' for assessing regulator effectiveness and capability

- The Financial Regulator Assessment Authority (FRAA) has released a consultation paper seeking feedback on a draft metrics framework for assessing regulator effectiveness and capability.
- Importantly, the draft metrics framework is proposed to supplement (not supersede the FRAA's existing assessment methodology). FRAA states that the draft metrics framework is:

> 'envisaged to form part of the FRAA's broader methodology for evaluating the regulators' effectiveness and capability. The FRAA's operational indicators will remain the primary tool in its assessments. The metrics framework is expected to provide complementary insights to the FRAA's other methods, such as stakeholder liaison, case studies and surveys. In future reviews, the FRAA may draw on those operational indicators and some metrics where relevant to the scope of a review. The FRAA intends to carefully assess where causality is present between regulator activities and financial system outcomes.'



- A proposed list of metrics is set out in Figure 1.4 at p15 of the consultation paper. It's envisaged that these metrics would 'move over time'.
- Page 8 of the Consultation paper sets out 'indicative information' about how the proposed metrics framework could be deployed in future reviews of the regulators.
- FRAA notes that it has not developed targets, other benchmarks or international comparisons for the metrics – though it is 'open to exploring' benchmarks/international comparisons in future. FRAA appears to be opposed to setting targets for the suggested metrics stating that:

  'Setting targets poses challenges alongside the complexity of APRA and ASIC's statutory mandates, stated objectives and activities, and the variety of ways regulatory activity may influence financial system outcomes'.
- FRAA confirms that the draft metrics framework was not used in the FRAA's inaugural review of the Australian Prudential Authority, which is due to be delivered to the government by 30 June 2023.
- FRAA plans to 'continue to refine the metrics framework' ahead of the next review of the Australian Securities and Investments Commission (ASIC).
- The due date for submissions is 27 July 2023.

  [Source: FRAA consultation: Draft Financial System and Regulator Metrics Framework 15 June 2023 – 27 July 2023]

ASIC enforcement | ASIC accused of 'hindering' the senate inquiry into its enforcement approach

- The Liberal Chaired Senate Committee Inquiry into the Australian Securities and Investments Commission's (ASIC) 'capacity and capability' to undertake investigation/enforcement action has published an interim report.
- The report accuses the regulator of 'hinder[ing] the committee's work by refusing to answer questions on notice' and recommends that the Senate 'order the provision of the information sought'.

What reasons has ASIC given for not answering the Committee's questions?

- ASIC has refused to answer (some) of the Committee's questions because it considers that it may not be in the public interest for the information requested to be disclosed – ie ASIC has claimed public interest immunity.
- ASIC has so far made 13 public immunity claims (covering a raft of questions) concerning various ASIC enforcement actions including (among other matters): certain closed investigations by the regulator and questions concerning ASIC's engagement with Senator's offices prior to the commencement of the inquiry.
- The questions over which ASIC has claimed public immunity are listed in Appendix 1 to the report.

Why does the Committee not accept this?

- Broadly, the Committee's view is that while:

  'there may be a good basis for [ASIC] not disclosing detailed information regarding open investigations, ASIC has not made a good case for not disclosing details for cases that have been closed'.
- Accordingly, the Committee has accepted two of ASIC's public immunity claims but has rejected the remainder which (largely) concern matters that ASIC has confirmed are closed.
- The report details the Committee's reasons for rejecting 11 of the 13 ASIC immunity claims.

What happens now?

- The report makes recommendations that the Senate order the provision of the information sought by 18 July.
- The Committee's expectation is that:

  'ASIC takes this as an opportunity to reflect on its conduct to date and to reassess how it will better engage with the committee's inquiry in an open and transparent manner moving forward'
- Chair of the Committee, Liberal Senator Andrew Bragg has issued a statement confirming that the committee intends to hold public hearings 'in coming months'. As yet, no dates are listed.
- A separate Labor-Chaired inquiry into ASIC's capacity and capability to respond to reports of alleged misconduct, established at the same time as the Liberal-Chaired Senate inquiry, has so far not yet issued a call

for submissions or listed any public hearing dates. The Labor-Chaired inquiry's reporting date remains June 2024.

[Sources: Senate Standing Committee on Economics Inquiry: Australian Securities and Investments Commission investigation and enforcement, Interim Report 20/06/2023; Senator Andrew Bragg media release 20/06/2023]

Council of Financial Regulators: Latest quarterly statement released

The Council of Financial Regulators (the Council) - the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), Treasury and the Reserve Bank of Australia (RBA) – has released an overview of the key points of discussion at its 8 June 2023 meeting. The main topics discussed were:

- lessons for Australian regulators in light of 'recent stresses in parts of the international banking system' (eg recent bank failures in the US and Switzerland). Essentially, the CFR's view is that despite the Australian banking system's 'high level of resilience', there is scope to 'further consider crisis preparedness and management arrangements in Australia' and in light of this, the CFR is assessing current 'crisis management settings to ensure they remain robust'. CFR agencies have also reviewed and updated their communication and coordination arrangements.
- the impact of high inflation and interest rates on households, businesses and the financial system:
  - The CFR is continuing to monitor 'the resilience' of households to cost of living pressures and higher rates.
  - The CFR's view is that 'most households are well placed to manage the impact on budgets due to strong labour market conditions and sizeable saving buffers'.
  - The CFR acknowledges that 'some households are experiencing significant pressure on their finances, including those on lower incomes (including many renters) and those with low savings buffers and high levels of debt relative to their income' and flags plans to 'closely monitor lenders' approaches to supporting customers experiencing financial hardship or other changes in financial circumstances'.
  - Commenting briefly on the 'very high levels' of refinancing activity in the home loans context, the CFR supports APRA's position that the 'the serviceability buffer – currently set at 3 per cent – remains at the appropriate level given the current environment, including the high degree of uncertainty and risks to the economic outlook'. The CFR notes that APRA will 'continue to assess the appropriateness of macroprudential policy settings as economic and financial conditions evolve'.
- planned payment systems overhaul: The CFR welcomed the government's strategic plan for payments and the related consultations on modernising the Payments System Regulation Act 1998 and defining payment functions that require a payments licence.
- Regulatory response to tackling scams/AML the key topic at the annual meeting with other agencies:
  - The key topic discussed at the CFR's annual meeting with other agencies, including the Australian Competition and Consumer Commission (ACCC), the Australian Transaction Reports and Analysis Centre (AUSTRAC) and the Australian Taxation Office (ATO), was recent reforms and regulatory developments aimed at tackling scams and money laundering activities.
  - AUSTRAC updated the Council on the government's proposed reform to the Anti-Money Laundering and Counter Terrorism Financing (AML/CTF) regime.
  - The Council discussed the increasing volume and sophistication of financial scams, especially investor-related scams and welcomed the government's decision to establish the National Anti-Scam Centre within the ACCC. Council members 'noted the importance of strengthening cooperation between government and industry and addressing potential regulatory gaps to respond to increasingly sophisticated scam activity'.
- RBA Review recommendations regarding the Council:
  - The Council welcomed the finding from the Review of the Reserve Bank that the cooperation among the Council agencies had been effective in mitigating financial stability risks.
  - The Council also discussed the Review recommendations to provide more clarity and transparency on how the Council agencies work together to promote financial stability and agreed that members would update their existing Memorandums of Understandings and the Council Charter.

[Source: CFR media release 14/06/2023]

Financial Services

Consumer protection | Assistant Treasurer flags addressing unfair trading practices as a priority, new consultation paper expected to be released in July

Our key takeaways from Assistant Treasurer and Minister for Financial Services Stephen Jones' 15 June 2023 address to the ACCC National Consumer Congress are below.

The starting point for Mr Jones' comments and the central message running through his address, is that the government 'sees consumer protection as core to economic policy'.

Mr Jones said that this commitment is reflected in both the reforms already being progressed by the government over the past 12 months and the government's reform agenda.

Tackling online scams

- Mr Jones reiterated the government's commitment to tackling online scams, including through funding the establishment of the National Anti-Scam Centre within the ACCC.
- Mr Jones flagged plans to consult on 'industry [scam] codes soon' (over the next 6-12 months).

Consumer Credit

- Mr Jones said that the government plans to build on the consumer credit reforms introduced by the Financial Sector Reform Act 2022 (Cth), by progressing plans for regulation of the Buy Now, Pay Later sector over the next 6-12 months.

Addressing unfair trading practices in the digital economy – consultation paper planned for release in July

- Mr Jones highlighted tackling Unfair Trading Practices in the digital economy – eg 'tricking consumers into consenting to data collection; omitting vital information to stop consumers making informed decisions; or preying on vulnerable consumers using excessive tracking of data' – as another priority area for the government.
- Mr Jones observed that two of the ACCC's recent inquiries recommended a prohibition on unfair trading practices. Mr Jones also noted that other jurisdictions such as the EU, UK, the US and Singapore already have regulations in place.
- As a first step, the government plans to release a consultation paper in July seeking feedback on potential options.

[Source: Assistant Treasurer and Minister for Financial Services Stephen Jones address to the ACCC National Consumer Congress 15/06/2023]

Simplifying and improving the navigability of Treasury portfolio laws: Treasury Laws Amendment (2023 Law Improvement Package No. 1) Bill 2023 introduced

On 14 June 2023, the Treasury Laws Amendment (2023 Law Improvement Package No 1) Bill 2023 (Cth) (Bill) was introduced into the House of Representatives.

Broadly, if enacted in its current form, the Bill would:

- implement a number of amendments to simplify and improve the navigability of existing Treasury portfolio laws in line with recommendations in interim reports A and B of the Australian Law Reform Commission (ALRC) Review of the Legislative Frameworks for Corporations and Financial Services Regulation. These changes include:
  - ensuring that the current version of the Acts Interpretation Act 1901 (Cth) applies to the Corporations Act 2001 (Cth) (Corporations Act) and the Australian Securities and Investments Commission Act 2001 (Cth)
  - creating a single glossary of defined terms in the Corporations Act
  - other technical changes eg repealing redundant provisions and correcting errors.

  These changes are included in Schedules 1-3.
- amending the enabling acts of certain legislative instruments regulating the insurance industry, to ensure sunsetting insurance instruments that are being remade are up to date (in line with the findings of a thematic review of Insurance Instruments that are due to sunset on 1 October 2023). These changes include:

- updating certain provisions to reflect modern communication practices
- allowing regulators to administrative prescribe the manner/form of certain notice to increase flexibility and align with modern drafting practices
- relocating some provisions in the insurance instruments to primary legislation

These changes are included in Schedule 4

- transferring what the explanatory memorandum describes as 'longstanding and accepted matters' currently contained in three ASIC made legislative instruments to the Corporations Act and the National Consumer Credit Protection Act 2009 (Cth) (Schedule 5)
- making 'minor and technical' changes to various Treasury portfolio laws to 'correct drafting errors, repeal inoperative provisions, address unintended outcomes, and make other technical changes' (Schedule 6)

[Source: Treasury Laws Amendment (2023 Law Improvement Package No 1) Bill 2023 (Cth)]

Financial Advice Experience Pathway | Treasury Laws Amendment (2023 Measures No. 3) Bill 2023 introduced

As previously flagged, Treasury Laws Amendment (2023 Measures No. 3) Bill 2023 (Cth) was introduced into the House of Representatives on 14 June 2023.

For context, the changes in Schedule 2 to the Bill are part of the government's broader planned overhaul of financial advice (see: Government response to the Quality of Advice Review - Insight - MinterEllison).

Key changes

Broadly, if enacted in its current form, the Bill would:

- introduce new rules to prohibiting 'schemes designed to avoid' the application of product intervention orders made under part 7.9A of the Corporations Act 2001 (Cth) (Corporations Act), in relation to a credit facility eg product intervention orders targeting predatory lending products. The aim to ensure predatory lenders cannot respond to a product intervention order by engaging in avoidance activity not covered by the order (Schedule 1)
- establish a pathway for experienced financial advisers with ten years experience and a clean disciplinary record who have passed the financial adviser's exam, to meet the qualification requirements for financial advisers (Schedule 2).
- make changes to existing laws to facilitate competition in the provision of clearing and settlement services for cash equities traded in Australia (Schedule 3). Specifically:
  - Part 1 of Schedule 3 to the Bill proposes to provide ASIC with a rule-making power to facilitate competitive outcomes in the provision of clearing and settlement services.
  - Part 2 of Schedule 3 to the Bill proposes to create a new arbitration regime (administered by the ACCC) for persons seeking to access clearing and settlement services.
- makes a number of technical changes to the Taxation Administration Act 1953 and Income Tax Assessment Act 1997 to address an operational issue with the First Home Super Saver Scheme (Schedule 4). Namely, to address the fact that users of the scheme are currently unable to access their savings under the scheme until retirement (instead of at the time they need to pay their deposit). It's proposed that the changes included in Schedule 4 would apply retrospectively to eligible applications made from 1 July 2018. The intention of the proposed changes is to help ensure that users of the scheme who have not been paid any of their First Home Super Saver Scheme savings can access the money they saved for that purpose to purchase their first home.

[Source: Treasury Laws Amendment (2023 Measures No. 3) Bill 2023]

Financial adviser registration requirement delayed to 1 October 2023

- ASIC Corporations (Registration of Relevant Providers) Instrument 2023/490 was registered on 19 June 2023.
- Broadly, the instrument (further) defers the requirement for AFS licensees and relevant providers to register financial advisers on the Financial Advisers Register until 1 October 2023.
- The further delay is to allow time for:
  - the amendments in Schedule 1 to the Treasury Laws Amendment (2023 Measures No. 1) Bill 2023 (currently before the Senate) to be further considered by Parliament; and (assuming the amendments are enacted).

– ASIC to implement these amendments
– industry to 'understand its rights and obligations concerning the registration requirement'
– 'AFS licensees to register their relevant providers with ASIC prior to the Registration Requirement commencing'.

[Source: ASIC Corporations (Registration of Relevant Providers) Instrument 2023/490]

DDO compliance | The Financial Services Council has released an update template TMD for funds management

- The Financial Services Council (FSC) has announced the release of an updated target market determination (TMD) template for funds management which replaces the 2021 version.
- The updated template is accessible to FSC members at no cost.
- Announcing this, FSC CEO Blake Briggs said that the updated template, which was developed in consultation with members and with the Australian Securities and Investments Commission (ASIC) will support industry in addressing the concerns raised in ASIC Report 762: Design and Distribution Obligations: Investment Products (summarised).
- More broadly, Mr Briggs said that the updated template is intended to complement other resources, including the FSC 'standard questionnaire for DDO-related due diligence for product distributors' that the FSC has developed to support DDO compliance and reduce compliance costs for industry.

[Source: FSC media release 07/06/2023]

New consumer resources released ahead of commencement of new Life Insurance Code of Practice

Ahead of the commencement of the new Life Insurance Code of Practice on 1 July 2023, the Financial Services Council (FSC) has released resources – a 'consumer guide to life insurance law' which the FSC describes as a 'detailed guide on life insurance law outlining the most important legal rights and obligations for life insurance customers' and a 'consumer fact sheet' on premiums – to support consumers' understanding of their rights under the new Code.

[Sources: FSC media release 02/06/2023; Life insurance Code of Practice resources]

Accounting and Audit

Report finds UK Audit Committee Chairs are already focused on ESG

The UK Financial Reporting Council (FRC) has released a report into Audit Committee Chairs' (ACCs) views on/approach to ESG reporting and assurance. Headline findings in the report include the following.

ESG is generally accepted as part of 'good business practice'

- The 'majority of ACCs…viewed ESG as an important part of good business practice'.
- All ACCs interviewed 'showed an interest in ESG and a good understanding of the ESG activities undertaken in their organisations' eg plastic reduction initiatives, carbon emissions and board diversity.
- 'Many' ACCs are not directly involved in ESG decision-making processes. This is especially the case when it comes to environmental and social issues. The report highlights that the ACCs' 'main role is related to risk and

compliance, as well as ensuring ESG is effectively reported on, rather than deciding on what to implement and how'

ESG disclosure

- The report found that there was a high level of familiarity, particularly among ACCs in larger companies, with the TCFD framework with the TCFD recommendations implemented by 'most'.
- Attitudes to the TCFD framework are described in the report as 'mixed'. For example, the report notes that there were 'a small number of negative reactions around continual changes to reporting standards. Alongside this, there were concerns from a few ACCs around the extended time and costs required for smaller businesses to comply with the recommendations'.
- The report also flags concern among 'some' ACCs about the challenges associated with reporting on environmental activities, particularly Scope 3 emissions and the impacts on markets outside the UK and Europe.
- There was also concern that the increased focus on ESG in reporting is adding to the length of annual reports making it 'harder to identify key information'
- There is also concern from 'some' ACCs about the time/cost around ESG reporting (especially among smaller organisation)

Growing focus on 'S' issues

- On the 'social' component of ESG, 'some' ACCs reported that the level of focus is increasing, especially with respect to: board and senior management diversity, staff wellbeing and equal pay.

Call for more (and more easily navigable) guidance

- The report found that:

  > 'Many ACCs commented that the guidance on ESG related activities, and how to measure them, is complex to navigate - particularly for businesses with limited resources, those who operate across markets and those who have only recently begun to invest time into environment and social activities'.

- A number of ACCs (especially those from smaller organisations) said they would 'welcome' more practical, sector specific guidance from the FRC and in particular, guidance around the measurement of environmental/social activities.
- Some ACCs would also welcome 'best practice examples to ensure ESG reporting is salient and meaningful, rather than adding more reporting requirements'.

FRC to provide additional guidance

Announcing the release of the report, FRC Executive Director of Regulatory Standards Mark Babington said that the regulator is 'pleased' at the extent to which ACCs are already focused on ESG reporting and assurance. Mr Babington also stated that the FRC is:

> 'committed to supporting ACCs with practical guidance and best practice examples to ensure high-quality and consistent ESG reporting.'
>
> [Sources: FRC media release 20/06/2023; Full text report: Audit Committee Chairs' views on, and approach to Environmental, Social and Corporate Governance (ESG)]

Risk Management

Top Story | An AI balancing act – Australia's potential regulatory measures under consideration by government

Following the release of the Safe and Responsible AI in Australia Discussion Paper on 1 June 2023, MinterEllison has released an article outlining the various potential regulatory measures that under consideration by the government.

You can access the full text here.

Don't neglect governance in the race to embrace new tech says ASIC Chair

Our key takeaways from Australian Securities and Investments Commission (ASIC) Chair Joe Longo's 20 June 2023 address to the International Swaps and Derivatives Association (ISDA)/Australian Financial Markets Association (AFMA) Forum are below.

New technology is a 'great opportunity' (but in embracing it governance/risk management standards cannot be allowed to slip)

Mr Longo said that ASIC regards the rapid rate at which technology is evolving, including the emergence of generative AI as 'a great opportunity' for wholesale markets and the economy more broadly.

In making this point, Mr Longo underlined that ASIC's continued focus on market integrity is unchanged, as is the regulator's expectation that existing governance and risk management standards continue to be met.

Against this background, Mr Longo called on wholesale markets to work with ASIC to ensure continued confidence in Australia's financial markets through both:

- adopting a cautious

approach to new technology (eg generative AI) ie ensuring there is appropriately strong focus on understanding the technology (and its potential impacts), and implementing robust governance and operational resilience measures accordingly

- cooperating with ASIC on key issues including giving ASIC access to the data needed to enable effective oversight of 'risk build ups in the financial system' and 'what each firm's exposures are'

When it comes to new technology, ASIC's expectations are unchanged

Mr Longo acknowledged that wholesale markets have long been early adopters of new technology.

Commenting specifically on the rapid emergence/availability of generative AI, Mr Longo observed that though there are moves in Australia and overseas around potential approaches to the regulation of AI 'there is as yet no real consensus on how to regulate AI, if at all'.

From a practical perspective, Mr Longo urged caution:

> 'Put simply, if you can't explain how a particular system works – and it seems that this is the case with some complex AI systems – how can you justify using it? As early as 1960 Prof Norbert Wiener, one of the architects of cybernetics, observed that 'If we use, to achieve our purposes, a mechanical agency with whose operation we cannot interfere effectively… we had better be quite sure that the purpose put into the machine is the purpose we really desire.'

Building on this, Mr Longo cautioned against rushing too quickly into embracing new technology, without taking the time ensure the necessary governance processes/controls are in place. Mr Longo stated:

> 'There is a very real danger here that entities may rush too quickly into innovations without applying appropriate controls and proper governance…With this in mind, entities need to focus on robust governance and operational resilience measures. This is nothing new – just because the technology has changed nobody should think that means your existing obligations around good governance have changed with it. They haven't. But it's all too easy to forget this in the face of such rapid and unprecedented change. Easy – and dangerous'.

In terms of meeting regulatory expectations in this context, Mr Longo stated:

> 'There must be an important focus on controls alignment with innovation. Our expectation is for appropriate controls to be part of the design phase and in place before new tech is switched on. It's important that the whole financial market ecosystem works to uplift controls – just as a convoy must go at the pace of its slowest vessel, so too is the financial ecosystem reduced to the strength of its weakest link'.

Looking ahead, Mr Longo flagged that in the 'next financial year' ASIC plans to consult on 'expanding automated order processing rules to futures markets to reflect developments with AI' as well as update its electronic trading guidance.

AI is a 'high and important priority for ASIC'

Commenting more broadly, Mr Longo emphasised that:

> 'ASIC has AI as a high and important priority. Not just in regards to wholesale markets, but also its role in – and for – the whole economy, including consumers and small business'.

Increased transparency

Mr Longo said ASIC regards market transparency, including through over-the-counter (OTC) derivative transaction reporting as a 'critically important element in identifying risk build ups in the financial system and what each firm's exposures are'.

Mr Longo said that having direct access to this data has already enabled ASIC to 'react quickly and make informed and timely decisions as financial markets experienced volatility coming from a variety of sources such as the US banking turmoil, COVID-19, and geopolitical events like the Russian invasion of Ukraine'.

Mr Longo acknowledged that this has been a 'pain point' for industry and said that ASIC is working to streamline requirements in order to reduce the reporting burden. Mr Longo noted that the new ASIC Derivative transaction reporting rules will commence in October next year, and the third round of consultation will be done in the second half of this year.

Mr Longo also underlined that ASIC is committed to 'being more open and consultative' stating that ASIC is 'keen to learn from you what the industry is focusing on, and where risks or issues are that we should be prioritising'.

Mr Longo pointed to industry calls for guidance on pre-hedging as an example of an issue where ASIC is listening. Mr Longo said that ASIC is engaging with ESMA on its call for evidence in Europe, as well as the FMSB and IOSCO, which is considering work in this area and hopes to provide industry with guidance 'soon'.

[Source: Speech by ASIC Chair Joe Longo at the ISDA/AFMA Forum 20/06/2023]

European Parliament progresses new draft AI laws

The European Parliament has announced it has adopted its negotiating position on new AI laws (the proposed Artificial Intelligence (AI) Act), ahead of meeting with member states to finalise the proposed legislation.

Once finalised, it's envisioned that the legislation will (among other things):

- **Prohibit 'AI systems with an unacceptable level of risk to people's safety'.** At this stage, this would include, introducing bans on:
  - 'Real-time" remote biometric identification systems in publicly accessible spaces;
  - "Post" remote biometric identification systems, with the only exception of law enforcement for the prosecution of serious crimes and only after judicial authorisation;
  - Biometric categorisation systems using sensitive characteristics (e.g. gender, race, ethnicity, citizenship status, religion, political orientation);
  - Predictive policing systems (based on profiling, location or past criminal behaviour);
  - Emotion recognition systems in law enforcement, border management, the workplace, and educational institutions; and
  - Untargeted scraping of facial images from the internet or CCTV footage to create facial recognition databases (violating human rights and right to privacy)'.
- **Introduce new risk management and registration requirements for 'providers of foundation models'.** That is, providers would need to 'assess and mitigate possible risks (to health, safety, fundamental rights, the environment, democracy and rule of law) and register their models in the EU database before their release on the EU market'.
- **Introduce transparency requirements for 'generative AI systems'** (eg like ChatGPT) including new requirements to disclose if content is AI-generated. It's also proposed (among other things) that 'detailed summaries of the copyrighted data used for their training would also have to be made publicly available'.
- **Strengthen the role of the EU AI Office in monitoring implementation of the new 'AI rulebook'**
- **Strengthen people's right to file complaints about AI systems** and 'receive explanations of decisions based on high risk AI systems that significantly impact their fundamental rights'

Co-rapporteur Dragos Tudorache (Renew, Romania) said that the new AI Act, once finalised will:

> 'set the tone worldwide in the development and governance of artificial intelligence, ensuring that this technology, set to radically transform our societies through the massive benefits it can offer, evolves and is used in accordance with the European values of democracy, fundamental rights, and the rule of law'.

[Source: European Parliament media release 14/06/2023]

Strengthening the public sector whistleblower scheme | Public Interest Disclosure Amendment (Review) Bill 2022 (Cth) has received Assent

- The Public Interest Disclosure Amendment (Review) Bill 2022 (Cth) (Bill) passed both Houses on 15 June 2023 and received Assent on 19 June 2023.
- Broadly, the changes in the Bill aim to strengthen protections for public sector whistleblowers (covered by the public sector whistleblowing scheme under the Public Interest Disclosure Act 2013 (Cth) (PID Act)) in various respects as well as implement changes to improve the administration and oversight of the scheme.
- The replacement explanatory memorandum sums up the five main changes introduced by the Bill as follows. Broadly, the Bill will:
  - 'make it easier for agencies to administer the PID scheme by providing greater flexibility in how they handle disclosures
  - provide increased protections for disclosers
  - enhance oversight of the scheme by the Office of the Commonwealth Ombudsman (Ombudsman) and the IGIS [Inspector General of Intelligence and Security]

- make it easier for a disclosure to be investigated under another law or power, including by the National Anti-Corruption Commission (NACC), where this is more appropriate than dealing with the disclosure under the PID Act, and
- improve information-sharing provisions, giving agencies more confidence to share information relating to a disclosure to ensure it can be investigated by the most appropriate agency'.

- The changes contained in the Bill implement the government's response to 21 of the 33 recommendations in the 2016 Review of the Public Interest Disclosure Act (Moss Review) and are also informed by other parliamentary committee reports.
- Announcing the passage of the Bill, Attorney General Mark Dreyfus described the Bill as:

  'a significant milestone towards a best practice whistleblowing framework for the public sector, which will support the establishment of the National Anti-Corruption Commission'.

- The government envisages that the changes will be the 'first stage' in reforming the PID Act to 'restore' it to 'a best practice whistleblowing framework.

Government to consult on second stage of planned reforms 'shortly'

- In his second reading speech, Attorney General Mark Dreyfus flagged that following the passage of the Bill the government plans to commence a second stage of reform which will include public consultation on:
  - notification of urgent disclosures in intelligence agencies to the IGIS as soon as possible, and
  - biannual reporting of statistics on all public interest disclosures to the parliament.
- Announcing the passage of the Bill, Mr Dreyfus reiterated the government's intention to consult on a second stage of reforms adding that the government intends to 'shortly begin consultations on a second stage of reforms' which will involve 'redrafting the Public Interest Disclosure Act to address the underlying complexity of the scheme and provide effective and accessible protections to public sector whistleblowers'.

Initial response

The Human Rights Law Centre, Griffith University and Transparency International Australia have welcomed the passage of the Bill and the government's commitment to further reform of the PID Act.

[Sources: Public Interest Disclosure Amendment (Review) Bill 2022; Replacement explanatory memorandum; Attorney General Mark Dreyfus media release 15/06/2023; Human Rights Law Centre media release 15/06/2023]

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