Governance News

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

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Contents

Diversity

Gender Diversity | ACSI says 30% women on boards is now a minimum expectation for ASX 300 companies

Under its new voting policy, the Australian Council of Superannuation Investors (ACSI):

> 'may recommend its members vote "against" existing directors of ASX300 companies with poor gender diversity, with a focus on those most accountable for board succession and composition'.

Specifically, ACSI has said it will *consider* issuing an 'against' recommendation against the Chair, the Chair of the Nomination Committee, a Nomination Committee member or other director seeking re-election where the board has less than 30% women directors.

According to ACSI, the policy change means that there are approximately 100 ASX 300 companies that could face voting action under the new policy.

However, ACSI CEO Louise Davidson made clear that:

> 'As always, our voting recommendations will be combined with direct company engagement and applied on a case-by-case basis. While around 100 companies could currently face 'against' recommendations, we believe that, following engagement, the number will be much smaller'

The new policy will apply, from July 2023 (during the 2023 AGM season).

ACSI states that it has written to ASX 300 boards to advise them of the change.

[Source: ACSI media release 17/05/2023]

Yet to crack 30%: Report finds women hold 28.9% of Russell 3000 boards seats, women of colour hold just 7.3%

Women on Boards has released its latest report tracking progress towards gender parity on Russell 3000 company boards (ie women holding 50% of seats, and women of colour holding at least 20% of all board seats).

Our key takeaways are below.

The figures are current to the end of Q1 2023 (31 March 2023).

Board gender diversity

- **Yet to crack 30%:** Women held 28.9% of board seats (up 0.5% on Q4 2022)
- **Almost half of boards include three or more women, and 11% are now gender balanced:**
  - 327 companies (11%) had gender balanced boards (up from 313 companies (or 10%) in Q4 2022)
  - 1,308 companies (45%) include three or more women (up from 1285 companies (43%) in Q4 2022)
- **One and done/all-male boards persist**:
  - 364 companies or 13% have one woman
  - 60 companies or 2%, have 0 women on their boards
- **Looking at it by State:** Of the 25 states with over 20 public companies:
  - California leads on gender diversity with 34% of board seats held by women and 21% of companies having achieved gender balance
  - Nevada has the lowest percentage of women on boards at 24% (but the report comments that Nevada has more gender balanced boards than Florida which ranks second last in terms of board gender diversity)
- **(Slightly) more women are being appointed:** 41.4% of the 626 new directors appointed in Q1 2023 were women (in line with Q1 and Q2 2022, and up from Q3 and Q4 2022 when the proportion was under 40%)
- **New seats being added:** 78% of the seats gained by women were new seats (ie seats added to the board not replacing an existing director)

(Minimal) movement on increased board racial/ethnic diversity

- **Increased transparency:** 33% of all directors appointed in Q1 2023 disclosed their race/ethnicity
- **Less than 20% of seats held by people of colour**:
  - People of colour hold 18.4% of seats (up 1.5% on Q4 2022)
  - Women of colour hold 7.3% of seats (up 0.5% on Q4 2022)
  - Men of colour hold 11.1% of seats (up 1% on Q4 2022)

[Source: 50/50 Women on Boards Gender Diversity Index Q1 2023]

Meetings and Proxy Advisers

Early US voting trends: Support for 'Say on Pay' and directors is up, support for shareholder E&S proposals is down

Semler Brossy has released its latest report monitoring early trends in votes on 'Say on Pay' proposals, director elections and shareholder E&S proposals.

Our key takeaways are below.

According to the report, as at 12 May 2023:

'Say on Pay'

- The level of support is up on last year:
  - The current Russell 3000 average vote result is 91.4% (up from 90.5% at the same time last year)
  - 78% of companies have received >90% support (up from 75% for the same period last year)
- The failure rate is down on last year: 11 Russell 3000 companies (1.5%) have failed Say on Pay so far this year (vs 2.8% last year)
- Top two (likely) drivers behind failed Say on Pay votes are identified in the report as: 1) 'Problematic pay practices' and 2) 'Rigour of performance goals'. These are closely followed by 'special awards/mega grants' and 'Pay and performance relation'.

Director elections

- Average support for directors is also at a five year high at 95.3% (up from 94.5% for 2022).

Support for shareholder E&S proposals is down on last year

- Shareholder 'Social' proposals:
  - The median level of support for the shareholder 87 shareholder social proposals that have gone to a vote so far is 17% (down from 22% average support for the whole of 2022)
  - Three social proposals (3%) have received greater than 50% support so far in 2023
- Shareholder 'Environmental proposals':
  - The median level of support for the 38 shareholder environmental proposals that have gone to a vote so far this year is 23% (down from 27% average support for the whole of 2022)
  - One environmental proposal (3%) has received greater than 50% support so far in 2023

[Source: Semler Brossy Report: 2023 Say on Pay and Proxy Results May 2023]

Shareholder Activism

Shareholder climate proposal at Chubb secures close to 30% support

Chubb Ltd's annual shareholder meeting was held on 17 May 2023. Ahead of the meeting, the board advised shareholders to vote 'against' both of the shareholder ESG proposals set to go to vote.

Neither proposal was carried though As You Sow's underwriting proposal secured close to 30% support – similar proposals were also filed at The Travelers and Berkshire Hathaway.

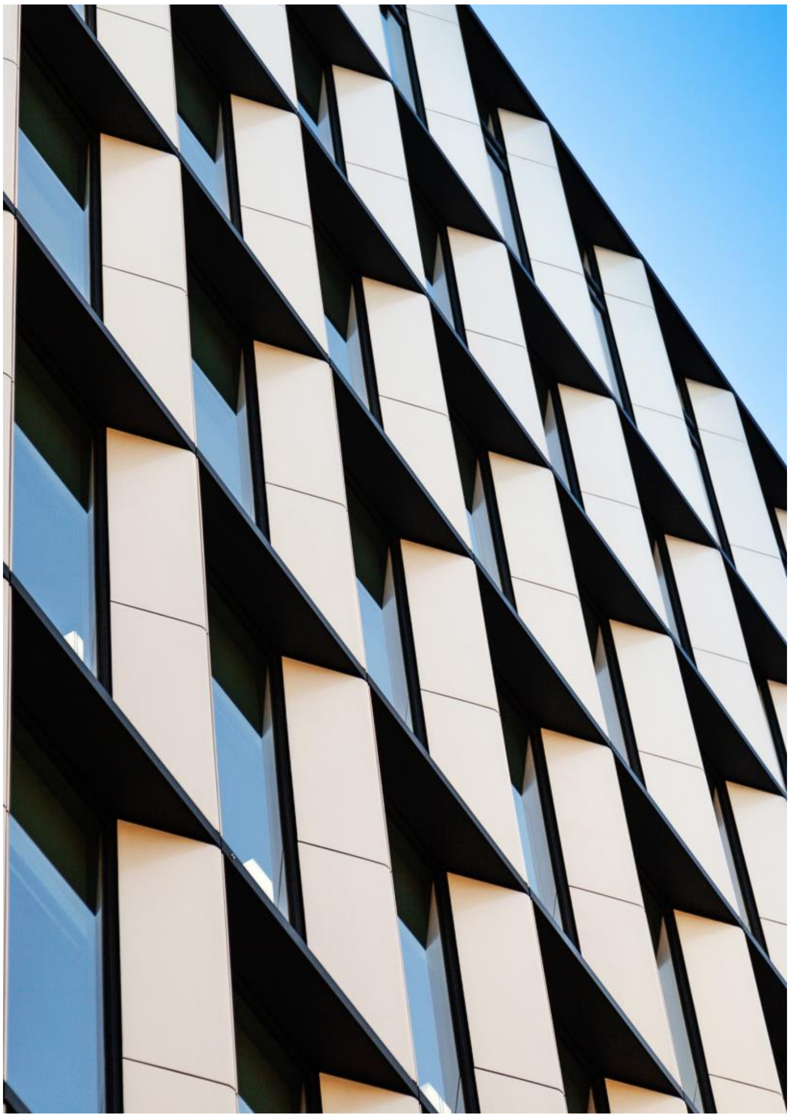
The table below provides a snapshot of the two proposals and an indication of how investors voted.

PROPOSAL	CHUBB RESULT	HOW INVESTORS VOTED
Climate: Alignment of underwriting/insuring/investment with Paris aligned GHG Targets: Agenda Item 14 in the Notice, filed by As You Sow as representative of Warren Wilson College and co-filers Jubitz Foundation and the Meyer Memorial Trust, called on the insurer to: 'issue a report…disclosing 1.5°C aligned medium and long-term GHG targets for its underwriting, insuring, and investment activities'. [Note: A similar Proposal filed with Berkshire Hathaway (Proposal 6 in the Notice), also filed by As You Sow) received approximately 23% support earlier this month. As You Sow has also filed a similar proposal at The Travelers.]	28.93% support	▪ Norges Bank Investment Management (NBIM) voted in support. The rationale given is that: 'The board should account for material sustainability risks facing the company, and the broader environmental and social consequences of its operations and products. Sustainability disclosures should be aligned with applicable global reporting standards and frameworks to support investors in their analysis of risks and opportunities'. NBIM also backed As You Sow's proposal at Berkshire Hathaway. ▪ Legal and General Investment Management (LGIM) also voted in support (also consistent with its support of a similar proposal at Berkshire Hathaway) ▪ Storebrand also voted in support (again, consistent with its support of a similar proposal at Berkshire Hathaway) ▪ CalPERS voted in support, consistent with its support for a similar proposal at Berkshire Hathaway. ▪ CalSTRS voted against. Interestingly, CalSTRS voted in support of a similar proposal at Berkshire Hathaway.
Human rights: Agenda Item 15 in the Notice filed by Domini Impact Investments LLC, as representative of the Domini US Impact Equity Fund called on the board to: 'publish a report, describing how human rights risks and impacts are evaluated and incorporated in the underwriting process.'	16.53% support	▪ NBIM voted in support giving the same justification given for voting in support of the proposal above (Agenda Item 15). ▪ LGIM voted in support ▪ Storebrand also voted in support ▪ CalSTRS voted in support. ▪ CalPERS voted against

As You Sow's response

In a statement commenting on the vote result, As You Sow said the results at both Chubb and Berkshire Hathaway put both insurers under pressure to amend their approach. As You Sow states:

> 'Twenty-eight global insurers have joined the United Nations' Net-Zero Insurance Alliance, committing to transition emissions from insurance and reinsurance underwriting portfolios to Net Zero by 2050. This strong show of shareholder support presents the opportunity for Chubb and Berkshire to adjust course and join their peers in responding to climate risk'.
>
> [Sources: Notice of Meeting, Results of Meeting]



Telsa shareholders reject 'key person risk' shareholder proposal, endorse CEO at shareholder meeting

The three directors standing for election at the 16 May 2023 Tesla Inc shareholder meeting were duly elected, with Tesla CEO Elon Musk securing the highest level of support of the three (approximately 95% support) and JB Staubel securing approximately 86% support.

To put this in context, according to Semler Brossy, the average level of support for Russell 3000 directors so far in 2023 stands at 95.3% (up from 94.5% for 2022).

Ahead of the meeting, a number of investors including SOC Investment Group, called on shareholders to vote 'against' the election of Mr Staubel on independence grounds. In their view, given Mr Staubel's close relationship with Mr Musk, his ability to 'reign in' Mr Musk/strengthen risk oversight at the company was in question.

Looking at how some of the larger investors voted:

- Norges Bank Investment Management (NBIM) voted in support of all three directors standing for election (in line with management's recommendation).
- Storebrand voted in support of Mr Musk's election, but against the election of both Chair Robyn Denholm and JB Staubel
- Legal and General Investment Management (LGIM) voted in support of Mr Musk and JB Staubel but against Robyn Denholm.

Shareholders rejected both shareholder proposals that went to vote

Two shareholder proposals were put to a vote at the meeting, both of which look to have secured under 7% support. The table below provides a snapshot of the proposals, and an indication of how some investors voted on Proposal 5.

TESLA	
PROPOSAL	**HOW INVESTORS VOTED**
Reporting on key person risk: Proposal 5 in the Notice (filed by Sumtris ehf.) called on the board to: 'oversee the preparation and maintenance of a publicly-disclosed report on Tesla's Key-Person Risk, including identification of key persons and actions to ameliorate the impacts of their potential loss'.	▪ NBIM voted against ▪ Storebrand voted against ▪ LGIM voted against
Child labour/human rights risk reporting: Proposal 6 (floor resolution) filed by As You Sow, called on the board to issue a report: 'describing if, and how, Tesla plans to eradicate child labour and forced labour from its supply chain by 2025. The public report should explain Tesla's supply chain tracing efforts and the concrete steps it is taking to ensure full supply chain transparency. Reporting is requested within one year from Tesla's 2023 annual meeting'.	Though given the result, it is unlikely the proposal secured strong investor support, information to confirm this is not readily accessible given this resolution was raised from the floor.

[Source: Tesla Notice of Meeting; Results of meeting]

NBIM to vote 'against' shareholder Climate Action 100+ flagged resolution at TotalEnergies

- Norges Bank Investment Management (NBIM) has predeclared its intention to vote (in line with management recommendations) for all management-proposed resolutions at the 26 May 2023 Total Energies shareholder meeting.
- NBIM has also flagged it will vote, in line with the board's recommendation, against a shareholder climate resolution (Resolution A in the Notice) filed by Follow This calling on the company to align its 2030 Scope 3 emissions reduction targets with the goals of the Paris Agreement.
- Resolution A has been flagged by Climate Action 100+

  [Note on 'flagging': For clarity, investor signatories to Climate Action 100+ are not bound to/required to vote against 'flagged' resolutions – they vote on shareholder proposals in their individual capacity and not on behalf of the Climate Action 100+ initiative. Nor does Climate Action 100+ 'take a formal position on shareholder voting'. Rather, 'flagging' a resolution considered to be aligned with the goals of the initiative is intended to highlight/draw attention to the resolution and help ensure it receives due consideration from investor signatories to the initiative. Climate Action 100+ publishes a list of 'flagged' proposals (which is regularly updated) here]

Similar resolutions filed at four other companies

- Follow This (backed by a €1.1 trillion investor coalition) has filed similar resolutions at Shell, Exxon, Chevron and BP.
- So far this year:
  - The Follow This resolution at BP (Resolution 25 in the Notice) failed to secure the necessary support to be carried at the company's 27 April 2023 shareholder meeting. The resolution secured 16.75% support. Ahead of the meeting, NBIM predeclared its intention to vote (in line with management's recommendation) against the resolution. California Public Employees Retirement System (CalPERS) also voted against as did Legal and General Investment Management (LGIM).
  - The Follow This resolution at Shell (Resolution 26 in the Notice) secured approximately 20% support (this is covered in more detail separately below).
- The annual shareholder meetings for the other companies targeted are scheduled for:
  - 31 May 2023: Chevron
  - 31 May 2023 ExxonMobil
- In 2022, resolutions calling on companies to set Paris-aligned Scope 1, 2 and 3 emissions reduction targets at Shell, BP, ExxonMobil and Chevron received 20%, 15%, 28% and 33% support respectively.

[Source: NBIM voting bulletin]

'Say on Climate': 20% of Shell shareholders vote 'against' management-proposed resolution

'Say on Climate' resolution

- 20% of Shell Plc investors voted 'against' the management-proposed, 'Say on Climate' resolution (Resolution 25 in the Notice) to approve the company's energy transition progress for 2022 as disclosed in the company's 2022 annual report and Energy Transition Progress Report.
- To provide some context, according to Glass Lewis just seven of the 18 manage-proposed 'Say on Climate' proposals that went to a vote at European countries in 2022 received 10%+ against votes.
- Ahead of the vote, the proposal was 'flagged' by Climate Action 100+.

  [Note on 'flagging': For clarity, investor signatories to Climate Action 100+ are not bound to/required to vote against 'flagged' resolutions – they vote on shareholder proposals in their individual capacity and not on behalf of the Climate Action 100+ initiative. Nor does Climate Action 100+ 'take a formal position on shareholder voting'. Rather, 'flagging' a resolution considered to be aligned with the goals of the initiative is intended to highlight/draw attention to the resolution and help ensure it receives due consideration from investor signatories to the initiative. Climate Action 100+ publishes a list of 'flagged' proposals (which is regularly updated) here]
- A number of investors predeclared their intention to oppose the resolution. The reasons given for this include that investors consider Shell's transition plan is not sufficiently aligned with the Paris Agreement. One issue flagged by investors is that the company has not set absolute Scope 3 emission reduction targets (the company's Scope 3 targets relate to intensity reduction).

Scope 3 resolution

- 20% of Shell shareholders voted in support of a shareholder proposed resolution (Resolution 26 in the Notice, filed by Follow This) calling on Shell to:

  'to align its existing 2030 reduction target covering the greenhouse gas (GHG) emissions of the use of its energy products (Scope 3) with the goal of the Paris Climate Agreement: to limit global warming to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C'.
- This resolution was also flagged by Climate Action 100+ ahead of the vote. Resolution 25 did not have board backing.
- Ahead of the vote, a number of investors predeclared their intention to support the resolution. Norges Bank Investment Management (NBIM) voted against.
- As flagged above, Follow this has filed similar resolutions at a number of other companies (Chevron, ExxonMobil, BP and TotalEnergies this year). So far, the resolution at BP secured 16.75% support.
- For context, in 2022, Follow This resolutions calling on companies to set Paris-aligned Scope 1, 2 and 3 emissions reduction targets at Shell, BP, ExxonMobil and Chevron received 20%, 15%, 28% and 33% support respectively

Shell intends to engage with shareholders 'to understand the reasons behind the result'

- Commenting on the vote results on Resolutions 25 and 26 Shell CEO Wael Sawan said that the level of support for the 'Say on Climate' resolution signals that 'the vast majority' of Shell's investors 'remain supportive of our strategy to become a net zero emissions energy business by 2050'. Having said this, they also said that:

  'The level of votes on Resolutions 25 and 26 requires us to explain what actions we intend to take to consult shareholders in order to understand the reasons behind the result, and report back within six months. We will meet this obligation by continuing to engage with shareholders on why we believe our strategy keeps us on the right path. The level of votes on Resolutions 25 and 26 requires us to explain what actions we intend to take to consult shareholders in order to understand the reasons behind the result, and report back within six months. We will meet this obligation by continuing to engage with shareholders on why we believe our strategy keeps us on the right path'.

  [Source: Notice of Meeting, Results of meeting]

ESG

Government moves to establish an interim body to advise on the establishment and begin some of the work of the planned National Net Zero Authority

Following the Prime Minister's 5 May 2023 announcement of the government's intention to establish a permanent National Net Zero Authority, the government has moved to establish a new interim body to advise on the establishment of the new permanent Authority and commence some of its key functions.

The Order will commence 1 July 2023.

[Source: Executive Order to Establish the Net Zero Economy Agency as an Executive Agency, Gazette - C2023G00539, 11/05/2023]

Climate Action 100+ consults on new Net Zero Standard for diversified mining

- Climate Action 100+ has released a draft Net Zero Standard for Diversified mining, developed in consultation with investors and mining companies, for broader consultation until June 2023.
- The aim of the new standard is to support investors in assessing the progress diversified mining companies are making in their transition to net zero. The Standard is designed to complement the sector-neutral Climate Action 100+ Company Benchmark.
- Announcing the release of the draft standard Investor Group on Climate Change and Asia Investor Group on Climate Change CEO Rebecca Mikula Wright commented:

  'Investors have been looking for a rigorous and reliable tool to assess the credibility of mining companies' plans and progress in the transition to net zero. As regulators around the world crack down on greenwashing, we hope this standard will provide clarity and consistency to all stakeholders, including the companies themselves."

- It's envisioned that the standards will be published in final form in Q3 2023.

  [Source: IGCC media release; Draft standard: Climate Action 100+ Net Zero Company Benchmark 2.0]

Regulators

Top Story | APRA Deputy Chair reminds boards that GCRA should be a continuing focus (including DEI)

Key takeaways from APRA Deputy Chair Helen Rowell's address to the Governance and Risk Management Forum 2023

Key Takeouts

- In her address to the Governance Institute of Australia's Governance Forum 2023, APRA Deputy Chair Helen Rowell identified failures of Governance, Culture, Remuneration and Accountability (GCRA) as a common thread running through many past crises in Australia (and further afield) over the last 20 years
- Despite the increased focus on strengthening GCRA over time, Ms Rowell underlined that there remains scope for industry to further improve and cautioned against complacency - GCRA should be an area of ongoing focus.
- Ms Rowell also reiterated that APRA considers diversity, particularly at board/leadership level, to be central to good governance. Ms Rowell also flagged again that the regulator is considering how consideration of DEI might be strengthened as part of planned reviews of Prudential Standards CPS 510 Governance and CPS 220 Risk Management.

Our key takeaways from Australian Prudential Regulation Authority (APRA) Deputy Chair Helen Rowell's 17 May 2023 address to the Governance Institute of Australia's 2023 Governance Forum are below.

GCRA failures a common thread running through crises over the last 20 years

As flagged, Ms Rowell identified Governance, Culture, Remuneration and Accountability (GCRA) failures as a common theme present in various 'crises' over the past 20 years and said that this has been a key driver behind APRA, and industry's increased focus on these issues over time. Ms Rowell observed:

> 'Each of these episodes was different but look closely and you will find things in common. Indeed, all can be traced in one way or another to failures in governance, risk culture, remuneration or accountability, which (because you know we love an acronym at APRA) we term GCRA. To quote, ECB (European Central Bank) Supervisory Board Member Elizabeth McCaul: "Supervision comes down to the idea that all roads lead to governance. Indeed, throughout my career, I have seen that strong governance is the true north that guides a sound bank."'

In light of this, and in light of what she described as 'gathering clouds that threaten the resilience of the financial sector' (eg energy transition, rising geopolitical risk and digital disruption to business models), Ms Rowell emphasised that both APRA and boards need to be focused on ensuring GCRA risks are being effectively managed going forward.

No room for complacency – GCRA should be a continuing focus area for boards

Ms Rowell observed that over time, the level of attention on so-called non-financial risk has grown within APRA, and within industry, in recognition of the seriousness of the consequences/flow on effects of poor leadership, weak risk culture, 'inappropriate financial incentives' and 'lack of accountability when things go wrong'.

Importantly, Ms Rowell made clear that though there has been improvement in risk and governance practices over time, including within APRA, there is no room for complacency. In illustration, Ms Rowell observed that:

> 'The general insurance industry in 2023 is further advanced in its governance and risk management practices than it was at the time of HIH's collapse. However, as we saw during the pandemic in relation to business interruption insurance, and the insurance risk management reviews that APRA subsequently required, there is no room for complacency when it comes to sound governance and risk management'.

Speaking more broadly, Ms Rowell underlined that GCRA should be (and is expected to be) a continuing focus for all boards.

> 'A key lesson for all boards – whether in the insurance industry or not – is the importance of embracing a culture of independent review and challenge, seeking different perspectives, and continuing to evolve and strengthen practices when it comes to managing core business risks. It is not a one-off, set and forget exercise but rather requires ongoing attention and enhancement.

> Boards need to ask for, and be provided with, the information needed to support them in meeting their governance and risk management responsibilities, and to be able to show evidence of how they are satisfied that management is proactively overseeing the effective management of the risks to which their business is exposed'.

Leadership culture is key

Ms Rowell identified leadership culture – 'boards and senior management leading by example in how they learn and grow from setbacks' - as vital to successfully embedding and operationalising the lessons learnt from past crises (including for example, the Hayne Commission).

Ms Rowell observed that:

> 'Better boards embrace feedback and lean into dealing with issues, see them as an opportunity for reflection, and to take steps to remedy the root causes and make genuine and enduring changes throughout their organisation. Others are more begrudging or half-hearted in their response, and do not nurture a culture that facilitates embedding of better governance and risk management practices throughout their organisation. And that approach almost inevitably leads to lessons not genuinely being learned and mistakes of the past being repeated'.

Board diversity

Ms Rowell observed that while there are a range of reasons why some boards 'do better than others in leading their companies', APRA considers that board composition is 'paramount' in this context, especially in light of the increased demands being made of directors.

Ms Rowell said:

> 'These increased demands have elevated the importance of boards that are equipped to analyse and make strategic decisions relating to a far broader range of issues than was once the case. Further, we know that better outcomes – including financial ones – result from bringing in a broader range of perspectives. As a result, we now see a much greater focus on building boards with the right mix of skills and experience for the challenges their organisation faces, now and into the future.
>
> In addition, the intrinsic importance of boards comprising a diversity of backgrounds and perspectives is recognised, as well as the need for an orderly renewal process to refresh directors over time to maintain independent perspectives and constructive challenge'.

In light of this, Ms Rowell raised concerns that 'genuine diversity [is] still lacking around too many board tables', often as a result of long-standing directors' electing not to step down. In illustration, Ms Rowell pointed to the fact that there are 38 directors on the boards of APRA-regulated credit unions and mutual ADIs (authorised deposit taking institutions) that have been in their roles since (at least 2002).

Given the known benefits of diversity, including from a governance perspective, Ms Rowell described the need to enhance DEI across industry, as 'the next frontier in ensuring sound governance and risk culture practices'.

APRA is considering how it can strengthen consideration of inclusion and diversity as part of this year's review CPS 510 and CPS 220

Ms Rowell said that to date APRA has been 'content to raise awareness of DEI and start a conversation'. For example, through the release of a report earlier in the year from the International Association of Insurance Supervisors (IAIS) (summarised) presenting insights from a recent 'stocktake' of the DEI initiatives being undertaken globally by insurance supervisors, relevant international organisations and the insurance industry. Announcing the release of this report APRA flagged at the time that it considers (in line with the IAIS' position):

> 'strong diversity and inclusion practices' within the financial services sector, and diverse representation on boards, to be important in enhancing governance and risk management'.

In her address, Mr Rowell reiterated that this remains APRA's view. APRA, Ms Rowell said, considers

> 'strong diversity and inclusion practices' within the financial services sector, and diverse representation on boards, to be important in enhancing governance and risk management'.

Ms Rowell also reiterated that APRA is considering:

> 'how we can strengthen this aspect [the DEI aspect] of governance and risk management as part of upcoming reviews of Prudential Standards CPS 510 Governance and CPS 220 Risk Management'.

For context, APRA has previously identified the review of CPS 510 and CPS 220 as policy priorities for 2023. In terms of timing, APRA plans to initiate consultation on CPS 510 (and broader governance requirements) 'in the latter half of 2023', with a view to the changes being finalised in 2024. The review of CPS 220 is planned to follow the completion of the review of CPS 510.

[Source: APRA Deputy Chair Helen Rowell - Speech to the Governance and Risk Management Forum 2023 17/05/2023]

An initial step towards ending regulatory uncertainty on crypto? IOSCO consults on recommendations for global crypto regulation

- The International Organisation of Securities Commissions Organisation (IOSCO), which bills itself as the 'global standard setter for securities regulation' has released a consultation paper seeking feedback on 18 draft policy recommendations for how jurisdictions globally should approach the task of regulating the trading of crypto-assets.
- Broadly, the aim of the recommendations is:

  > 'to support greater consistency with respect to regulatory frameworks and oversight in its [IOSCO's] member jurisdictions, [and] to address concerns related to market integrity and investor protection arising from crypto-asset activities'.

  As such, IOSCO Chair Jean-Paul Servais considers the consultation is a first step towards addressing the current 'regulatory uncertainty' around the regulation of crypto-assets globally.

- The recommendations cover six areas:
  - Conflicts of interest arising from vertical

integration of activities and functions
- Market manipulation, insider trading and fraud
- Cross-border risks and regulatory cooperation
- Custody and client asset protection
- Operational and technological risk
- Retail access, suitability, and distribution.

Timing and next steps

- The due date for submissions on the consultation is 31 July 2023.
- IOSCO has indicated it intends to finalise the recommendations 'in early-Q4 2023'.
- Once finalised, IOSCO expects that jurisdictions will review their regulatory frameworks 'to ensure that they comply with the standards and fix any gaps promptly'.
- The proposed recommendations do not cover activities, products or services provided in the 'decentralised finance' area. IOSCO plans to publish a consultation report with proposed recommendations 'later this summer'.

[Source: IOSCO media release 23/05/2023]

US agencies issue joint statement on their approach to AI-enforcement

Officials from four US agencies – the Federal Trade Commission, the Department of Justice, the Consumer Financial Protection Bureau and the Equal Employment Commission – the agencies responsible for (among other things) enforcing civil rights, non-discrimination, fair competition, consumer protection, have issued a joint statement outlining their commitment to enforcing existing laws/regulations 'to protect the public from bias in automated systems and artificial intelligence'.

The statement acknowledges that while new technologies have the potential to deliver various benefits, automated systems, including AI also have 'the potential to perpetuate unlawful bias, automate unlawful discrimination, and produce other harmful outcomes'.

In light of this, the statement underlines that law enforcement agencies are committed to enforcing existing laws, where necessary, to protect the public.

For example, in the financial services context, the Consumer Financial Protection Bureau (CFPB) recently published a circular confirming that:

> 'federal consumer financial laws and adverse action requirements apply regardless of the technology being used. The circular also made clear that the fact that the technology used to make a credit decision is too complex, opaque, or new is not a defence for violating these laws'.

The four agencies state that they intend to:

> 'monitor the development and use of automated systems and promote responsible innovation. We also pledge to vigorously use our collective authorities to protect individuals' rights regardless of whether legal violations occur through traditional means or advanced technologies'.

[Source: Joint Statement, Rohit Chopra, Director of the Consumer Financial Protection Bureau, Kristen Clarke, Assistant Attorney General for the Justice Department's Civil Rights Division, Charlotte A. Burrows, Chair of the Equal Employment Opportunity Commission, and Lina M. Khan, Chair of the Federal Trade Commission, 25/05/2023]

Financial Services

Top Story | ASIC updates breach reporting guidance for AFS and credit licensees

ASIC recently released an updated version of its guidance on breach reporting (RG 78). MinterEllison has released an article highlighting the key changes. You can access the full text here.

Top Story | Tightening BNPL regulation: BNPL products to be regulated as credit products

Following consultation on potential options to strengthen BNPL consumer protections, the government has announced next steps. Our key takeaways are below.

Key Takeouts

- Following consultation (summarised) the government has confirmed plans to progress the second of the three potential options put forward to tighten BNPL regulation.
- The Assistant Treasurer has indicated that the government plans to consult on the detail of the proposed reforms later in the year, with a view to introducing the necessary legislation into Parliament by the end of 2023. It is not clear at this stage when the changes would commence.

Tighter BNPL regulation on the way

Currently, the consumer protections that apply to other forms of credit regulated under the National Consumer Credit Protection Act 2009 (Cth) (the Credit Act) do not apply to Buy Now Pay Later (BNPL) arrangements, because BNPL falls under the exemptions available to certain types of credit in Schedule 1 to the Credit Act (the National Credit Code).

The government has previously commented that this:

> 'unintended regulatory gap creates the potential for consumer harm due to the absence of key protection'.

Following consultation (summarised) on three potential options to address this issue, Assistant Treasurer Stephen Jones has confirmed that the government plans to:

> 'change the law, so that buy now, pay later products are regulated as credit products'.

Importantly, this is not to say that BNPL providers and the products/services they offer, are proposed to be regulated in the same way as other credit products (eg credit cards) under the Credit Act (we discuss this in more detail below).

The Treasurer provided minimal detail around the changes, instead confirming that further consultation on the detail of the reforms is planned for later in the year.

Here's what we know about the proposed changes and timeline so far.

Regulating BNPL: Introducing an ACL requirement and a 'sliding unsuitability test'

The Assistant Treasurer confirmed that the government plans to progress the second of the three options previously put forward for consultation (summarised). The Assistant Treasurer summed up the proposed changes, briefly as follows.

Under the proposed changes, BNPL Providers would be required to:

- 'hold Australian Credit Licences;
- comply with Responsible Lending Obligations;
- meet statutory dispute resolution and hardship requirements;
- comply with statutory product disclosure and other information obligations;
- abide by existing restrictions on unacceptable marketing; and

- meet a range of other minimum standards in relation to their conduct, and in relation to their products.
- Our plan will give ASIC strong enforcement powers'.

The Options paper itself providers a little more detail on some of these points.

The Options Paper suggests that BNPL providers would be required to:

- hold an Australian Credit Licence (ACL) or be a representative of a licensee, with BNPL providers required to comply with 'most general obligations' of a licensee eg internal and external dispute resolution, hardship provisions, compensation arrangements, fee caps and marketing rules.
- comply with 'modified' Responsible Lending Obligations (RLOs), or a 'sliding unsuitability test' under the Credit Act, 'scaled to the level of risk of the BNPL product or service'.

In addition, BNPL providers would be banned from increasing a consumer's spending limit without explicit instructions from the consumer requesting this.

Fee caps for charges (eg late fees) as well as new disclosure requirements would also be introduced.

Stronger industry Code?

The Options paper also flagged that under Option 2, the existing (voluntary) BNPL Industry Code of Practice (launched by the Australian Financial Industry Association (AFIA) in 2021) would be strengthened in various respects. For example, the Options Paper suggested that:

- the Code could be made mandatory for all BNPL providers and enforceable by ASIC (subject to AFIA submitting the necessary application to ASIC and ASIC's approval). For context, as flagged the Code is currently voluntary and nine BNPL providers - Afterpay, Brighte, Humm, Klarna, Latitude, Openpay, Payright, Plenti and Zip - are signatories However, PayPal, the CBA and some smaller BNPL providers are not Code signatories.
- the Code could be revised to include tighter controls around certain industry practices including: use of consumer fees/charges (including default fees), refunds and chargeback processes, advertising and marketing, and product.

'Strong' ASIC enforcement

The Options Paper suggests that if BNPL were brought under the Credit Act, ASIC would increase its monitoring of the BNPL sector, supported by data collection to enable oversight of consumer outcomes.

It was also suggested that ASIC's industry funding arrangements could be extended to enable the regulator to recover the cost of regulating BNPL from the BNPL sector.

In his address, the Assistant Treasurer said that the government's 'plan will give ASIC strong enforcement powers', but provided no further detail. It's not clear whether it's envisaged that this would be supported by new data collections as flagged above and no mention was made around funding.

Why is this the government's preferred option?

As flagged, Option 2 is the second of three potential options for reform previously put forward for consultation and arguably represents the 'middle ground' in that the government proposes to extend a modified version of responsible lending obligations to BNPL products, without subjecting them to the same level of regulation as other credit products (eg credit cards) as envisioned under the third and most stringent of the three reform options.

Mr Jones emphasised that the government considers Option 2 appropriately balances increased consumer protection with the benefits that BNPL provides eg enabling access to credit for consumers who he said have 'been excluded from traditional forms of credit, and who use BNPL carefully and frugally, to smooth the impact of large expenses'.

Mr Jones said:

> 'We have had to find a balance. And we think we've done it.
>
> Our plan maintains the benefits of BNPL that many Australians enjoy, and we must ensure that providers will have appropriate safeguards in place, and we must ensure that they operate honestly, efficiently, and fairly, in line with other regulated credit products'.

Timing

- Mr Jones flagged plans to consult with industry on the specifics of the changes later in the year.

- It's envisioned that legislation will be introduced into Parliament by the end of 2023.
- It is not clear when the new changes (if/when) legislation would apply.

Initial industry response

In a statement responding to the Assistant Treasurer's announcement AFIA indicated it will continue to work collaboratively with the government on the design of the reforms.

AFIA CEO Diane Tate added that:

'It is good to see the Government acknowledge the important role of BNPL in improving financial inclusion for consumers, increasing innovation and competition, and driving opportunities for retailers'

Stronger protections welcome, but need to see more detail say consumer groups

Consumer groups (eg CHOICE, the Consumer Action Law Centre, the Financial Rights Legal Centre, Financial Counselling Australia) have strongly advocated for BNPL to be regulated in the same way as other credit products are regulated (ie for Option 3) in light of the harms they consider BNPL causes, especially harm to consumers experiencing vulnerability.

In a statement responding to the Assistant Treasurer's announcement, consumer groups welcomed the introduction of stronger consumer protections but emphasised that they need to see more detail before it will be clear whether the changes go far enough. In particular, the statement highlights the importance of ensuring that the proposed 'modified' RLOs are fit for purpose.

CHOICE CEO, Alan Kirkland commented:

> 'To protect people from the unsafe lending practices we are seeing now, these changes will need to include strong requirements for BNPL providers to check that a loan is suitable, regardless of the size of the amount involved. We will be particularly concerned about how the safe lending provisions of these reforms are drafted. While the government has said these will be scalable, we should not assume that small loans are automatically safe. Many of the people who end up in financial hardship as a result of BNPL have smaller loans, often many of them.'

Financial Rights Legal Centre CEO, Karen Cox expressed disappointment that BNPL will not be 'not be treated the same as all other credit' cautioning that 'small amount, low cost credit does not equal safe or sustainable lending.'

Ms Cox also called for all of the new requirements to be enshrined in legislation, rather than in the industry Code, because 'in our experience, complaints under the BNPL Code don't lead to any real consequence or change in industry practice.'

[Source: Assistant Treasurer Stephen Jones address to the Responsible Lending & Borrowing Summit 22/05/2023]

Top Story | Combatting online scams: Government and the banking sector announce new measures

Government and the Australian Banking Association push forward with anti-scam measures following a year that that saw record consumers scam losses

Key Takeouts

- The 2023 Federal Budget includes a number of measures focused on addressing online fraud, including the establishment of a new a new National Anti-Scam Centre (NASC) within the ACCC. The new NASC which will coordinate scam disruption activity across industry sectors, government and digital platforms, is set to be operational by 1 July 2023.
- Separately, the Australian Banking Association (ABA) has announced the launch of a new Fraud Reporting Exchange digital platform (FRX platform) which aims to help banks to respond more quickly and effectively to scams, including through streamlining communication between banks, enabling them to move more quickly to block the movement of money en route or transferred to another bank. The launch of the new platform follows the release of ASIC's report on the big four banks' approach to scam activity (REP 761, summarised) which highlighted various improvement areas.

Combatting scams a key priority

According to the Australian Competition and Consumer Commission (ACCC) losses to scam activity topped $3.1 billion in 2022, a record high, with people experiencing vulnerability also suffering record financial losses. The report also flags that the recent spate of cyber incidents has only increased people's vulnerability to scams.

In light of this, it is perhaps unsurprising that both the ACCC and the Australian Securities and Investments Commission (ASIC) have stepped up their focus on the issue, with ASIC including 'combating and disrupting investment scams' [the highest loss category identified in the ACCC's report] as a key enforcement priority for 2023, and the ACCC likewise identifying scam detection and disruption as a key priority.

The issue is also a focus for government. The 2023-24 Federal Budget ear-marks $86.5 million over three years to combat scam activity and online fraud, including $58 million in funding for the ACCC to move forward with establishing a new National Anti-Scam Centre (NASC).

What the NASC and what will it do?

The Assistant Treasurer described the new NASC as:

> 'the government's primary weapon to detect, disrupt and deter scammers and tackle online fraud'.

Broadly, Mr Jones said that the new NASC, which is planned to be operational by 1 July 2023, will do three things:

- 'use cutting-edge technology to share intelligence across Government and with authorised industry participants to interrupt scams in real time;
- combine the expertise of Government and the private sector to disrupt scams and;
- raise consumer awareness on the risk of scams and how to avoid them'.

Of the $58 million in funding to establish the NASC, the bulk - $44 million – has been allocated to building the technology for the new centre to be able to support high frequency data sharing with a range of agencies, law enforcement and the private sector. This capability is set to be built over the next three years.

The remaining $14 million will be used to fund:

- 'fusion cells' (ie groups of experts with experience/expertise across different sectors which will coordinate scam prevention efforts across government and the private sector)
- education and communications activities in collaboration with the private sector
- ongoing data analysis; intelligence gathering, and scam disruption work.

The ACCC has indicated that in the first year of operation, it's envisioned that the NASC will work closely with ASIC in delivery of its scam website takedown service as well as support the Australian Communications and Media Authority (ACMA) in combatting telecommunications scams.

Coordinating anti-scam efforts across industry sectors, digital platforms and government is identified as a key focus.

More is needed?

While welcoming of the various anti-scam measures being progressed, the ACCC's Deputy Chair Catriona Lowe commented:

> 'While these are all positive steps in the fight against scams, we also believe the work of the NASC would be greatly assisted by the establishment of effective cross-industry standards with coverage and teeth to ensure scammers can't exploit weak links'.

Separately, the Consumer Action Law Centre also welcomed the NASC announcement, but called for further action, including 'new laws that mandate industry action on scam prevention and impose liability for losses when they fail'.

A new cross-industry code on the way?

Reportedly (The AFR) the Assistant Treasurer has committed to the development of a mandatory cross-industry 'co-regulatory' Code by the ACCC over the next six months with a view to the Code being in place by the end of 2023.

ABA launches Fraud Reporting Exchange platform

The Australian Banking Association (ABA) has announced the launch of a new digital platform – the Fraud Reporting Exchange platform (FRX platform) – which aims to:

> 'enable faster and more targeted communication to help banks stop and recover as much money as possible when customers have paid scammers'.

For context, the ACCC has identified traditional bank transfers as one of the most commonly reported payment methods used by scammers.

According to the ABA's announcement, a trial of the new FRX platform showed that the time taken to resolve most scam cases fell by more than 50% - largely through streamlining communication.

Key features of the FRX platform, highlighted in the ABA's launch announcement, include the following:

- 'Near real-time reporting of fraudulent transactions between member banks
- The ability to, where possible, halt multiple fraudulent transactions taking place as part of the same scam
- Shared intelligence between banks to assist with fraud and loss prevention efforts
- A faster, more streamlined return of funds, where possible
- Secure and tracked communications between member banks within the platform with agreed timeframes, reducing the need for multiple phone calls and emails between banks.'

A case of heeding ASIC's call?

The ABA's announcement follows the release of a report from ASIC in April 2023 (REP 761, summarised) into the big four banks' approach to scam activity. While acknowledging the work banks have put in to improving their approaches, the key message running through REP 761 is that ASIC considers banks 'can and should do more to protect Australians from the financial loss of scams', including improving their approach to scam detection and response. ASIC's REP 761 found that 'banks are detecting and stopping a low proportion of scam payments [the report put its at 13%]' with most consumers not recovering their funds.

ASIC's report also flagged that the regulator has commenced a review of the scam prevention, detection and response activities in other parts of the banking industry (that is, beyond the big four banks) and ASIC's intention to monitor the actions being taken by the big four banks in response to the issues identified in the report.

Industry funding for financial counselling services: Government sets timeline

A key message from Labor MP Amanda Rishworth's 17 May 2023 address to the Financial Counselling Australia 2023 National Conference is the government's expectation that companies from the financial services, energy, telecommunications and gambling sectors commit to contributing to the cost of providing financial counselling services under a proposed co-funding model. Ms Rishworth also made clear that the government's expectation is that industry do so by 31 August 2023 in order to ensure that the new independent body (which will distribute the funds) is in operation by 1 January 2024.

Ms Rishworth stated that:

> 'A lot of consultation has been undertaken on the model with the release of a discussion paper on the proposed model in November last year. But with the consultation process now complete, my focus is on securing funding commitments from the industry, including from the online wagering sector. The time for talking is over'.

Ms Rishworth said that to date a number of bodies - including The Australian Banking Association; Responsible Wagering Australia; The Australian Energy Council; The Australian Finance Industry Association; Tabcorp; The Communications Alliance and; The Insurance Council of Australia - have given their in principle agreement to the proposed funding model.

The Department of Social Services has now issued Memorandum Of Understandings industry and, as flagged, it is the government's expectation that these agreements will be 'signed and taken through all internal industry processes by August 31 this year' in order to ensure the new not-for-profit independent body with oversight of this industry-funded model can be fully operational by 1 January 2024.

Timeline for implementation of the new industry funding model welcomed

Responding to this, Financial Counselling Australia (FCA) welcomed the progress being made.

FCA CEO Fiona Guthrie said that having a timeframe for implementation is an important step forward.

> 'The idea of an industry funding model was first raised more than 20 years ago, so this is a momentous development for our sector. Securing the funding commitments will mean the industry funding model will finally

get under way and allow more people to access financial counselling. At a time when demand for financial counselling is manifestly exceeding supply, we need this model up and running as quickly as possible'.

[Sources: Labor MP Amanda Rishworth, Department of Social Services: Address to the Financial Counselling Australia 2023 National Conference 17/05/2023; 17 May 2023 media release 17/05/2023]

APRA will continue to review the suitability of the capital framework in light of recent international bank failures, but for now considers that existing settings remain appropriate

Following recent bank failures in the US and the takeover of Credit Suisse, the Australian Prudential Regulation Authority (APRA) has released an article outlining why the regulator considers the revised capital framework which came into effect from 1 January 2023, is fit for purpose. The focus of the article is on explaining the rationale behind the two main approaches permitted under the framework for calculating capital for credit risk: the standardised approach and the international ratings (IRB) approach.

Ultimately, APRA's message is that:

> 'APRA will continue to review the ongoing suitability of the broader capital framework, taking on board lessons of the recent international bank failures. For now, APRA has confidence that the current credit risk capital framework and the ongoing supervision of its entities, bolstered by recent adjustments, mean that the differences between the IRB and standardised approaches are justified and ultimately deliver on the goals of fair and equitable capital adequacy rules for Australian banks'.

[Source: APRA article: Is the capital benefit of being an advanced modelling bank justified? 23/05/2023]

Strengthening crisis preparedness: APRA finalises standard and guides

The Australian Prudential Regulation Authority (APRA) has released final prudential requirements and guidance for recovery and resolution planning. This includes:

- **Prudential Practice Guide CPG 190 Recovery and Exit Planning (CPG 190)**The g
  - The guidance supports Prudential Standard CPS 190 Recovery and Exit Planning (CPS 190), which was finalised on 1 December 2022.
  - APRA states that the guidance 'has been finalised without material revision to the draft proposals'.
  - CPS 190 will come into effect from 1 January 2024 for banks and insurers, and from 1 January 2025 for RSE licensees. APRA has indicated it plans to engage with entities on their approach to implementation ahead of this.
- **Prudential Standard CPS 900 Resolution Planning (CPS 900); and accompanying guidance** (Prudential Practice Guide CPG 900 Resolution Planning (CPG 900)).
  - APRA states that the finalised CPS 900 and CPG 900 'have not been materially revised from the draft proposals'.
  - CPS 900 will come into effect from 1 January 2024, and will be implemented on an entity-by-entity basis, as applicable.
  - Importantly, APRA states that:

    > 'While CPS 900 will formally come into effect from 1 January 2024, individual entities would only be subject to the requirements of CPS 900 when notified by APRA that it is commencing bespoke resolution planning for that entity. Prior to this, there are no formal requirements under CPS 900 that the entity would need to meet'.

  APRA has also flagged it plans to release 'periodic updates' on APRA's resolution planning program going forward and these will 'foreshadow APRA's future plans for extending bespoke resolution planning to other entities'. APRA's first update is planned to be released 'within the next 12 months'.

  Annex B to APRA's letter provides more detail around implementation.

Announcing the release of the new standard and guidance, APRA Chair John Lonsdale commented:

> 'CPS 190 and CPS 900, and their prudential practice guides, aim to promote the stability of the financial system in times of stress. We expect the requirements and guidance for recovery planning to underpin existing expectations for banks and insurers, which have experience in this area. For superannuation trustees, these requirements are new and will be more challenging. It is important that trustees continue to invest in their crisis preparedness ahead of their formal requirement to comply with CPS 190 at the start of 2025'.

[Sources: APRA media release 18/05/2023; APRA letter: Recovery and resolution planning 18/05/2023]

Consultation on draft Bill to enable AFCA to hear superannuation matters

- The government has released a draft Bill for consultation – [exposure draft] Treasury Laws Amendment (Measures for Consultation) Bill 2023: AFCA jurisdiction to hear superannuation matters – proposing to amend the Corporations Act 2001 (Cth) (Corporations Act) to expand the Australian Financial Complaints Authority's (AFCA) jurisdiction to hear superannuation complaints.
- The consultation follows the decision in MetLife v Australian Financial Complaints Authority [2022] FCAFC 173 which held that AFCA's jurisdiction to hear superannuation-related complaints is limited to complaints listed in section 1053(1) of the Corporations Act (to hearing complaints within the jurisdiction of the former Superannuation Complaints Tribunal, which AFCA has replaced).
- According to the draft Explanatory Memorandum the proposed amendments would 'reinstate the original policy intent following the MetLife decision' for AFCA to hear a broader range of superannuation complaints. Expanding on this, Assistant Treasurer Stephen Jones said that the draft Bill is intended to:

  'clarify that AFCA can consider complaints that "relate to superannuation" in line with its established practice prior to the MetLife decision. The amendments will apply retrospectively to ensure that consumers do not lose access to external dispute resolution and consumers who have had their complaints paused will be able to have their claims considered by AFCA as intended when AFCA was established'.
- The due date for submissions is 16 June 2023.

  [Source: Treasury Consultation: Treasury Laws Amendment (Measures for Consultation) Bill 2023: AFCA jurisdiction to hear superannuation matters 23 May 2023 - 16 June 2023]

Interim updates to APS 610 on minimum capital requirements for PPF providers expected to apply from 'early June'

- APRA has updated Prudential Standard APS 610 Prudential Requirements for Providers of Purchased Payment Facilities (APS 610) to incorporate changes proposed in the November 2022 consultation, aimed at aligning capital requirements for PPF providers more closely with the broader capital framework for other APRA-regulated industries.
- The changes to APS 610 will commence on registration of the standard on the Federal Register of Legislation, which APRA envisions will be 'in early June'.
- APRA states that this is 'interim measure ahead of a broader review of APS 610, which will be part of the implementation of broader reforms to the regulatory framework for stored-value facilities'.

  [Source: APRA media release 19/05/2023]

Accounting and Audit

UK regulator releases new minimum standard for FTSE 350 audit committees

- The UK Financial Reporting Council (FRC) has released a new minimum standard for FTSE 350 audit committees in their role on external audits – the Audit Committees and the External Audit: Minimum Standard –
- The FRC states that the key objective of the new Standard is to:

  > 'enhance performance and ensure a consistent approach across audit committees within the FTSE350. By setting out clear expectations and guidelines, the FRC aims to support the delivery of high-quality audits and reinforce public trust in the financial reporting process'.

- The new Standard has been released ahead of the expected introduction of legislation which will make compliance mandatory, in order to allow audit committees to familiarise themselves with the requirements and enable early (voluntary) adoption.

  [Source: FRC Media release 22/05/2023]

Risk Management

Top Story | Government consults on 'tranche 2' reforms to AML/CTF regime

Following years of reviews, recommendations and debate, Government has released a consultation paper to implement 'tranche 2' of Australia's anti-money laundering and counter-terrorism financing regime.

MinterEllison has released an article outlining the key points. You can access the full text here.

How to approach (and not approach) emerging risk - Insights from an expert panel discussion

An expert panel - Jacqui O'Dea (Chief Risk Officer, GPT Group), Pedram Danesh-Mand (Director, Infrastructure Assets & Places, KPMG) and Carolyn Campbell (CEO Scouts NSW), Chaired by Simon Berglund (Senior Vice President & General Manager, APAC, Diligent) - at the Governance Institute of Australia's Governance Forum 2023, offered insights into 'managing' emerging risk.

The starting point for the discussion is that while principal (or material) risks – the risks you can see – can be managed, the nature of emerging risks necessitates they be tackled differently. These risks are constantly changing and evolving, requiring continual monitoring and continual assessment. Yet, despite these challenges, by incorporating consideration of emerging risks into their strategic thinking, businesses can better position themselves to more rapidly and effectively adapt to change – to build and maintain resilience, which in turn means that they're better able to weather uncertainty. As such, staying on top of emerging risks is critical.

Among other things, the discussion touched on:

- how/why emerging risk management differs from material risk management
- techniques to identify emerging risks
- meaningful reporting on emerging risks
- the role of data

Our key takeaways are below.

Why/how management of emerging risk differs from material of principal or material risk

As flagged, due to the nature of emerging vs principal/material risk, the way organisations tackle them is necessarily different.

Ms O'Dea explained that within her organisation, emerging risks are monitored continually by the risk team, but reported on less frequently – six monthly rather than quarterly.

Every six months, the risk team undertakes a 'deep dive' to distil the key issues, and report on them to the sustainability/risk committee. Importantly, the focus of this reporting is on 'velocity' – the speed at which the emerging risks identified are thought to be approaching – rather than on quantifying the risk (as would be the case for principal/material risks).

In contrast, Mr Danesh-Mand observed that the approach is different in the construction/infrastructure context where the key focus, when it comes to emerging risk, is the level of (potential) exposure.

In terms of the difference in approaching emerging vs principal risk, Mr Danesh-Mand opined that emerging risk requires a different mindset – a whole of organisation mindset rather than a 'my project' mindset because emerging risk management is inherently broader, and entails different challenges.

In terms of identifying emerging risk, Mr Danesh-Mand said that a key challenge can be the potential for conflicts of interest to arise between different areas of an organisation. He added that culture within an organisation also has a 'huge impact' in this context.

Identifying and keeping a handle on emerging risks

The panellists were in agreement that identifying and monitoring emerging risks is a continuous task that requires ongoing focus.

Ms O'Dea nominated four techniques her organisation uses to stay abreast of emerging risk.

- The board: Ms O'Dea suggested directors could be a source of information on emerging risk given their other board roles/positions.
- Industry networks: Ms O'Dea observed that in terms of gaining an external perspective, industry networks can be a valuable source of insight. Ms O'Dea's organisation is a member of the risk leadership network – which has international reach – and has proven to be a valuable source of insight (eg in planning for/approaching the COVID-19 pandemic).
- Paid services: Ms O'Dea also referenced Sention (or other tools), as a means of staying abreast of threats/risks on the horizon.
- Other risk publications: Finally Ms O'Dea referenced other risk publications (eg the World Economic Forum risk publication) as a source of potential insights.

In doing so, Ms O'Dea emphasised the importance of distilling this plethora of information into meaningful insights, specific to/relevant to the organisation.

Mr Danesh-Mand said that in the engineering/construction context, where there is a very strong quantitative focus – even when it comes to emerging risk - scenario analysis and risk modelling is often used in this context.

Being prepared for what's on the risk register

Asked to comment on whether there are specific questions that boards/executives/risk professionals should be asking when it comes to making sure their organisation is prepared for what is on the risk register, the panellists offered the following insights.

- Ms Campbell emphasised the value of continual focus the issue and continual questioning around the potential impact/level of preparedness within an organisation. Considering the hypothetical impact of crises happening to others on your own business, and how this might play out within your own organisation is one way, Ms Campbell suggested of testing/challenging the level of your organisation's preparedness.
- Mr Danesh-Mand spoke about the need to challenge what can sometimes be an overly 'optimistic' mindset within organisations when it comes to emerging risk, and the need to ensure that emerging risks (the downsides of which can be very significant) are not discounted too quickly/dismissed on the basis that they are considered to be unlikely to be 'that bad'. Interrogating
- Ms O'Dea emphasised the importance of the 'voice of risk' within an organisation being heard when it comes to dealing with inherently less visible/quantifiable emerging risk – if this 'voice' is lost/muted, organisations risk taking a short term approach (with all the downsides this entails). Ms O'Dea pointed to climate risk as an example, noting that she has moved climate risk to her organisation's current/principal risk register because she considers that despite the uncertainty, the issue requires that level of focus, and immediate action. Ms O'Dea further suggested that building consideration of risk into decision making – for example, building consideration of risk into the template for every project – can be helpful in ensuring risks are at least identified from the beginning.

Crises as a learning opportunity?

Asked for their views on whether there is something to be learned from a crisis the panellists were in agreement that crises should not be wasted – that is, that crises are a (potential) opportunity.

Ms Campbell opined that crises can be used 'as a carrot' to incentivise and catalyse rapid change on a particular issue or issues (eg internal processes/systems, especially where they may not have been appetite for action to address flaws previously), because the crisis makes clear the need to do things differently, and to act quickly to do so.

Ms O'Dea said that responding to a real or simulated crisis is a source of valuable insights from a risk management perspective. So much so, that within her organisation, crisis training – where the organisation responds to a simulated, realistic crisis in real time - is used annually.

Similarly, Mr Danesh-Mand said that crises can be a learning experience, though he emphasised the need for the response to be a well-considered, and ongoing. Mr Danesh-Mand said that he has observed that in some cases, organisations jump into action before understanding the scale of the crisis, or taking steps to ensure that any learnings/responses identified are embedded and are working as intended. He cited the response by some organisations to the COVID-19 pandemic as an example of this. Mr Danesh-Mand observed that in some instances, organisations developed copious documentation but stopped there – assuming that the documentation of the risk was the end of the task. In doing so, they failed to ensure the new policies/procedures/learnings were implemented (eg no thought was given to the necessary training), resourced or monitored.

The role of data

The panel spoke about the critical role that data plays in improving and informing risk assessments and ultimately, in how organisations prepare for/respond to risk.

A key theme to emerge from the discussion was the challenge of keeping a handle on/perspective on emerging risk – the need to be aware of continually evolving and changing emerging risks on the one hand vs the need to ensure a level of focus on the risks of most relevance/importance to the organisation at this point in time.

This was identified as a challenge both in terms of:

- compromising the effectiveness of organisation's overall approach. Mr Danesh-Mand spoke about a risk register he had seen that ran to 70 pages of very small font, identifying multiple risks as an example of an instance where the tool had become unwieldy and essentially unworkable.
- ensuring 'buy in' from within organisations, and in particular senior leaders. Ms O'Dea opined that overwhelming leaders with a data dump of endless potential risks, rather than offering insights into the key emerging risks relevant to the organisation risks 'losing' them.

The panel was in agreement that it is important to focus on the data that is most important – to focus and report on what you are trying as an organisation, to assess and manage – trying to capture everything can be counter-productive.

[Source: Based on notes from an expert panel discussion from Day 2 of the Governance Institute of Australia National Forum 2023: 'Panel discussion: Managing emerging risks']

In Brief | The Governance Institute has released the: Governance principles for boards of public sector entities in Australia Guide 2023. Updates reflect recent changes to best practice in public sector workplace culture and behaviour and more closely aligns with the fourth edition of the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (Corporate Governance Principles and Recommendations)

[Sources: Governance principles for boards of public sector entities in Australia Guide 2023]

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