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Sustainable Finance Forum
The Aotearoa Circle
New Zealand

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Feedback on the Sustainable Finance Forum's Interim Report

The Institute of Directors (IoD) appreciates the opportunity to provide feedback on the Sustainable Finance Forum's [Interim Report](#) (the report). The report summarises why New Zealand needs to shift to a sustainable economy and sets out priority areas and potential pathways for creating a more sustainable financial system by 2030.

The Sustainable Finance Forum fills an important gap to help lead and develop New Zealand's financial system. We welcome the opportunity to contribute and note a strong alignment of intent with IoD, for example, a number of the issues raised in the report are featured in our [article](#) on the top five issues for directors in 2020. Boards have a critical role in leading sustainable success for business and society, and the opportunities and challenges over the next decade will demand high-performing, effective, and progressive directors to drive long-term change.

Our feedback focuses on director and governance related matters including long-term purpose, fiduciary duties and corporate reporting.

About the Institute of Directors

The IoD is New Zealand's pre-eminent organisation for directors and is at the heart of the governance community. We believe in the power of governance to create a strong, fair and sustainable future powered by best practice governance.

Our role is to drive excellence and high standards in governance. We support and equip our members who lead a range of organisations from listed companies, large private organisations, state and public sector entities, small and medium enterprises, not-for-profit organisations and charities.

Our Chartered Membership pathway aims to raise the bar for director professionalism in New Zealand, including through continuing professional development requirements.

Summary

We urge the Forum to take a strategic approach to any proposed corporate governance reform (including taking a holistic and system-wide view of the responsibilities of boards, directors and organisations) and search for opportunities to drive change through leadership and other lateral solutions rather than regulation.

Long-term purpose: There have been a number of initiatives globally promoting the importance of corporate purpose in the last 6 months and we expect to see an increasing focus on this as companies continue to adapt to stakeholder and shareholder expectations of business in the 21st Century. In New Zealand, we support change being driven through leadership rather than regulation. We also encourage the Forum to make a recommendation that New Zealand develop an investor stewardship code to promote long-termism.

Fiduciary duties: Corporate governance regimes around the world are giving more recognition and weight to stakeholder interests. This is also an important matter that deserves greater consideration in New Zealand and we would welcome the opportunity to be involved. We also highlight the trend of increasing director responsibilities and liability and the consequential impact.

Corporate reporting: We highlight the trend and importance of more holistic corporate reporting and note that it's vital to balance requirements with the type and size of entity (eg as per the tiered approach of the XRB financial reporting framework). We also urge the Forum to consider the disclosure burden on all companies (and particularly listed companies) in arriving at recommendations in its final report.

Background

A sustainable financial system is described in the report as a system where value is created today while also valuing the natural and social resources that will provide value for future generations. The report also states that “a sustainable financial system considers material sustainability risks on the sector but also considers the impact the sector has on planet and people. Such a sustainable economic transformation will require financial system transformation, involving the redirection of public and private capital on a massive scale over a short period of time.”

A number of other countries and jurisdictions are progressing similar initiatives including:

- The Australian Sustainable Finance Initiative
- The Canadian Expert Panel on Sustainable Finance
- The European Union High Level Expert Group on Sustainable Finance
- The United Kingdom Green Finance Taskforce.

Global organisations are also taking action. In January 2020, the World Economic Forum launched a Sustainable Markets Initiative (a collaboration with HRH The Prince of Wales) and Larry Fink's annual letter to CEOs around the world (as chair and CEO of BlackRock) was about reshaping finance.

Before commenting on some of the potential pathways set out in the report, we note that corporate

governance reform in New Zealand (and in other jurisdictions and countries) has often been as a reaction to corporate scandals and failures rather than strategically planned. We urge the Forum, in its final report, to take a holistic and system-wide view of the responsibilities of boards, directors and organisations. We also support lateral solutions to raising standards without resorting to regulation, including market-led initiatives.

Long-term purpose and leadership

The Forum states that “currently decision-making is largely driven by short-term financial performance — often at the expense of social and environmental outcomes. A fundamental change to the business leadership and culture is needed to focus on long-term value creation for all stakeholders.”

“Governing for purpose” is one of our top five issues for directors in 2020. In the last six months, we have seen a number of initiatives promoting the importance of corporate purpose including the US Business Roundtable Statement on the *Purpose of a Corporation*, The British Academy’s *Principles of a Purposeful Business* and the launch of the new Davos Manifesto, *Universal Purpose of a Company in the Fourth Industrial Revolution*. We are also monitoring what is happening in other countries and jurisdictions in this space.

Purpose beyond profit is the key to remaining competitive and sustainable in the long-term and needs to be led by the board. The board’s role in strategic thinking and taking a long-term view provides it with the opportunity to champion sustainability across the organisation and set the tone for change to help ensure long-term value creation for stakeholders and shareholders. We expect to see an increasing focus on purpose as companies continue to adapt to stakeholder and shareholder expectations of business in the 21st Century. We support change being driven through leadership rather than regulation. We agree with the report that regulation generally lags leadership and sets a compliance mindset, rather than focusing on the opportunities.

Should New Zealand develop a stewardship code?

Many jurisdictions have investor stewardship codes designed to improve the quality of engagement between investors and companies, strengthen corporate governance, and promote long-term profitability. Codes recognise that large shareholders have a responsibility to engage with boards in a constructive way and to not pressure a company to deliver short-term results. They are often voluntary, and usually apply to institutional investors. Many countries and jurisdictions have stewardship codes in place including the United Kingdom (recently revised), the United States, Australia, Hong Kong, Japan and South Africa.

We encourage the Forum to make a recommendation in its final report that New Zealand develop a stewardship code and we would welcome the opportunity to be involved.

Fiduciary obligations

The Forum states that “existing fiduciary duties do not explicitly require environmental and social factors to be considered and are sometimes interpreted as prohibiting this. The scope of fiduciary duty needs to be reviewed and clarified, along with a move from shareholder focus to stakeholder

focus.”

Today, the issue is not whether a company should account for stakeholder interests but rather the extent to which it should. In the decade since the Global Financial Crisis, corporate governance regimes around the world have been reformed and strengthened, swinging the pendulum away from shareholder primacy, and giving more recognition and weight to stakeholder interests.

In the context of climate change, the Forum’s 2019 legal opinion provides that “directors of New Zealand companies are generally permitted, and will in many contexts be required, to take climate change into account when making business decisions.”

The opinion also states in the context of section 131 of the Companies Act 1993 (the duty of a director to act in good faith and what they believe to be in the best interest of the company) that “it is unclear whether and to what extent a New Zealand court could seek to interpret a director’s duty to act in the best interests of the company as indirectly including a requirement to consider the interests of broader stakeholders.” This is an important matter that deserves greater consideration and we would welcome the opportunity to be involved.

Increasing director responsibilities and personal liability

Boards have to be across an array of complex and diverse issues. They also need to be responsive to increasing stakeholder demands and expectations. New laws targeting directors personally are adding to an already large legal onus and there is greater accountability with active regulators and liquidators and the growth in litigation funding. At the same time, the role of the board is now more important than ever in guiding companies to deliver sustainable success for stakeholders and shareholders. It is critical that boards continue to attract highly skilled, experienced, and responsible stewards for New Zealand’s wellbeing and prosperity.

However, the [2019 Director Sentiment Survey](#) found that the scope of director responsibilities is more likely to deter directors from taking on governance roles now than 12 months ago (40%, up from 33% in 2018). There was also an increase in the proportion of directors (47%, up from 39% in 2018) who agree they are more cautious in business decision-making due to increased personal liability.

We encourage the Forum (and the government and regulators) to take a holistic view of board and director responsibilities. We are very concerned that increasing regulation, coupled with personal liability for directors, will discourage well-qualified people from joining boards, distract attention from long-term business goals, dampen innovation and ultimately diminish corporate governance.

Corporate reporting

The Forum states that “having accurate and comparable data and reporting is a key element in valuing assets and investments. Environmental and social data and reporting needs improved accuracy, comparability and availability to become integral to financial decision making.”

There is a global trend for more holistic corporate reporting, however the particular frameworks

and metrics are still evolving. Many organisations have already adopted established frameworks such as the Global Reporting Initiative or Integrated Reporting to better report on value and tell their performance story and make environmental, social and governance disclosures. It is important that reporting is meaningful to the organisation and its stakeholders, this includes accuracy and comparability. It's also vital to balance requirements with the type and size of entity (eg as per the tiered approach of the XRB financial reporting framework).

We support transparency and appropriate disclosure obligations. However, additional or more onerous obligations can result in too much time spent by directors and managers on compliance rather than performance. We know directors are already struggling under the weight of compliance and red tape. In the 2019 Director Sentiment Survey, 42% of directors said regulatory red tape was a key barrier to economic performance. In addition, 80% of directors said they spent more time on compliance related activities than in the previous year (up from 71% in 2018).

We urge the Forum to consider the disclosure burden on all companies (and particularly listed companies) in arriving at recommendations in its final report.

In December 2019, we submitted on the government's consultation on a proposed climate-related financial disclosure regime for organisations. We supported the proposal to use the Task Force on Climate-related Financial Disclosure (TCFD) framework in New Zealand. However, we raised questions around how it is intended to be implemented, monitored or enforced. We also called for exemptions for some smaller organisations in the list of proposed entities given the existing disclosure burden (particularly for listed companies) and costs associated with complying.

Conclusion

The Forum raises a range of important and complex issues relevant to New Zealand and the future of governance. We urge the Forum to take a strategic approach to any proposed corporate governance reform including taking a holistic and system-wide view of the responsibilities of boards, directors and organisations. There are also opportunities to drive change through leadership and other solutions rather than regulation.

We appreciate the opportunity to comment on behalf of our members and would be happy to discuss this with you.

Yours sincerely



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