Insurance Council of Australia

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Continuous disclosure: Review of changes made by the Treasury Laws Amendment (2021 Measures No.1) Act 2021

The Insurance Council of Australia (ICA) welcomes the opportunity to contribute to the independent review of the 2021 amendments to the continuous disclosure laws made by the *Treasury Laws Amendment (2021 Measure No.1) Act 2021* (The Act).

The ICA's feedback relates specifically to the insurance implications of the 2021 amendments.

Fault element "knowledge, recklessness, negligence" must be maintained

The ICA is firmly of the view that the fault requirement introduced in the 2021 amendments (that an entity or its officers must have acted with 'knowledge, recklessness or negligence' to be liable for breach of continuous disclosure laws) should remain in place.

As was seen prior to the 2021 amendments, the absence of this fault element has the effect of imposing a strict civil liability on entities and directors for breach of the continuous disclosure obligations. Any strict liability presents a significant underwriting challenge for insurers as well as their insured entities and officers, as it removes any potential defence for breach even in situations where the insured entity has acted honestly and undertaken appropriate risk management steps to help ensure compliance. Ultimately the increased underwriting and liability exposure risk adds additional cost to the insurance premiums to those entities and directors subject to the continuous disclosure rules.

To this extent the ICA agrees with the findings of the Parliamentary Joint Committee on Corporations and Financial Services that the 2021 changes to continuous disclosure are a positive step in addressing the imbalance between the benefits to the market of the continuous disclosure obligations and the costs imposed on disclosing entities and their officers from class actions for breaches of those obligations.

The impact of the 2021 amendments on insurance – further time is required

The 2021 amendments to the continuous disclosure laws are a positive step in relation to improving the affordability and availability of D&O insurance in Australia. However, the long tail nature of D&O claims combined with the short period of time these changes have been in place means it is simply too early to make many meaningful observations on the impact on these changes on D&O insurance.

It may take a number of years before more meaningful observations can made on the impact of the changes. This is because there are multiple factors at play that determine the price of D&O insurance premiums.

These factors may include frequency and cost of other types of D&O insurance claims (for example, consumer class actions, of which there have been a recent increase in numbers since the 2021 changes were introduced).

Other factors impacting the price of premiums include changes in and the influx of global capacity and resultant competition in the market (which the Australian market has experienced recently which has contributed to significant decreases in premiums for some D&O insurance customers).

It is possible the 2021 changes may have contributed in very small part to the increase in competition and capacity. However, the significant increases in premiums rates in the preceding three years (required due to historical under-pricing of risk) is likely to have been the main driver to attract new and/or additional capacity.

Similarly, going forward, emerging environmental, social and governance (ESG) risks are expected to become a major source of class action claims on D&O policies which are likely to maintain or add pressure to the cost of premiums.

It should be noted that insurers' claims data indicates that shareholder continuous disclosure class actions began to stabilise prior to the introduction of the 2021 reforms, indicating other factors were also at play (For example, during the extended COVID period many companies did not provide earnings guidance due to uncertainties impacting their businesses).

Significantly, the industry is now beginning to see signs of an uplift in securities class action claim frequency, reflecting the ongoing need to both maintain and monitor the 2021 changes in a more normalised (post-pandemic) economic environment.

However, despite these variables, the ICA and insurers can say with certainty that the 2021 changes will reduce the number of securities class actions from what there would have been in the absence of the reforms due to the threshold requirement of fault-based liability rather than the previous strict liability regime. For this reason and given there has been inadequate time to provide more conclusive observations on the impact of the reforms on D&O insurance, the ICA are of the view the 2021 continuous disclosure law changes should remain in place.

If you have any queries in relation to this submission please contact Tom Lunn, Senior Policy Manager, Regulatory and Consumer Policy at [redacted] or on [redacted].

Kind regards,

Andrew Hall
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