

AUSTRALIAN GOVERNANCE SUMMIT 2024 #AGS2024

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Update on the regulatory environment

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2024: Context and themes

1. The regulatory state
2. Disclosure-driven sustainability
3. Corporate integrity
4. Workforce and culture
5. NEDs' (expanding?) duty to monitor



The regulatory state (of play)

- The volume and complexity of business and NFP regulation continues to grow, and with it overlapping regulatory mandates
- The quality of that regulation can be variable, increasing the cost and difficulty of compliance and enforcement
- Stakeholders expect that directors will be active in monitoring financial and “non-financial” (conduct, compliance, operational) risks
- Civil penalties for individuals, including for involvement in corporate contraventions, are also increasing (in coverage and quantum)



Volume, complexity, quality

- Across business and NFP, the volume and complexity of regulation continues to grow
 - Legislating for civil penalties against both corporations and individuals continues – for example, unfair contract terms
 - Civil penalty proceedings do not have the same protections for individual defendants as criminal prosecutions, and the penalties (now over \$1.5m for negligence) are probably uninsurable
- The Australian Law Reform Commission's inquiry into the corporations and financial services laws found they are a “tangled mess” and no longer fit for purpose
 - As the ALRC President observed, this has a significant economic and social cost by making both compliance and enforcement more difficult
 - Should the manner in which laws are made, not just the laws themselves, be re-examined? What would work better - the financial sector “regulatory grid”?



The disclosure-driven sustainability imperative

- ‘Sustainability’ – the ability to keep going. Stakeholders (each for their own reasons) may care about whether the corporation’s success can be sustained over time
- We are at a global tipping-point on transparency: mandatory disclosure is intended to make clear (and drive improvements in) the impact of the corporation’s operations on:
 - the climate system
 - the environment: nature, biodiversity, water
 - humans and human society
- For directors, the challenges are capacity and assurance – “reasonable grounds” – given the regulatory and investor focus on greenwashing



The tipping point

- Climate-related financial disclosure laws – the exposure draft legislation released in January raised significant issues about coverage, content, assurance and liability
 - This is a difficult policy to deliver in the context of Australia’s disclosure liability laws
 - The ‘sustainability report’ component of the annual report may eventually include additional environmental reporting eg TNFD
- Human impact reporting: modern slavery, WGEA, Ruggie Principles (human rights), UN Global Compact (SDGs), RAPs
 - For disclosure that requires board sign-off, the Centro principles are the model
 - Delegation and reliance rules require an exercise of independent judgment by directors
 - Will we see the control frameworks for sustainable business behaviour mature and become more integrated, at both management and board levels?



Workforce and culture

- The Closing Loopholes legislation, and changes to the concept of “serious contraventions”, have moved the goalposts
- WHS (including psychosocial risk) and Respect@work obligations sit clearly with the board
- For some corporations, COVID-disrupted work practices remain an ongoing operational challenge
- Culture is a choice, made manifest in what you do and reward, not what you say. Culture binds purpose and governance together



Corporate integrity

- The health of broader systems depends on entities within them acting with integrity. This includes protecting against bribery, corruption, money-laundering, foreign interference, cyber attack
- Whistleblower and PID laws are being strengthened
- Responsible development and deployment of AI matters, because of its potential to undermine autonomy and distort system behaviour



Directors' legal responsibilities

- Where is the case law going?
 - Have the legal responsibilities of directors changed? Has the standard against which “reasonable” efforts are measured moved?
 - Should directors worry about being ‘involved in a contravention’ by the company or others?
 - Member governance disputes – access to books, contested elections, oppression
 - The flow of information to the board
- Law design: Why do evidential and legal burdens matter? Why is a safe-harbour different from a defence different from a duty?
 - A person must exercise reasonable care/ take reasonable steps / is liable if they fail to take reasonable steps / is liable unless they can prove they took reasonable steps
 - Remember the tripod: legal responsibilities, ethical duties, stakeholder accountabilities



Directors' duty to monitor

- Directors and other officers have a duty to take reasonable care when exercising their powers and functions as directors, to address reasonably foreseeable risks of harm to the corporation's interests
- For NEDs, this includes being satisfied that the risk framework, risk appetite and management reporting (escalation) framework are appropriate
- What is reasonable depends on the circumstances (this legal obligation is calibrated, not vague). The liability risk is low, but...

Four areas for heightened vigilance?

POSITIVE REASONABLE STEPS DUTIES

- Affirmative statutory duties to take reasonable steps or measures to ensure compliance, imposed directly on the board
- Examples: annual reporting, WHS, sex discrimination and harassment, FAR, CIS directors' duties
- Watch CA ss 1308 and 1309 – now civil penalties

RED FLAGS

- Directors who ignore red flags – things they personally know are not right – are at risk
- It is not always enough to ask management for reassurance (they may be the problem)

CONFLICTED TRANSACTIONS

- Conflicted transactions should be closely scrutinized
- Disclosing the conflict is not the whole answer – the decision must be in the company's interest
- A careful director will make sure all proper procedures are followed

MISSION-CRITICAL RISKS

- For the individual company, what is the unthinkable (unmentionable) risk? If there is a problem in the sector, it is probably your problem too
- For your company, what else should be on the board agenda alongside, the positive reasonable steps items?