Mertons' Corporate Snapshot – April 2018

Mertons' Corporate Snapshot provides you with an overview of current corporate governance matters, including regulatory changes, trends, and other important issues.

To discuss how these may affect you, please contact us on 03 8689 9997

ASIC's new industry funding model

The government has introduced legislation that allows ASIC to recover costs directly from regulated businesses effective 1 July 2017. ASIC's regulatory costs will be allocated across 48 industry subsectors based on actual costs incurred in the previous financial year. Forecast costs for ASIC's regulatory work will be shared by subsector and published in the annual Cost Recovery Implementation Statement (CRIS) each October.

ASIC's costs will be allocated to these subsectors either as a flat fee or as a graduated levy. In January each year, regulated entities will receive an invoice from ASIC via the Regulatory Portal, with first invoices to be issued in January 2019. Detailed methodology for the calculation of levies for each sector is outlined in Report 535: *ASIC cost recovery arrangements 2017–2018* and ASIC has published indicative levies for 2017-18.

New obligations for ASIC's regulated entities

- **Between July and September each year**, regulated entities will provide their business activity metrics for the previous financial year to ASIC. The first collection will occur in July to September 2018.

Regulated entities should have systems in place to capture the information required by ASIC.

Disclosure of material contracts

Several companies have recently had their disclosures about customer contracts and revenue projections called into question by the ASX. The ASX has updated Guidance Note 8 (see below), to include the disclosure expectations for material contracts. As a minimum, announcements should include: customer name, term of the contract, the nature of products or services to be supplied, significance of the contract, any material conditions that need to be satisfied before the customer is legally bound to proceed with the contract, and any other material information relevant to assessing the impact of the contract or the price or value of the entity's securities.

Listed companies that decide to disclose revenue projections for contracts should consider the guidance in ASIC's Regulatory Guide 170 – Prospective Financial Information.

Safe Harbour - what you need to know

The Safe Harbour reforms provide directors with protection from insolvent trading liability if the director "starts taking a course of action that is reasonably likely to lead to a better outcome for the company and its creditors". The legislation is expected to encourage directors to keep control of their company, engage early with possible insolvency and take reasonable risks to facilitate the company's recovery. A 'better outcome' is defined as an outcome that is better than the immediate appointment of an administrator or liquidator.

It's important for directors to document all steps taken when seeking to rely on Safe Harbour provisions. It's also important to understand that Safe Harbour does not affect continuous disclosure obligations. There's no special treatment for companies in financial distress. However, according to new ASX guidance (Guidance Note 8, section 5.10), the fact that directors of an entity in financial difficulty are considering alternatives to administration is not likely to require disclosure, 'unless it ceases to be confidential or a definitive course of action has been determined', in which case, disclosure is required.

The Turnaround Management Association has published a 'best practice guideline' setting out the steps to take if considering Safe Harbour provisions.

ASIC news

ASIC remakes 'sunsetting' class order

ASIC has remade Class Order [CO 08/10] Share and interest sale facilities, which was due to expire on 1 April 2018. More information is available here.

Strikes down, but pay still in focus at AGMs

In a recently released report, ASIC notes that only five ASX 200 companies received a first 'strike' on pay in 2017, and only one of the companies that received a strike in 2016 also received a second strike in 2017. However, there has been an increase in 'close calls', with the number of companies receiving a 20–24% against vote on their remuneration reports increasing to nine in 2017, from five in 2016.

ASIC warns of renewal scam

Scammers pretending to be from ASIC have been contacting registry customers asking them to pay fees and give personal information to renew their business or company name. These emails often have a link that provides an invoice with fake payment details or infects your computer with malware if you click the link. Read more. To notify ASIC of a potential scam email, forward the entire email to ReportASICEmailFraud@asic.gov.au

ASX News

Guidance Note updates

- Guidance Note 8 – Continuous Disclosure. Changes include guidance regarding disclosure expectations for material contracts (see more below) and addressing what needs to be disclosed under the new insolvent trading safe harbour (section 5.10).
- Guidance Note 12 – Significant Changes to Activities. Reflects a change in policy for back door listings requiring all directors or proposed directors to provide evidence of their good fame and character.

Upcoming deadlines for periodic reports

- Quarterly Reports for Mining and Commitments Test Entities – Monday 30 April 2018.
- Annual Reports (December year-end) – Monday 30 April 2018.

Improving Cybersecurity Oversight

A new report by the Harvard Law School Forum on Corporate Governance and Financial Regulation, predicts that the global annual costs of cyber-crime damage will double from US$3 trillion in 2015 to US$6 trillion by 2021.

Despite how pervasive the threats are, 44% of the 9,500 executives surveyed in PwC's 2018 Global State of Information Security® Survey say they don't have an overall information security strategy. PwC's 2017 Annual Corporate Directors Survey found that only 39% of directors are very comfortable that their company has identified its most valuable and sensitive digital assets. And a quarter had little or no faith that their company has identified who might attack.

The report notes that few boards have directors with current technology or cybersecurity expertise and that puts directors at a disadvantage in being able to figure out if management is doing enough to address cyber risks.

The report provides a list of the most common reasons for cybersecurity break down in companies. It also provides a set of challenges or questions for boards to consider, as well as advice for boards on how to improve their oversight. Read the Harvard report.

Managing Culture – a practice guide

'Poor culture can undermine … trust and confidence. By contrast, good culture, which is more conducive to good conduct, helps maintain trust and confidence.' John Price, ASIC Commissioner.

Managing Culture – a Good Practice Guide is a new report by the Ethics Centre, Governance Institute, Chartered Accountants Australia New Zealand and Internal Auditors aims to guide organisations in managing strong corporate cultures.

Common areas that may influence an organisation's risk culture include: leadership, governance, translating values and principles into practice, measurement and accountability, effective communication and challenge, recruitment and incentives.

The guide argues that the board must set the 'tone at the top' and that an ethical framework (including a clearly espoused purpose, supported by values and principles) should sit at the heart of the governance framework of an organisation.

The publication argues that the role of boards is to determine the purpose, values and principles of the company, that senior management have the responsibility for implementing the desired culture and that personnel in human resources, ethics, compliance and risk functions all have a role to play in embedding values and ethics. The guide sets out these key roles and their respective responsibilities.

A global crisis of trust

The 2018 Edelman Trust Barometer presents a picture of global distrust in business, government, not-for-profit organisations, and the media, with 20 out of 28 markets surveyed in distrust territory. For the first time, the media is the least trusted institution globally in 22 of the 28 markets surveyed, and government officials or regulators are the least credible at 35%, despite a ***six***-percentage point increase from the previous year.

"Business is now expected to be an agent of change. The employer is the new safe house in global governance, with 72 percent saying that they trust their own company." CEO credibility rose by seven points to 44% and nearly two-thirds of respondents want CEOs to take the lead on policy change instead of waiting for government.

Building trust is now the no. 1 job for CEOs, ahead of producing high-quality products and services

Maintaining the Social Licence to Operate

The 2018 KPMG and Australian Institute of Company Directors Trust Survey of almost 600 directors paints a similar picture. The study showed that 0ver 94% of respondents agreed or strongly agreed that trust was important to their organisation's sustainability. The top three most critical stakeholders whose trust is required were clients or customers (82% of respondents), employees (82%) and local or regional community in which the organisation operates (35%). Yet, less than half of respondents felt that their board had a proactive approach to building trust with these stakeholders.

Creating value through corporate reporting

The reporting process should be seen as an investment which can bring huge rewards, says Dr Carol Adams, an author, consultant and Non-Executive Director with expertise in financial and non-financial reporting and environmental, social and governance risks.

In an interview with the Governance Leadership Centre, Dr Adams set out some of her research findings, from her interviews with large listed companies on the ASX and JSE, including:

- Integrated reporting has been mandatory in South Africa since 2010.
- In South Africa, corporate reporting processes, and in particular the processes for integrated reporting, influence the way board members think. Directors think more broadly about what value means, about the risks and opportunities facing their organisation and the types of resources they need to run it, and a broader. They also had a stronger understanding of what influences long-term value of and a heightened awareness of the impact of social issues on long term business success.

- Compared to South Africa, Australian directors showed a lower level of awareness of the impact of the environment, social and governance issues, and sustainable development issues, and was not as natural or engrained.

Dr Adams advice to Australian Boards

“I’m surprised that more boards don’t include an understanding of climate change and sustainable development risks and opportunities in their board skills matrix. It is critical to the long-term success of the company.

Also, boards tend to see the annual corporate report as an outcome, and partly a compliance exercise. But it is also a process which can be transformational. What you report influences what you do and how you do it. The reporting process should be seen as an investment which can bring huge rewards.”

Read the interview.
Download the Integrated Reporting Guide.

Sources of information: Ashurst; Australian Charities and Not-for-profits Commission (ACNC); Australian Government; Australian Institute of Company Directors (AICD); Australian Securities and Investments Commission (ASIC); Australian Securities Exchange (ASX); Chartered Accountants Australia New Zealand; Governance Institute of Australia; Grant Thornton; Institute for Internal Auditors – Australia; New Zealand Stock Exchange (NZX); Productivity Commission; The Ethics Centre; Turnaround Management Association.