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13 June 2025

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Your reference: **Our reference:** [redacted]

Dear Sir/Madam

Submission for APRA Governance Review - Discussion Paper dated March 2025

Introduction

Thank you for the opportunity to provide a submission to the Australian Prudential Regulation Authority (**APRA**), on APRA's Governance Review Discussion Paper dated March 2025 (**Discussion Paper**).

Norton Rose Fulbright is a global law firm with offices in over 50 locations worldwide, including London, Houston, New York, Toronto, Mexico City, Hong Kong, Sydney and Johannesburg, covering Europe, the United States, Canada, Latin America, Asia, Australia, Africa and the Middle East. We provide global and domestic corporations and financial institutions with a full business law service. We have experts advising our clients on good governance practices across financial services institutions in Australia and globally.

We hope you find our submission helpful as APRA considers options for strengthening its core prudential standards and guidance on governance and remedying areas currently of concern to APRA.

Scope of our submission

This submission does not address all eight proposals in the Discussion Paper, rather we focus our comments on the following proposals which have generated the most discussion amongst our partners and our APRA-regulated clients:

(1) **Proposal 3**:

Extending current RSE licensee conflict management requirements to banks and insurers so they are also required to:

(a) proactively identify actual and potential conflicts of interest and duty;

(b) avoid or prudently manage conflicts; and

(c) take remedial action when conflicts are not disclosed or managed properly.

Requiring regulated entities to consider perceived conflicts, in addition to actual and potential conflicts.

(2) **Proposals 4(a) and (c)**: strengthening independence for the boards of banks and insurers by:

(a) requiring that at least two of their independent directors (including the chair) are not members of any other board within the entity's group; and

(c) extending the current requirement for boards of banks and insurers to have a majority of independent directors to include boards of entities with a parent that is regulated by APRA or an overseas equivalent;

(3) **Proposal 5**: the requirement for significant financial institutions (**SFIs**) to commission a qualified independent third-party performance assessment at least every three years on the Board, committees and individual directors; and

(4) **Proposal 6**: defining APRA's core expectations of the Board, the chair and senior management and providing additional guidance on the delegation of APRA's requirements to board committees and senior management,

(collectively referred to as the **Proposals**).

Summary of our position

There may not be a compelling case for changing APRA's existing prudential standards to give effect to the Proposals. This is because existing requirements arising under APRA's prudential standards on governance, the *Corporations Act 2001* (Cth) (**Corporations Act**), common law and equity provide a sufficiently comprehensive framework for requiring good corporate governance practices on issues such as independent directorships and conflicts management. Furthermore, it has been our experience that most APRA-regulated entities we advise already have appropriate conflict management arrangements in place and implement good corporate governance practices.

Therefore, in an environment where 60 per cent of directors rate compliance and regulation as the number-one issue affecting their board's risk appetite and 70 per cent of directors believe a major deregulation agenda would have a positive impact on Australia's productivity and economic growth[1], we suggest it may be preferable for APRA to use other tools that may be available to it in response to individual instances of non-compliance by APRA-regulated entities. For example, APRA has the power to impose additional licence conditions and to issue directions, which could be a more targeted and proportionate response to governance concerns, rather than making wholesale, cross-industry changes to its governance standards that affect all APRA-regulated entities.

In the alternative, if APRA decides to proceed with changes to its existing governance standards, we provide our feedback on the Proposals below.

Proposal 3 – Conflicts management

In the Discussion Paper, APRA states that it saw weaknesses in how APRA-regulated entities identify and manage conflicts. The most common issues according to APRA are personal financial dealings of responsible persons, directors performing multiple roles across a group, relationships with suppliers and personal affiliations.

Additionally, APRA states that "[c]ontemporary good practice generally involves officers and directors identifying actual, potential and perceived conflicts of interest; disclosing these conflicts to the Board and other stakeholders; actively managing conflicts including through recusal from decisions and structural changes where necessary; and documenting and sharing information as appropriate."[2]

APRA seeks feedback on whether banks and insurers should be required to maintain and disclose registers of duties and interests and what the effect of this would be. APRA also proposes to strengthen the requirements in SPS 521 Conflicts of Interest by incorporating some material that is currently in the guidance into

[1] Australian Institute of Company Directors Director Sentiment Index H1 2025.
[2] Governance Review - Discussion Paper.pdf, p 21.

obligations, which would apply to all regulated industries. This includes APRA's current guidance that entities should actively manage not only actual conflicts, but also potential or perceived conflicts and conflicts that affect the reputation of the business.

We have a number of comments on aspects of this proposal.

First, APRA may wish to carefully consider any changes that might have the effect, in regard to managing conflicts, of removing the distinction between trustees, who have well-established duties as fiduciaries under legislation and common law, and banks and insurers. It will be important that APRA does not inadvertently blur the line between the distinct duties in relation to conflicts that a superannuation trustee owes to its members, versus the obligations of an ADI to depositors and the obligations an insurer owes to policyholders.

Secondly, we consider that this proposal may introduce unnecessary, additional regulation in an area which is sufficiently regulated to an appropriate level. Currently, all banks, insurers and trustees who hold an Australian financial services licence are required under s 912A(1)(aa) of the Corporations Act to have arrangements for managing conflicts of interest (with further expectations set out in ASIC Regulatory Guide 181 Licensing: Managing conflicts of interest (RG 181)). Moreover, there are other legislative requirements (such as Chapters 2D and 2E of the Corporations Act), regulations and common law that apply to conflict of interest scenarios. For listed entities, they are also subject to the ASX Listing Rules which deal with conflicts: such as 'Chapter 10: Transactions' with a person in a position of influence.

In the Discussion Paper, APRA states:

Contemporary good practice generally involves officers and directors identifying actual, potential and perceived conflicts of interest; disclosing these conflicts to the board and other stakeholders; actively managing conflicts including through recusal from decisions and structural changes where necessary; and documenting and sharing information as appropriate.[3]

Directors have well-established obligations in relation to conflicts under common law and statute. This is broadly referred to as the "conflict rule". The conflict rule applies where there is an actual conflict or a substantial possibility of conflict between the director's duty to the company and his or her personal interest. It also applies where a conflict arises between the director's duty to the company and his or her duty to someone else (e.g. another company of which he or she is a director). The courts have accepted that mere acceptance of more than one fiduciary position cannot be allowed to trigger the prohibition against conflicts automatically, since it is generally accepted that company directors may act as trustees or as directors of other companies or in some other fiduciary role, such as the role of solicitor. Relevantly, the High Court of Australia has stated that where there is a conflict of duties, the test of whether there is an actual or substantial possibility of conflict should apply.[4] Other cases support the position that where there is a conflict of duties, the test that should apply is whether there is an actual or substantial possibility of conflict. We consider that the existing conflict rule is arguably sufficient to address APRA's concerns about conflicts.

Proposal 4 - Independence

Proposal 4(a)

Current legislative framework and practices are sufficient

We understand APRA's intention, in putting forward this proposal (along with proposal 4(c)), is to avoid the possibility of potential or actual intra-group conflicts and poor conflict management practices within regulated entities, particularly for individual directors.[5] We agree it is important for regulated entities to manage conflicts appropriately and maintain proper governance and independent decision-making within corporate groups. Based on our experience of advising APRA-regulated entities, it seems to us that most entities have well-established and robust conflicts management frameworks, consistent with the requirements of CPS 510 Governance (**CPS 510**) and other relevant regulatory requirements, such as the Corporations Act provisions

[3] Governance Review - Discussion Paper.pdf, p 21.
[4] *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165; 180 ALR 249; [2001] HCA 31 at [78]–[79].
[5] Governance Review - Discussion Paper.pdf, p 22.

noted above.[6] We note also our comments above, about the conflict rule, which we consider apply equally in the context of proposal 4. Accordingly, we believe there is a good argument that existing regulatory requirements and current industry practices on managing conflicts and director independence are sufficient to ensure there is the requisite degree of independent decision-making and judgement being applied by directors of regulated entities that is consistent with contemporary standards of proper corporate governance. As noted above, individual instances of inadequate conflicts management and insufficiently independent decision-making could be dealt with by APRA effectively (and more proportionately) on a targeted, entity by entity basis using its existing supervisory (including enforcement) toolkit.

Operational inefficiencies and reduction in diverse, group-wide perspectives

Another consideration is that the proposal risks giving rise to operational inefficiencies in internal corporate governance processes for group entities, such as wholly owned cover-holders of insurers. For instance, it is usual for there to be common directors across the boards of a regulated entity and its subsidiaries and/or related entities. In the interests of operational efficiency and facilitating diversity of group-wide perspectives, it is usual for board meetings of regulated entities and its subsidiaries and/or related entities, to be run concurrently for group-wide agenda items. There are advantages to adopting this governance practice:

1. On a practical level, the directors who are common across the boards do not need to sit in multiple board meetings that cover the same agenda topics and presentations.

2. For group executives who need to present and speak at various group entity board meetings, they are not required to provide the same presentation at multiple, separately timed and convened board meetings. Instead, they can give the same presentation once, at concurrently held board meetings.

3. Various entity directors of different boards can benefit from being in the room together at concurrent board meetings and hearing a range of diverse views and perspectives on the matters for discussion and decision, such as risk management (financial and non-financial) and remuneration.

Typically, there is a commonality of interests across group entities, rather than competing interests. Thus, the starting point should be that the interests of group entities are generally aligned. If specific, conflicts arise, they should be managed appropriately on a case-by-case basis.

Lastly we anticipate not only operational inefficiencies but increased costs to APRA-regulated entities and groups if APRA proceeds with this proposal. For example, APRA-regulated entities and their subsidiaries will need to engage more independent directors and hold more Board meetings. This will come at an additional cost which will be borne by shareholders in the case of for profit ADIs, insurers and superannuation trustees and members, in the case of mutuals and profit for member superannuation trustees. The benefits would need to outweigh these costs to justify proceeding with this proposal.

Accordingly, we suggest the introduction of more prescriptive corporate governance requirements concerning director independence is unnecessary and could instead lead to unwarranted inefficiencies and additional cost.[7]

The definition of 'independence' needs to be carefully scoped

The Discussion Paper provides a sample definition for 'independence', as follows:

'a non-executive director who is not an employee of the entity, or the group to which it belongs, and who is free from any business or personal relationship that interferes, or could reasonably be perceived to interfere, with their exercise of objective judgement or acting in the interests of the regulated entity.'.[8]

As currently drafted, the application of this definition is potentially very broad, going far beyond the current definition in CPS 510, particularly with the inclusion of the words *'reasonably be perceived to interfere'.* The Discussion Paper provides limited guidance on its likely scope. If APRA proceeds with this proposal, we

[6] Banking, Insurance, Life Insurance and Health Insurance (prudential standard) determination No. 1 of 2023 - Federal Register of Legislation.
[7] See Microsoft Word - directors - research report.doc, p 57.
[8] Governance Review - Discussion Paper.pdf, p 22.

recommend it carefully scopes this definition and we encourage APRA to do so with the benefit of industry input.

In considering proposal 4, we think it is useful to consider the position in other comparable jurisdictions. For example, the United Kingdom prescribes relatively flexible criteria for determining 'independence' under the UK Corporate Governance Code when considering the duty of independent judgement under the *Companies Act 2006* (UK) (see **Appendix 1**).[9] For the United States, there are a range of relatively nuanced approaches that apply across different entities such as banks and mutual funds, including the criteria for 'independent directors' of funds under the *Investment Company Act 1940* (USA) (see **Appendix 1**). Accordingly, we suggest APRA consider whether its proposals could give rise to the risk of Australia being seen as out of step with other peer jurisdictions.

Proposal 4(c)

We consider proposal 4(c) of the Discussion Paper gives rise to many of the same considerations we have raised above in relation to proposal 4(a). Moreover, based on the wording of the Discussion Paper, we were unclear as to the intended scope of the proposed 'independence' requirements. As drafted, it appears that the proposal could potentially be construed very broadly to:

1. require each subsidiary within an APRA regulated entity group to have a majority of independent directors; and

2. extend to entities in a group that are regulated by a foreign prudential regulator even where no entities in the group are regulated by APRA.

We understand that this is not APRA's intention but would welcome clarification on this point.

Proposal 5

This proposal broadly aligns with recommendation 1.6 of the ASX Corporate Governance Principles and Recommendations (**Principles**).[10] Under the Principles, a Board must have a proper process for regularly reviewing the performance of the Board, committees and individual directors, and periodically use external facilitators to conduct such reviews.[11] This is eminently appropriate for ASX listed entities. For unlisted APRA-regulated entities, we consider it may possibly be appropriate and proportionate to extend these requirements to Significant Financial Institutions (**SFIs**) only, consistent with APRA's proposal. Of course, such a requirement would need to be meaningful in practice to avoid the risk that a reviewer adopts a formulaic or 'tick the box' approach to Board performance reviews, which could lead to an insufficiently meaningful review.

We note that the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) highlighted the issue of superficial evaluations of governance and culture and addressed this explicitly in Recommendation 5.6 – Changing Culture and Governance, which suggested that all financial services entities should (as often as reasonably possible), take proper steps to: (a) assess the entity's culture and its governance; (b) identify any problems with that culture and governance; (c) deal with those problems; and (d) determine whether the changes it has made have been effective...[12]

Moreover, the Royal Commission highlighted those entities (and for the purposes of this submission, SFIs) must undertake much more than an exercise in 'box-ticking'. Rather what is required is 'intellectual drive, honesty and rigour' to evaluate the practices of the Board, committees and individual directors.[13] We suggest therefore that APRA-regulated entities should ultimately be responsible for evaluating the practices of the Board, committees and individual directors rather than APRA or third parties.

[9] *Companies Act 2006* (UK), s 173.
[10] Corporate governance principles and recommendations, p 11.
[11] Corporate governance principles and recommendations, p 11.
[12] Final Report - Volume 1, p 392. See e.g., the Court Enforceable Undertaking between APRA and ANZ, where there were gaps in operational and compliance risk management practices.
[13] Final Report - Volume 1 p 392, 393.

Proposal 6

APRA notes some board agendas place too much emphasis on operational matters, to the detriment of strategic issues.[14] We acknowledge APRA intends to update the existing requirements of CPS 510 and proposes an outcomes-based approach that focusses on clarifying the role of management in executing an APRA-regulated entity's activities, which are based on a board-approved strategy and culture.[15] We welcome the approach by APRA to define more clearly the roles of the Board, the chair and senior management, as well as the APRA requirements which may be delegated to board committees and senior management. However, any such proposal must be consistent with the principles of non-delegable duties in case law and the acts of directors which cannot be delegated to other persons in an APRA-regulated entity.[16]

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[14] Governance Review - Discussion Paper.pdf, p 25.
[15] Governance Review - Discussion Paper.pdf, p 26.
[16] See e.g., *Australian Securities and Investments Commission v MacDonald (No 11)* (2009) 256 ALR 199 and *Australian Securities and Investments Commission v Healey* (2011) 196 FCR 291. The former case held that there was a non-delegable obligation on a statement relating to a significant restructure of the James Hardie group. The latter case held that directors must individual review annual financial statements and cannot delegate such undertaking to other persons.

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Appendix 1- Comparison with other jurisdictions regarding definition of 'independence' and requirements for board composition

United Kingdom	United States of America	Singapore	Australia
Under the UK Corporate Governance Code (**Code**) a board should identify in its annual report each non-executive director it considers to be independent. The Code also outlines the circumstances which are likely to impair, or could appear to impair, a non-executive director's independence, which include, whether a director: • is or has been an employee of the entity/group in the last five years; • has, or has had within the last three years, a material business relationship with the entity; • has received or receives additional remuneration from the entity apart from a director's fee, participates in the company's share option or a performance-related pay scheme, or is a member of the company's pension scheme; • has close family ties with any of the entity's advisers, directors or senior employees; • holds cross-directorships or	The director "has no material relationship with the listed company" as a partner, shareholder or officer of an organisation that has a relationship with the company (s 303A.02 of the NYSE Listed Company Manual). A director is '**not independent**' when: • they were an employee of the listed company within the last three years or an immediate family member is, or has been within the last three years an executive officer of the listed company; • they received or has an immediate family member who received, during any 12-month period within the last three years, more than $120,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation; and • the director, or its immediate family member is a current partner or employee of a firm that is the listed company's internal or external auditor, or is a current employee of such firm. In the case of US mutual funds sold to retail investors, 'independence' of directors is determined on the connections to the fund manager. An 'independent director' cannot be:	The Monetary Authority of Singapore defines' independent director' as 'independent in conduct, character and judgement and has no relationship with the company, its related corporations, its substantial shareholders or its officers that could interfere, or be reasonably perceived to interfere with the exercise of the director's independent business judgment.'[18] Chapter 50 of the *Companies Act (Singapore)* defines 'Related Corporations' as a corporation that is the company's holding company, subsidiary or fellow subsidiary. Rule 406(3)(d) provides circumstances where a director may be '**non-independent**': • a director who has been employed by the company or any of its related corporations for the current or any of the past three financial years; • a director who has an immediate family member who is, or has been in any of the past three financial years, employed by the company or any of its related corporations and whose remuneration is determined by the Remuneration Committee; and	**Proposed requirement of 'independence'** • Requiring that at least two of their independent directors (including the chair) are not members of any other board within the entity's group. • Extending the prohibition on directors who are substantial shareholders in a regulated entity or group from being considered independent, to include material holdings of any type of security. • Extending the current requirement for bank and insurer boards to have a majority of independent directors to include boards of entities with a parent that is regulated by APRA or an overseas equivalent. • APRA proposes to define 'independence' as '*a non-executive director who is not an employee of the entity, or the group to which it belongs, and who is free from any business or personal relationship that interferes, or*

[18] Code of Corporate Governance

United Kingdom	United States of America	Singapore	Australia
has significant links with other directors through involvement in other entities or bodies; • represents a significant shareholder; or • has served on the board for more than nine years from the date of their first appointment." The Code requires that at least half the board, excluding the chair, should be non-executive directors whom the board considers to be independent. The PRA/FCA largely reference the requirements of the Code on the subject of independence and board composition. The PRA will consider optimal board structure on a case-by-case basis and will not as a blanket rule prevent group executive and non-executive board members from sitting on a subsidiary's board, so long as the overall independent balance of the board is maintained. Directors have an overarching duty of independent judgment under s 173 of the *Companies Act 2006* (UK).	• an employee of the fund manager or a member of the immediate family of an employee; • an employee or shareholder with more than 5% shareholding in any registered broker-dealer (whether or not affiliated with the fund manager); • have an affiliation with any recent legal counsel to the fund.[17] The fund board generally must have a majority of independent directors. There is a grace period, generally 90 days, if the fund board has less than a majority of independent directors due to death or resignation. The independent directors are tasked with nominating replacement independent directors. In general, the fund will have an audit committee that consists entirely of independent directors and has the power to hire and fire the auditors. Any legal counsel for the independent directors (which they frequently retain at a board level as a matter of course) must be a separate firm from the fund manager's legal counsel. The fund must disclose to its investors basic information about the identity and business experience of the directors, the number of shares owned by the directors, and information relating to potential conflicts of interest. It is commonly expected that a fund's independent directors will also be investors in the fund.	• a director who has been a director of the company for an aggregate period of more than 9 years (before or after listing).[19]	*could reasonably be perceived to interfere, with their exercise of objective judgement or acting in the interests of the regulated entity.'*

[17] See *Investment Company Act 1940* (US).
[19] SGX Listing rules.

United Kingdom	United States of America	Singapore	Australia
	There is a specific restriction that no fund can have a majority of directors who are all directors, officers or employees of the same bank or banking group. Significantly, it is common and considered a best practice for the same group of individuals to serve on the board of each fund that is managed by the same fund manager (a pooled or clustered board for the whole fund group). One rationale for this is to prevent duplication of presentations and discussions on issues common to many funds in a group, such as shareholder servicing or audit matters. Another reason is for the same individuals to evaluate efficiently (compare and contrast) the performance of funds that follow a range of strategies from the same fund manager. The directors on the pooled board are tasked with overseeing many conflict situations. For example, if a fund manager is rebalancing its fund portfolios and wants to sell stock from one fund to another to avoid paying extra brokerage commissions, this would be reviewed by the board of each fund, and those boards could have the same directors, including independent directors. The idea is that the pooled board, with visibility over a wide range of the fund complex's activities, is in the best position to identify and address conflicts of interest across the complex and for each constituent fund. This can, of course, still lead to the pooled board favoring one fund over another in the complex. For US banks, the usual practice is to have a bank holding company that then owns the bank and certain other businesses, such as an affiliated broker-dealer. Under current law and practice, two independent directors are required for the bank holding company and the bank, and they		

United Kingdom	United States of America	Singapore	Australia
	can be the same individuals. Throughout US federal and state bank regulations, there are various definitions of independence and insider or affiliated status for different contexts, reflecting a nuanced approach to risk (including conflicts) management.		