3rd August 2017

Manager
Banking, Insurance and Capital Markets Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: bear@treasury.gov.au

Attention: Ms Kate Wall

Dear Ms Wall

Banking Executive Accountability Regime
Consultation Paper July 2017

The Australian Financial Markets Association (AFMA) is a member-driven and policy-focused industry body that represents participants in Australia's financial markets and providers of wholesale banking services. AFMA's membership reflects the spectrum of industry participants including banks, stockbrokers, dealers, market makers, market infrastructure providers and treasury corporations.

AFMA promotes the conditions that enable financial markets to enhance Australia's economic performance by:

- advocating policies and regulation that support development of the financial markets and user confidence in them;
- encouraging responsible conduct and efficient markets through industry codes, conventions, guides and preparing and maintaining standard documentation; and
- promoting high professional standards through education and accreditation programs.

AFMA members include Australian-owned banks, foreign subsidiary banks and branches of foreign banks who will be required to comply with the Banking Executive Accountability

Regime (BEAR). AFMA is happy to provide additional information about our members or facilitate direct discussions with particular entities if required.

AFMA's submission is comprised of this letter and the accompanying responses to the consultation paper questions.

1. Scope of the BEAR regime

AFMA understands the Government's desire to ensure that financial institutions are held to high standards of accountability and transparency that meet community expectations about how firms govern and conduct their business.

However, the BEAR is a very significant reform proposal, the implications of which have not been fully thought through in terms of its interaction with the current regulatory framework for authorised deposit-taking institutions (ADIs) under the prudential standards and other areas of regulation. The time allowed to comment on the consultation paper does not reflect the significance of the reforms and the implementation effort that will be required. This is exacerbated by the lack of detail in the consultation paper about exactly which organisations and roles the regime will apply to and why, how it will be administered in practice, and how APRA's regulatory powers will interact with other statutory obligations and the powers of other regulators, most notably ASIC. Accordingly, AFMA is likely to make additional substantive comments about the detail of the reforms as they are developed.

AFMA agrees that strong accountability processes are an integral part of the operation of good business, and an important mechanism in enhancing consumer confidence in the financial system. However, the pursuit of policy reforms that impact only on selected entities for reasons that are not properly articulated will likely give rise to longer run, unanticipated outcomes that may actually be detrimental to the financial system and Australia's attractiveness as a place to do business. This is particularly the case in the context of competition if BEAR were to apply beyond the banking activities of ADIs ie. to the subsidiaries of ADIs. It is also relevant to note that foreign banks which are not ADIs service the Australian market from offshore locations in accordance with APRA guidance, and will continue to do so without BEAR applying to them.

It is essential, in the development of new regulatory policy that will impose substantive new obligations and compliance burden on firms and individuals, that actual problems and failures are identified and clearly articulated as the basis for reforms, and that the policy solution is directed at those problems and failures, rather than taking a broader approach for reasons that are not properly defined and explained.

2. Banking business

The BEAR regime implies, by its very name, that it is aimed at bank entities that undertake banking activity. Allowing that a "bank" is an ADI for these purposes, under the Banking Act 1959, "banking business" means:

(a) a business that consists of banking within the meaning of paragraph 51(xiii) of the Constitution; or
(b) business that is carried on by a corporation to which paragraph 51(xx) of the Constitution applies and that consists, to any extent, of:
    (i) both taking money on deposit (otherwise than as part-payment for identified goods or services) and making advances of money; or
    (ii) other financial activities prescribed by the regulations for the purposes of [the] definition.

Only the Reserve Bank and bodies corporate that are ADIs may carry on banking business, and APRA regulates ADIs in the context of their banking business.

Given the reasoning for the introduction of BEAR and the application to ADIs as described in the consultation paper – that is, that banks are in a privileged position of trust, and that prudential regulation is important for consumer confidence in the safety of their deposits - no actual reasons have been articulated as to why the regime should apply to activities that are not banking business and which do not relate to products or services provided to retail customers.

Although the proposals paper suggests that these non-banking activities operate with an ADI brand and therefore poor behaviour has the potential to undermine confidence in the ADI itself, this is inconsistent with the existing prudential framework and APRA regulation. A subsidiary of an ADI is still subject to the prohibition under section 66 of the Banking Act from holding, assuming or using the word "bank" and therefore cannot hold itself out as such. Prudential Standard APS 222 requires the non-ADI group entities in their dealings to give clear, comprehensive and prominent disclosure that:

- the group member with whom the counterparty is dealing is not an ADI and that the group member's obligations do not represent deposits or other liabilities of the ADI in the group; and
- the ADI does not stand behind the group member, unless support is provided in a formal agreement. The nature and limit of such support should also be prominently disclosed where appropriate.

The corporate structure of ADIs varies – some are part of a group where the ADI is the parent company and others are part of a group where the ADI is a subsidiary of a parent. However structured, a number of entities that are regulated as ADIs also have within their group businesses and activities that are not banking business as per the Banking Act definition – for example equity capital markets, debt capital markets, institutional and corporate advisory, securities, derivatives, prime broking, research and custody services - and which are not retail services. These financial services and financial markets activities are comprehensively regulated by ASIC.

Consideration should be given to whether the existing powers and prudential oversight arrangements in APRA Prudential Standard CPS 510 Governance and 520 Fit & Proper could be expanded to include the elements of the proposed BEAR regime. This type of approach would achieve the same policy outcomes, is already familiar to and

understood by ADIs, and could be implemented more efficiently and at a lower cost than new legislation.

3. Competitive neutrality – ADIs and non-ADIs

It is accepted that the BEAR regime should apply to banking business and that there should be a relatively level playing field for ADIs who offer the same types of banking services, given that an entity must be an ADI when carrying on banking business in Australia.

However, the prospect of an uneven playing field is particularly concerning in relation to non-banking activities, especially where they are offered in subsidiaries of an ADI group. It is quite probable that under the BEAR regime, an ADI group that offers non-banking products and services will be subject to additional burdensome regulation in relation to those non-bank products and services, whereas another entity that offers the same products and services but is not an ADI will not be subject to the same regulatory requirements. Even taking into account the stated purpose of the regime (banks are in a privileged position of trust and prudential regulation gives consumers confidence about the safety of their deposits), the differences in regulatory impost on ADI groups compared to non-ADIs in relation to non-banking business is undesirable from a policy perspective, and unwarranted. We believe this is an unintended consequence of the regime that has not been properly considered and which requires further review and examination.

4. Foreign ADIs

Foreign subsidiary banks operating in Australia who provide banking services to retail customers should be considered for inclusion in the BEAR regime in relation to these activities given the nature of the issues that BEAR is seeking to address (ie. consumer confidence).

However the position is different with respect to the main business of branches of foreign banks in Australia, which tends to be a combination of corporate lending, trade finance, wholesale funding, provision of risk hedging, treasury functions, and securities trading offered to other ADIs, large corporate borrowers and depositors. APRA's longstanding policy prohibits the provision of these services to retail consumers, and indeed, it is a standard condition of a foreign ADI's authorisation by APRA that the bank must not accept initial deposits of less than $250,000 from individuals. This prohibition on deposit taking creates a practical disincentive to doing other forms of business with retail customers.

Under the Basel Accord, the prime responsibility for oversight of a foreign ADI rests with its home supervisor, and this is recognised through APRA's prudential standards. Although a foreign ADI is subject to APRA's supervision in respect of its Australian operations there are limits to the control APRA can exert over the entire operations of a large complex cross-border group which happens to have a branch in Australia.

The prudential standards recognise explicitly the role of the home jurisdiction supervisor in respect of the foreign bank's Australian operation. For example, the obligations in CPS 510 Governance and CPS 520 Fit & Proper apply only in relation to the Australian branch operations of that institution, and not to the institution's global operations. This is a highly practical position for APRA to adopt.

The current prudential framework also to a certain extent acknowledges that the senior roles within the branch of a foreign ADI are not equivalent to the senior roles within locally incorporated banks. A significant part of the management of a local branch is influenced by the strategy, governance and control framework of the global institution and management located offshore.

Group subsidiaries of a foreign ADI located in Australia typically do not sit directly under the Australian branch, are not subject to the direct control or management of the branch, and these lines of business commonly have reporting lines outside of Australia. It is not appropriate that these subsidiaries are subject to the BEAR, as they are neither part of the operations of the foreign ADI's Australian branch, nor are they managed or controlled by the Australian branch. The regime could have a potentially unintended extraterritorial effect if applied to group entities incorporated offshore which, although technically subsidiaries of the ADI, do not otherwise have any relevant nexus to Australia.

If the BEAR is to apply to foreign ADIs, it should be limited to the foreign ADI and its employees within the scope of the current framework to prevent unintended consequences. The BEAR should not be applicable to the foreign ADI's related entities.

The stated intention of the regime is to enhance the responsibility and accountability of ADIs and their directors and senior executives, rather than replacing or changing the existing prudential framework. To this end, in line with existing concepts of responsibility and accountability, such as definitions of 'responsible persons', 'director' and 'senior managers' under APRA's Fit & Proper framework, we are of the view that the BEAR should apply only to the foreign ADI's most senior personnel ordinarily resident in Australia. If any local employees are to be included, only the most senior management would be appropriate. We suggest expressly restricting application to the Head of the Foreign Bank Branch.

More generally, careful consideration needs to be given to the potential impact of BEAR on the Australian market's attractiveness to foreign financial services firms. There are significant potential unintended consequences that may arise for global and regional resource allocation decisions away from Australia and to other financial hubs including Hong Kong and Singapore if the BEAR model does not provide the appropriate scaled approach for foreign ADIs who in most cases are subject to substantive control frameworks in their home jurisdictions.

5. Remuneration

As a matter of principle and good corporate governance, boards and their remuneration committees should retain accountability for setting and managing remuneration arrangements. It is not clear how APRA's enhanced powers in relation to remuneration will interact with the existing responsibilities and rights of boards and shareholders – for example, will APRA's powers override rights with respect to approving equity grants.

There is a risk that any increase in deferrals of variable compensation will result in fixed pay being perceived as more valuable by employees, and there could be market pressure to increase fixed pay.

Deferred variable remuneration is likely to reduce the perceived and time-discounted value of awards resulting in ADI groups shifting a larger part of remuneration from variable to fixed, in order to remain competitive in attracting and retaining talent, which is not a desirable outcome. Remuneration deferral requirements are likely to have a negative impact on the attractiveness of senior positions in ADI groups compared to positions in non-ADI groups and other sectors and jurisdictions that are not subject to such rules. This has potentially serious implications in terms of ensuring sufficiently skilled and qualified people fill senior positions.

Foreign ADIs are subject to home jurisdiction rules about remuneration as well as comprehensive internal controls and requirements, including Risk and Control review of senior employees' remuneration and performance, and in some cases claw back provisions for employees. The deferral requirements may also give rise to potential barriers to entry and competiveness issues, in particular where ADIs will not be permitted to vest deferred variable remuneration over the 4 years.

Many foreign ADIs have global compensation deferment schemes in place that have been agreed with the relevant home regulator and that would meet the policy objectives of BEAR. Any variation to a firm's global compensation scheme to meet prescribed BEAR variable remuneration requirements would require manual workarounds by the global compensation teams within the firms. Consideration should be given to whether the BEAR regime can accommodate substitution provisions or some other form of recognition to enable a foreign ADI to adopt comparable home country requirements about remuneration where it achieves essentially the same outcomes as the proposed Australian regime.

The flow-on effects of a shift towards more fixed pay may include increases in the banks' cost base, a diminished capacity to reduce costs in times of stress, and a limitation on the usefulness of remuneration as an incentive tool.

We have made some suggestions as to how these outcomes could be mitigated in the response to the consultation paper questions accompanying this letter.

6. Regulator responsibilities

It appears that there will be a significant degree of intersection between the proposed BEAR framework and other regulation to which ADIs are already subject including APRA's existing prudential framework, the Australian Financial Services Licensing obligations under Part 7.6 of the Corporations Act, directors duties under the Corporations Act and other statute, the ASX corporate governance requirements for listed entities, and home regulations for foreign ADIs. While it is intended that ASIC's role will continue as it is, how the regulators will operate together in administering the regulatory regime as a whole is a key issue for organisations and individuals in understanding all of their compliance obligations and in meeting the expectations of the community. It is expected that the regulators will work closely together to produce appropriate detailed guidance for industry as quickly as is feasible, and that they will ensure maximum efficiency in the implementation of BEAR given the potentially overlapping obligations.

7. Insurance against civil penalties

In the context of civil penalties against ADIs and disqualification powers against accountable persons, the consultation paper raises the question of whether the ADI and accountable person should be precluded under BEAR from taking out insurance against civil penalties and the exercise of disqualification powers, respectively. It is common for insurance not to extend to criminal conduct and indeed, public policy renders void any insurance or other indemnity in respect of serious criminal conduct. There are specific statutory limits on the availability of insurance against civil liability for regulatory obligations, including some breaches of directors' duties under the Corporations Act. The purpose of the regime in acting as incentive against poor conduct is understood. However, if ADIs and accountable persons are precluded from taking out insurance against civil penalties and disqualification, this will significantly increase the risk to which ADIs and their executives are exposed, perhaps well beyond what the reasonable person would expect to be the case given the size of the possible penalties. This is therefore a matter that should be left to the ADIs, accountable persons and their insurers to determine.

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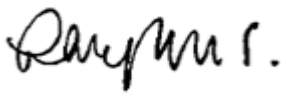
If you have any queries about this submission or would like additional information from AFMA members please contact me on tlyons@afma.com.au or 02 9776 7997.

Yours sincerely



Tracey Lyons
Head of Policy

Banking Executive Accountability Regime – Consultation Paper responses

Consultation paper question		AFMA comment/position
Individuals to be covered by the BEAR		
1	Does the prescriptive element of the proposed definition of accountable persons capture the roles which, at a minimum, should be subject to enhanced accountability under the BEAR? 1.1. Are there any other roles which should be included at a minimum? 1.2. Should any of the roles be excluded?	The BEAR should apply to an ADI and entities in the ADI group that conduct banking business. The definition of "accountable persons" should not apply to individuals in ADI subsidiaries as a prescribed matter. The most effective application of the regime would be to individuals who perform the most senior functions within the ADI group and meet the applicable principles-based test, irrespective of which ADI group entity they are employed by or in which ADI group entities the businesses and functions they are responsible for are conducted. CPS 520 provides a suitable starting point for determining which roles should be in scope. There should be a greater emphasis on a principles-based approach to determine "accountable persons". This would improve the effectiveness of the regime by ensuring that those individuals who have significant influence over conduct and behaviour and whose actions could pose material risks to the business and its customers are within scope. This will be particularly important given the large variation and complexity in the structure of many ADI groups. However, we appreciate that including a prescriptive component to the definition of accountable persons assists with ensuring that key functions are included and that there is a level of consistency in application across ADIs. Consistent with the objective of providing sufficient flexibility to address differences between ADIs (eg. taking into account different corporate structures and role descriptions), APRA should have the ability to approve modifications to the prescribed persons by applying an "if not, why not" rationale where appropriate. This approach is consistent with the objective of the BEAR to apply a heightened responsibility and accountability framework to the most senior executives within the ADI.

Consultation paper question		AFMA comment/position
		The BEAR model that is ultimately adopted must acknowledge the existing differences between the organisational structures of domestic ADIs and foreign ADIs. Domestic ADIs are most often the parent company of non-ADI subsidiaries. This is generally not the case for foreign ADIs who have globally aligned organisational structures which tend to be more complex in nature, with primary reporting lines generally offshore. Foreign ADIs are generally the local branch of a parent bank based in a different jurisdiction, rather than an independent legal entity. Branches are not capable of independently holding shares in subsidiaries. Further, any subsidiaries even if incorporated in Australia, may be held through complex structures with numerous levels of ownership across different offshore jurisdictions. The subsidiary may ultimately be beneficially held by the same legal entity which has a foreign ADI branch, but that legal entity may not be the direct parent of the subsidiary. Therefore, for foreign ADIs the scope of BEAR should be limited to activities, products and services covered by the foreign ADI itself. That is, the scope should not creep out to the activities, products or services provided by related bodies corporate. Apart from the CEO, the "executive function" roles set out in Table 1 (Chapter 4 of the consultation paper) do not correlate to the key roles in the Australian organisational structure of many branches of foreign banks. Many senior persons in these functions with primary reporting lines to the Board are based offshore. To make the structure outlined in the consultation paper workable, the CEO would need the authority to delegate various responsibilities/accountabilities to persons internally. However, it is not expected that the BEAR regime will be used as a mechanism to create local responsibilities for individuals where they do not currently exist. Accordingly in respect to foreign ADIs it should be expressly noted that only the Head of the Foreign Bank Branch is applicable for foreign ADIs in terms of the functions listed in Table 1.

Consultation paper question		AFMA comment/position
		In light of the existing fit and proper person assessment for the Senior Officer Outside Australia (SOOA) required by CPS 520, the inclusion of the SOOA role in the BEAR is an unnecessary territorial over-reach of jurisdiction by Australia, is inconsistent with the UK PRA Senior Manager Regime and HK Manager in Charge regimes, and duplicates the existing and to date effective prudential supervision and Banking Act powers APRA already has – for example, section 23 of the *Banking Act 1959* (the Act), which provides that APRA may direct the foreign ADI to remove a person from the role of SOOA if the person does not meet one or more of the criteria for fitness and propriety set out in the prudential standards. It has been suggested that this may be the appropriate time to merge the SOOA concept into the BEAR regime – namely, by focussing first on the appropriate onshore senior/C-suite level personnel. If that person(s)' level of control is deemed insufficient to meet the objectives of the existing prudential standards and the BEAR, then the foreign ADI could be required to appoint a SOOA-type offshore executive. To the extent the definition of "accountable person" is broader than the CEO role i.e. Head of the Foreign Bank Branch for foreign ADIs, to address the possibility that other management roles are captured, there should be a minimum salary threshold requirement applied in addition to a demonstrated level of seniority/authority for the proposed executive function to be caught. Some other regulators use a tiering system to categorise accountable persons – so for example, the executive team of a large local institution are Tier 1, and he next levels down are Tiers 2 and 3. The different tiers are subject to scaled remuneration and conduct requirements. More generally, questions have arisen about the extent to which chairs of committees such as risk and audit are undertaken by different people than the executive roles pertaining to those functions e.g. the CRO and the CFO. The description of the chairs of committees as "overseeing the performance of [the committee]" seems to overstate the chair's role.

Consultation paper question		AFMA comment/position
2	Does the principles-based element of the proposed definition of accountable persons provide sufficient flexibility to reflect differences in business models and group structures?	A greater emphasis should be placed on the principles-based approach to BEAR rather than attempting to prescribe a larger number of accountable persons or responsibilities at a granular level. With proper oversight from APRA, this will enable each ADI group to right-size the approach for their organisation without diluting the intent of the regime. However, it would be helpful if there is more clarity and guidance around what will be considered material in terms of "significant influence" and "pose risks". The regime should be focussed on behaviour that has potential material or systemic outcomes for the ADI. As noted in the response to Question 1, organisational structures vary across organisations, particularly between local ADIs and foreign ADIs, and there are differences between the permitted activities of local ADIs and foreign ADIs. There should be a relatively level-playing field for entities carrying out the same activities. As foreign ADIs are not permitted to engage in the same extent of regulated activities as local ADIs, it makes sense that there would be differences in the application of the BEAR to foreign ADIs and local ADIs. The principles based element of the "accountable persons" definition can accommodate these differences in structure between ADIs, subject to the comments provided above in Question 1. Group subsidiaries of a foreign ADI located in Australia do not necessarily sit directly under the Australian branch, are not subject to the direct control of the branch, and operate lines of business that have reporting lines outside of Australia. Extending the definition of "accountable persons" in the "executive function" to anyone beyond the "Head of Foreign Bank Branch" would amount to seeking to interfere with the governance structure and arrangements of the wider firm, as it would effectively require the Australian branch to allocate responsibility to certain functions, regardless of their size and complexity and overall whole firm internal and external (home state regulator) governance arrangements and requirements. The principles based part of the proposal does not clarify how BEAR would treat people who are unit heads or similar but based overseas. For foreign

Consultation paper question		AFMA comment/position
		ADIs it is sometimes the case that line 1 staff have a solid reporting line to a person based offshore but a dotted line to the local country head.
3	Should the definition of accountable persons apply to individuals in the subsidiaries of a group or subgroup with an ADI parent, including where the subsidiaries are not regulated by APRA?	The BEAR should not apply to Australian incorporated subsidiaries or other Australian incorporated entities in the same group as a foreign ADI, on the basis that these entities have historically not been within APRA's jurisdiction as they do not conduct banking business, and are regulated by other local regulators (namely ASIC). As such, the "accountable persons" requirement should not apply to individuals/executives of these entities. Similarly, foreign subsidiaries of ADIs which operate solely outside of Australia should also be excluded from the regime. Based on our understanding of the UK PRA SMR, the PRA does not, in extending its regime to UK branches of foreign banks, extend to subsidiaries of those incoming branches. The Hong Kong MIC regime does not extend to Hong Kong branches of foreign banks, but limits its regime to those entities that it directly regulates. The definition should not apply to persons whose activities are for related bodies corporate of the foreign ADI. The inclusion of locally incorporated subsidiaries or other Australian incorporated entities in the same group as the foreign ADI gives rise to the risk of unintended consequences, which could ultimately create an uneven playing field. To the extent there is interplay between ASIC and APRA powers, the requirements of the two regulators should be harmonised – for example in relation to: (a) these entities being subject to both APRA's "accountable persons" requirement and ASIC's "Responsible Manager" regime; and

Consultation paper question		AFMA comment/position
		(b) locally incorporated subsidiaries or other Australian incorporated entities in the same group as the foreign ADI being regulated by APRA, but non-ADIs providing the same services in the Australian market not being regulated by APRA. Notwithstanding the above, if it is determined that the definition will apply to subsidiaries not regulated by APRA, the manner in which the definition is intended to apply to foreign ADIs needs to be clarified having regard to their offshore ownership structures. Specifically, a foreign ADI may be a branch of a foreign bank, rather than an independent legal entity. Branches are not capable of independently holding shares in subsidiaries. Further, any subsidiaries even if incorporated in Australia, may be held through complex structures with numerous levels of ownership across different offshore jurisdictions. The subsidiary may ultimately be beneficially held by the same legal entity which has a foreign ADI branch, but that legal entity may not be the direct parent of the subsidiary.
Expectations of ADIs and Accountable Persons under the BEAR		
4	Do the options canvassed for the expectations of ADIs capture the behaviours that should be expected under the BEAR? 4.1. Are there any other behaviours which should be included? 4.2. Should any of the behaviours be excluded?	The new expectations are intended to identify a heightened standard of conduct and behaviour, to support the prudential regulation objective of consumer confidence in the safety of their deposits. Given that the intention of the new regime is to build on, rather than replace, existing concepts of responsibility and accountability including APRA's Fit and Proper Framework (under which senior managers in an ADI are subject to fit and proper assessments) it is vital that the additional or incremental criteria, responsibilities and conduct expectations that are to be imposed, and which are not otherwise covered under the existing framework, are clearly expressed. This will assist to avoid duplication or overlap in oversight by one or more regulators, and clarify compliance obligations for ADIs.

Consultation paper question		AFMA comment/position
		Substantial clarity and guidance is needed on what will constitute 'taking reasonable steps' and how APRA will assess this. Clear non-prescriptive guidance from APRA is required about (a) where they would use the new powers, and (b) the factors that would be taken into consideration. BEAR should focus on systemic conduct and not capture one-off events that are not the result of misconduct or irresponsible management. While the intention of the BEAR is to ensure that senior executives are accountable, it should not create a separate basis for individual liability. The accountable person's responsibility and liability should be linked directly to the impact of their behaviour on the ADI. In the context of directors' duties, it is accepted that a director should be entitled to delegate to a person who they reasonably believe is reliable and competent (see section 190 of the Corporations Act). Section 189 of the Corporations Act similarly entitles a director to rely on expert advice from a person the director reasonably believes is competent to provide the advice. Any test of 'reasonable steps' in the BEAR must incorporate equivalent concepts in order to be workable. It will also be important to understand how the 'reasonable steps' test will be applied to foreign ADIs who in many cases do not deal with consumers – will the expectation under the reasonable steps test differ for foreign ADIs? For example, in section 5 of the consultation paper one of the 'Expectations of the ADI' is to ensure that the expectations and accountabilities of the BEAR are applied and met throughout the group or subgroup of which the ADI is parent. Where foreign ADIs are concerned, should 'ADI' be construed to mean the Australian branch of the ADI? If not, and it instead means the whole bank globally, then BEAR appears to have significant extraterritorial reach. The Government's intentions need to be more clearly articulated in this area. There may be a potential tension between "collective" board/management responsibility and individual accountability. Based on the information that is currently available, BEAR does not

Consultation paper question		AFMA comment/position
		reflect or recognise the reality of a degree of collective decision making in large institutions, and there is also a risk of conflict with company law principles.
5	Do the options canvassed for the expectations of accountable persons capture the behaviours that should be expected under the BEAR? 5.1. Are there any other behaviours which should be included? 5.2. Should any of the behaviours be excluded?	Due to the broad nature of the expectations of ADIs and accountable persons, there appears to be considerable scope for overlap between APRA's oversight and that of ASIC. Ideally, where a material conduct issues arises only one regulator should undertake any relevant investigation and enforcement action. The obligation to be "open and co-operative" needs to be further defined. There are potential issues from a legal perspective concerning legal professional privilege and how that may apply in connection with being open and co-operative.
	Remuneration	
6	Would deferring variable remuneration be likely to result in a shift from variable to base remuneration? Would this be problematic and, if so, can anything be done to prevent this outcome?	There is a risk that any increase in deferrals of variable compensation will result in fixed pay being perceived as more valuable by employees, and there could be market pressure to increase fixed pay. Deferred variable remuneration is likely to reduce the perceived and time-discounted value of awards resulting in ADI groups shifting a larger part of remuneration from variable to fixed, in order to remain competitive in attracting and retaining talent, which is not a desirable outcome. Remuneration deferral requirements are likely to decrease the attractiveness of senior positions in ADI groups compared to positions in non-ADI groups and other sectors and jurisdictions that are not subject to such rules. This has potentially serious implications of ensuring sufficiently skilled and qualified people fill senior positions.

Consultation paper question		AFMA comment/position
		Many foreign ADIs have rolled out globally home jurisdiction rules about remuneration as well as comprehensive internal controls and requirements, including Risk and Control review of senior employees' remuneration and performance. However this may also give rise to potential barriers to entry and competiveness issues, in particular if ADIs will not be permitted to vest deferred variable remuneration over the 4 years. The effects of fixed pay may include increases in the banks' cost base, a diminished capacity to reduce costs in times of stress, and a limitation on the usefulness of remuneration as an incentive tool. To prevent these types of outcomes, either or a combination of: (a) a proportionality approach based on the ADI's size and complexity; and/or (b) pro rata vesting (i.e. vesting a proportion in each year of the deferral period); and/or (c) application of de minimis thresholds could be introduced. Proportionate application in particular is important because each firm has its own unique risk and remuneration practices. Since there is a very large range of risk appetites across firms, a "one size fits all" approach will inevitably not be able to cover the whole range of practices. Certainty is required that, if the SOOA is included in the regime (which is not AFMA's preferred outcome), the SOOA's remuneration is excluded, on the basis this is not an executive role. As the SOOA is the representative/delegate of the Group Board of the wider foreign firm and may also be performing an executive function in the overseas head (or regional) office, it would be an

Consultation paper question		AFMA comment/position
		inappropriate territorial over-reach by APRA to seek to dictate the compensation structure of a member of a Board of the institution as a whole.
7	What are the complexities in defining variable remuneration, including in relation to non-cash remuneration?	There are limited complexities in defining variable remuneration as such. However, the value of variable remuneration can vary between the date of issue and the time of vesting. More clarity is required as to when the value of the variable remuneration is to be determined, for the purpose of compliance with the 60% deferment rule. Many foreign ADIs have global compensation deferment schemes in place that have been agreed with the relevant home regulator and that would meet the policy objectives of BEAR. Any variation to a firm's global compensation scheme to meet prescribed BEAR variable remuneration requirements would require manual workarounds by the global compensation teams within the firms. Consideration should be given to whether the BEAR regime can accommodate substitution provisions or some other form of recognition to enable a foreign ADI to adopt comparable home country requirements about remuneration where it achieves essentially the same outcomes as the proposed Australian regime.
8	Does the proposed principles-based definition of variable remuneration provide sufficient clarity as to the application of the BEAR to current and potential future remuneration structures?	Much more clarity needs to be provided around: (a) whether the relevant year is the year where the performance occurred that earned the bonus/variable component, or the year in which the bonus was awarded to the employee; and (b) whether any vesting periods will apply – for example, in the UK variable income can begin to vest after 3 years. The UK also has a de minimis concession so that if an individual earns less than total GBP 500K and his/her variable pay for the performance year is not more

Consultation paper question		AFMA comment/position
		than 33% of total remuneration, the firm can use its discretion to apply the remuneration rules, in terms of years to defer and percentage to defer if any. Aspects of the proposed requirements pose greater concerns for foreign ADIs who are subject to home regulator requirements and are influenced by the strategy and control framework of their global institution. Depending on the structure of an international group's bonus pool arrangements, the application of the BEAR to subsidiaries could effectively purport to force the application of the same rules to the entire group and in countries where BEAR does not have any jurisdiction nor does APRA have any responsibility for macro-prudential stability. The extra-territorial impacts of the proposals should not be ignored and must be taken into account in the cost/benefit analysis. Clarity is required as to whether principles-based recognition for variable remuneration defined through existing compensation schemes that broadly meet the BEAR remuneration policy objectives will be deemed adequate, or if a strict 4-year minimum deferral period will be enforced. Clarity is also needed in relation to how existing compensation schemes afoot will be handled – for example, will there be grandfathering arrangements?
9	Is the proposal for deferring 60 percent of the variable remuneration of certain executive accountable persons appropriate?	It has been noted that a 4 year deferral period would put Australia out of line with international practice (which is generally 3 years). This taken together with the 60% deferral are hard "rules" rather than a principles based approach. Principles that are consistent with a foreign ADI's home regulatory practice should align with APRA's published remuneration policy stance. This would also be consistent with APRA's stance that banks should design their own risk management tools and not rely on APRA to determine what the rules are.

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		It may be more proportionate/appropriate that only executives who earn a minimum variable pay for a calendar year are captured by the 60% deferral. In the UK this threshold is GBP 500K. This ensures that the deferral percentage is more broadly proportionate to risk taken on behalf of the firm (assuming that higher variable pay correlates with higher risk taking). Senior roles within the branch of a foreign ADI are not equivalent to the senior roles within locally incorporated banks. This proposal is more problematic for foreign ADIs as they are subject to home jurisdiction rules governing remuneration as well as comprehensive internal requirements and controls. Foreign ADIs prefer to be able to continue to apply the deferment schemes agreed with their home regulators, so that the business in Australia remains consistent with the broader group, provided that those existing arrangements satisfy the key objectives of the BEAR. Some firms have global compensation deferment schemes in place where a significant portion of variable compensation is deferred for employees beyond the scope of the "accountable person" definition as per the consultation paper. These frameworks ensures a closer alignment of employee and investor interests by linking a greater proportion of variable compensation to the firm's own equity and debt instruments and subjecting awards to longer deferral periods. For example, for all employees with a total compensation above a specified amount, a specific amount of the overall performance award is deferred. Clarification is needed for foreign ADIs that deferral of 60% of variable remuneration is limited to the CEO-equivalent i.e. the Head of the Foreign Bank Branch.

Consultation paper question		AFMA comment/position
10	Are the proposed enhancements to APRA's remuneration powers appropriate?	Boards and remuneration committees should retain accountability for setting and managing remuneration arrangements. It is not clear how APRA's powers will interact with the existing responsibilities and rights of boards and shareholders – for example, will APRA's powers override rights with respect to approving equity grants. Any direction by APRA to reduce the variable remuneration of an accountable person must be subject to due process and oversight by an appropriate body. Clarity is also required in relation to practical issues such as what constitutes, and who determines, an "inappropriate outcome", and the right of appeal mechanism. There is no information about how APRA's powers will operate or co-exist with a foreign ADI home regulator's jurisdiction. For commercial reasons we have not included information here about the specific remuneration control arrangements that global entities are subject to and have agreed with their home regulator, but access to information can be arranged if required.
Registration and Accountability Mapping		
11	Should ADIs be required to map the allocation of prescribed responsibilities, similar to the approach under the Senior Managers Regime in the United Kingdom? 11.1. Are there any other prescribed responsibilities which should be included? 11.2. Should any of the prescribed responsibilities be excluded?	Where it has been implemented in other jurisdictions, the mapping requirement is seen as a useful business process that helps to create clarity within the firm, creates greater certainty about responsibilities, and reduces bureaucracy. However, mapping of prescribed responsibilities in exactly the same manner as the UK regime will inhibit a firm's ability to allocate responsibilities in a way that suits its business structure. APRA operates on a principles based approach rather than prescriptive requirements, and this should be reflected in the BEAR framework including in the mapping requirements. By way of comparison, the HK MIC regime requires an organisational chart to be provided to the regulator which sets out the organisation's governance and management structure, business and operational units, key human resources and reporting lines, including all "managers in charge" and their roles and responsibilities.

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		A more tailored approach should be adopted for foreign ADIs by excluding some of the "prescribed responsibilities". A number of these responsibilities would be difficult to map to local "accountable persons" as they are globally driven policies or processes – for example development of remuneration policies; responsibility for independence, autonomy and effectiveness of a firm's policies and procedures on whistleblowing and so on. CPS 220 should be used as a guide for linking any prescribed responsibilities to how the ADI manages its material risks. The role and responsibility of the SOOA is defined by APRA pursuant to CPS 510 and CPS 520. As such, to the extent the SOOA is included, we seek confirmation that the only feasible and logical "accountability statement" of the role and responsibility of the SOOA to be produced by a foreign ADI under the BEAR is a statement which is consistent with the role and responsibilities as set out in CPS 510 and CPS 520.
12	Should ADIs have discretion to add to the prescribed list of responsibilities?	Entities have scope to add functions and individuals through the principles-based element of the regime.
Removal and Disqualification		
13	Are the options canvassed for enhancing APRA's removal and disqualification powers appropriate?	It should be made clear that the removal and disqualification powers will only be exercised where there is a systemic or prudential issue that will have a material impact on the ADI. Clarity is needed on the implications of removing/disqualifying "accountable persons" when the individual does not meet the expectations under BEAR – that is, can an individual be appointed an "accountable person" of the same entity or another APRA regulated entity in the future? How long will the disqualification last and will it be made public? Will this information be shared with other regulators and will they be entitled to act on the mere fact of the removal or disqualification and

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		not be obliged to undertake any other enquiry or investigation? While it is understood that the regime is intended as a deterrent to poor behaviour, the consequences for individuals who are subject to removal or disqualification are potentially very severe and as such, they should be entitled to fair process. Clarity is required on matters related to the administrative of the regime such as who determines whether an individual has not met the expectations under BEAR – APRA, an independent industry panel or some other mechanism, and how the appeal process will work for "accountable persons". Any removal and/or disqualification of an individual should be determined/ratified by an appropriate independent panel and appeals mechanism. Discussions with Treasury to date have indicated that this type of guidance will be provided in due course, but until it is available there is substantial uncertainty for organisations and individuals about their obligations and the rights that will be afforded to them. If the process of applying to the Federal Court for removal of a senior manager no longer applies, then it is essential that appropriate procedural fairness arrangements are in place. A review process is even more critical given the subjective nature of the standards of conduct proposed to be mandated (e.g. “with integrity’, “prudent” and “due care”). To the extent the SOOA role is included, the APRA removal and disqualification powers proposed in the BEAR consultation paper should, for the avoidance of doubt, in the context of the SOOA role, be expressly limited to the performance of the SOOA role.

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Civil Penalties		
14	Are the proposed circumstances in which the civil penalties should apply appropriate?	Constitutional restrictions limiting the exercise of judicial power mean that APRA cannot require payment of a civil penalty without recourse to the courts. Clear guidance is required as to how APRA intends to use the civil penalty power. If the policy intention is that APRA's powers would generally be reserved to address the most egregious conduct or behaviour that is of a systemic and prudential nature, this should be clarified in the implementing legislation, or as an alternative, in explanatory materials and guidance. The consultation paper notes that it is intended that there should be proportionality between the seriousness of the contravention and the quantum of the penalty. The UK regime has an entire chapter in the FCA Enforcement Guide about how penalties are calculated that is publicly available. Other disciplinary bodies have issued clear guidance as to the expected penalty ranges for each category of behaviour/conduct/breach. APRA should be similarly transparent given the significant size of the potential penalties. The scale of the proposed civil penalties, combined with the ongoing potential for sanctions from other regulators, has the potential to confuse ADIs in their dealings with regulators. There is a real prospect that the same conduct or misconduct by an ADI or a subsidiary could amount to a breach of both an ADI's responsibilities under the BEAR and a contravention of a range of other civil penalty or other provisions to which the ADI or subsidiary is subject. For example, significant systemic failures in the wealth management business of an ADI could give rise to civil penalty provisions under the FOFA regime as well as the BEAR regime. Further guidance on the interaction of APRA's powers with other regulators is required, particularly as to whether, in this type of situation, APRA or ASIC would take the lead in civil penalty proceedings or whether each could commence proceedings within their respective jurisdictions. Arguably, it is not an appropriate use

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		of time and resources for an ADI to be subject to separate proceedings by the two regulators, and APRA's powers in this regard should be limited to scenarios where another regulator is unable or unwilling to act. The BEAR legislation should include provisions analogous to those in the Corporations Act that, in effect, prevent a person from being held to be both criminally and civilly liable.
15	Is the proposed definition of large ADIs appropriate?	The definition is consistent with other legislation.
General Implementation and Transition Issues		
16	What would be a reasonable period of time after the passage of legislation for ADIs to implement the BEAR?	Foreign ADIs face additional implementation complexities by virtue of being part of a global organisation, which need to be taken into account. Experience in the UK and other locations suggests that an implementation period of a minimum 2 years is needed, with the implementation of compensation arrangements potentially taking longer. AFMA is generally supportive of a phased implementation approach. Treasury and the Government also need to be mindful of other current APRA regulatory initiatives impacting ADIs that are costly and resource-intensive to implement such as Economic and Financial Statistics (EFS) reforms. Clarity is required on the interplay with the current prudential framework and how this impacts on the Responsible Persons (i.e. CPS 510, CPS 220) and Fit and Proper (i.e. CPS 520) regimes, and responsibilities for making the annual Risk Management Declaration.

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17	How significant are the costs associated with implementing the BEAR? How can these costs be mitigated consistent with the policy intent of the BEAR?	Costs can be mitigated by avoiding regulatory duplication and/or conflicting regulatory requirements. It is difficult to determine the costs to implement the BEAR until further detail is available with respect to the scope, implementation timeline, and any external audit requirements. Many firms are not able to determine yet the extent to which the firm and in scope "accountable persons" will require assistance from external consultants or legal advisors. There will also be significant ongoing maintenance costs related to the regime. Costs will also vary given the size and scope of different institutions. It is expected that recruitment costs will increase as a result of implementation of the regime to compensate for the increased inherent risks of the BEAR. The cost of the potential uneven playing field between ADIs and non-ADIs, and between large ADIs and small ADIs in terms of attraction and retention of staff is very difficult to quantify. Implementation of bespoke Australian compensation regimes (that do not take account of other requirements) would be costly.