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29 September 2017

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

Dear Sirs

Banking Executive Accountability Regime

On 13 July 2017, the Australian Treasury released a Consultation Paper seeking feedback and comments in relation to policy considerations involved in the design of a Banking Executive Accountability Regime (**BEAR**) announced by the Government in the 2017-18 Budget. We made detailed submissions in relation to the Consultation Paper.

On 22 September 2017, the Australian Treasury released an exposure draft of the *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017* (**Bill**) and accompanying Explanatory Memorandum (**EM**). We are pleased to see a number of our submissions in relation to the Consultation Paper reflected in the Bill.

Clifford Chance now welcomes the opportunity to provide submissions in relation to the Bill.

Clifford Chance

We are one of the world's pre-eminent law firms, with more than 3,300 lawyers across 5 continents led by a single integrated partnership. We were named the number 1 law firm in Chambers Global Top 30 for the years 2014, 2015 and 2016.

We have significant experience working with clients globally in relation to individual accountability regimes, including with respect to implementation assignments for global banks in relation to the United Kingdom Senior Managers and Certification Regime (**SMR**) and Hong Kong Manager-in-Charge Regime (**MIC**), preparing joint submissions on behalf of global banks to regulators in relation to the SMR and assisting regulators (via secondees) with drafting proposed rules and consultation papers.

Submissions

Our views and recommendations expressed below are confined to the Australian commercial and jurisprudential context. Further, the content of our submissions are not intended to be exhaustive nor do they constitute legal advice.

Cognisant of the detailed submissions to be submitted by various industry groups, we have confined our submissions to what are, in our view, some of the overarching issues.

Timing

1. Per [1.155] of the EM, the BEAR provisions are to apply from 1 July 2018. The UK *Financial Services (Banking Reform) Act 2013*, which gives legislative effect to SMR (upon which the BEAR is based), was passed in December 2013. The SMR went live in March 2016, over two years later, in which intervening period there were extensive consultations with the industry and rules published by the regulators. It is worth noting that the SMR developed from the arguably similar Approved Persons Regime and that UK has long had exposure to broad principles-based enforcement regulation.

   The time proposed be afforded to ADIs to implement the BEAR is far too short. The determination of "accountable persons", reduction of their responsibilities to writing, accountability mapping exercise and associated actions will not be without difficulty, as was the UK experience. Further, to date Australia's banking industry has had nothing like the level of industry consultation that characterised the introduction of the SMR and, given the intervening time between now the proposed introduction of the BEAR, it is not likely to have this benefit. Finally, the potential penalties associated with ADI breaches of the BEAR are the largest in Australian history.

   In the circumstances, our view is that the 1 July 2018 date should be extended.

"Systemic and prudential" matters

2. In our view, greater conditionality should be incorporated into the Bill to make clear that the principles-based definition of "accountable person" [37BA] and, additionally, the obligations to be incumbent on them and ADIs [37C - 37CA] are framed by reference to "systemic and prudential" matters in accordance with the policy intent of the BEAR. For example, under the general principle of determination as to whether a person will be an "accountable person", which rests on the concept of management or control of the ADI or subsidiary or of a significant or substantial part of the same, what constitutes management or control should be determined with reference to "systemic and prudential" aspects of the ADI's business and not otherwise.

It is not enough that the civil penalties for ADIs [37G] are referable to "prudential matters". Without the above conditionality, the BEAR regime may be subject to considerable confusion and potential overlap with ASIC's remit.

Obligations

3. The obligations to be imposed on ADIs and "accountable persons" are lifted from the UK regime. They are broad principles-based regulation that do not have an established history in Australian jurisprudence. The EM at [1.49] states that the key terms comprising the obligations, including "honesty", "integrity", "due skill" and "diligence", and "open, constructive and co-operative", while not defined in *Banking Act 1959* (Cth), have their ordinary meaning well understood, are used in other laws and have been considered by established case law. The laws and cases are not specified.

We do not share Treasury's apparent view as to the clear-cut nature of these obligations. As we stated in detail in our previous submissions, the guidance given by policymakers and authorities as to what these behaviours mean in practice is critical. For example, does acting with integrity mean simply abiding by applicable laws or is something else required? This debate is occurring now in the UK, underscoring our point. Such guidance is essential for ADIs and "accountable persons" to appreciate the expectations being placed on them. Great efforts were made in the UK to ensure that the industry had the benefit of such guidance and we hope to see APRA issue detailed guidance in due course.

Breach reporting

4. We think that the breach reporting requirement [37FC(d)] is framed too broadly, particularly given the existing broad nature of the obligations that will be placed on ADIs and "accountable persons". If it remains unchanged, this could lead to confusion and stress ADIs' resources.

One means of balancing the requirement is to qualify that only "significant" breaches should be reported and also introducing an objective "reasonableness" test to make it easier for ADIs to make reporting decisions. This approach would align with the position vis-a-vis AFSL breach reporting to ASIC, with which ADIs are familiar, and would also take into account the proposals in ASIC's enforcement review on breach reporting that is currently underway (and which itself borrows from the UK regime upon which the BEAR is based; accordingly, there would be multiple alignments).

Disqualification

5. The proposed powers to accrue to APRA to take punitive action as against "accountable persons" [37J] lack sufficient procedural fairness mechanisms. They are more draconian than the corresponding UK regime upon which the BEAR is based. In relation to the UK FCA, its Regulatory Decisions Committee (**RDC**), made up of the FCA's Board Members, make decisions on behalf of the FCA regarding penalties, prohibitions, etc. The RDC is separate to the FCA investigations team (we expect APRA will ensure similar mechanics are in place) and, in making its decision, an appreciable number of procedural fairness provisions are in place for example, written submissions, representations meeting, etc. Any decision of the RDC is appealable to the Upper Tribunal.

   Given the significant professional and personal consequences of any adverse decision made by APRA with respect to an "accountable person", it is our view that Part 6 of the *Banking Act 1959* (Cth) should apply to the BEAR, such that APRA's decisions will be reviewable by the Administrative Appeals Tribunal. As a corollary, APRA will have to set out its findings on material questions of fact; refer to the evidence or other material on which those findings were based; and give its reasons for confirming, revoking or varying the decision, as the case may be.

Remuneration

6. The Bill proposes a requirement on ADIs to have a remuneration policy which mandates that, if an "accountable person" is (emphasis added) "**likely** to have failed to comply..." with an obligation under the BEAR, that person's variable remuneration will be reduced in proportion to the likely failure [37E(1)(b)(ii)]. In our view, as a matter of contract law and procedural fairness, this requirement is problematic.

   If a concern exists that an "accountable person" is likely to have breached their obligations, there should be provision for simply extending the deferral period by a short timeframe (say 3 months) to enable investigations to be conducted and conclude. A decision regarding remuneration consequences can then be made on the resulting evidence, as opposed to what arguably amounts to subjective speculation.

Industry engagement

7. We note the additional budget to be provided to APRA to administer the BEAR in the 2017-18 Budget Papers. The regulator's resources to engage with the industry around implementation, including by issuing guidance with respect to the practical meaning of the obligations imposed on ADIs and "accountable persons", will be critical.

As we stated in our earlier submission, a sizable number of consultation papers and guidance notes were issued and industry-engagement exercises were undertaken in the UK. We hope that the same will occur in Australia.

We thank you for considering our submission in relation to the Bill.

If you wish to discuss our submission, please contact Angela Pearsall, Partner at angela.pearsall@cliffordchance.com or Liam Hennessy, Senior Associate at liam.hennessy@cliffordchance.com.

Yours faithfully

Clifford Chance