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Mr Bede Fraser
The Treasury
Langton Crescent
PARKES ACT 2600
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Dear Mr Fraser

Exposure Draft - Corporations Amendment Regulation 2013 (*Grandfathering*)

Introductory comments

The ABA would like to express our appreciation for the efforts of your team in addressing a number of technical matters associated with the application of the Future of Financial Advice (FOFA) reforms, and in particular the impact of these reforms on the banking industry. The complex nature of the financial advice system has resulted in implementation challenges with regards to the retail banking business and in application challenges for bank staff across banks and banking groups, so we appreciate your ongoing efforts to discuss and resolve outstanding legal uncertainties and technical issues.

The ABA welcomes the opportunity to provide comments on the proposed Regulation amendments to clarify the conflicted remuneration provisions, amendments to the grandfathering provisions (s1528) and a contracts savings provision.

The ABA would like to express support for the Financial Services Council (FSC) and the Australian Financial Markets Association (AFMA) submissions regarding these proposed regulations. With this in mind, the ABA restricts our comments to the areas that represent specific potential impact to retail banking operations.

Clarity is needed around the meaning of employment arrangements and the application of the grandfathering provisions for existing employment arrangements as well as for new employees and existing employees who change positions under those arrangements

The draft regulation, and the law to date, does not adequately provide clear grandfathering protection for the range of employment arrangements (workplace agreements, remuneration systems, salary packages, and performance bonus payments of employees of banks and banking groups) in place across banks and banking groups. As drafted, the regulation is focused on platform operators, but there is legal uncertainty for other arrangements.

As previously raised with the Government, banks and banking groups are unsure how to treat employment arrangements, and in particular agreements or contracts with employees who provide advice to retail clients.

There are several critical issues that need to be resolved, including:

- Treatment of existing employment arrangements and transition to new arrangements (where necessary); and
- Treatment of bank staff who start working with banks or banking groups, existing staff who move between roles or positions with new conditions (but contained within existing arrangements), or existing bank staff who have their conditions and requirements altered, on or after the commencement date of 1 July 2013.

Existing employment arrangements

Bank's employment arrangements vary from institution to institution depending on the operating structure and business model. The following provides some indications of existing workplace arrangements used across banks:

- *Employment agreements:* These agreements are generally ongoing and tend to include provisions for employees to be eligible to participate in a reward program with outcomes based on key performance indicators. Some of these reward programs can be varied or cancelled at any time. (We note that there are also legacy agreements in place across banks and banking groups.)
- *Enterprise agreements:* These agreements are negotiated and approved by Fair Work Australia and can contain provisions for employees to receive discretionary payments. Incentive plans and variable reward schemes (including the details of scorecard methodology and the nature of targets) are typically contained in separate policy documents, but are generally subject to provisions contained in the enterprise agreement. Enterprise agreements are usually rolling in nature and negotiated to be in place for a fixed term (i.e. 2-5 years) until the expiry date, unless there are significant and material changes. Consultation and amendment arrangements, including with employee and union representatives, varies from bank to bank. The renewal arrangements generally align with the banks' financial reporting year, being for many member banks, 1 October.
- *Contractual agreements:* These agreements are generally based on fixed terms and tend to include detailed provisions on remuneration structures, including commission payments or performance bonus payments. Contracts can be individual or business related. Termination clauses tend to be strict with little ability for unilateral variation. (We note that termination or variation of these agreements would need to comply with various laws, for example, for business contracts the Franchising Code of Conduct which has effect under the *Competition and Consumer Act*. We also note that commission payments and interests are clearly detailed in the Financial Service Guide (FSG) of banks operating an agency or franchise network.)

The ABA believes that the grandfathering provisions should clarify that where a bank or banking group has in place an employment arrangement with locked in salary and performance pay increases which is automatically renewed each year, but negotiated periodically, that those existing salary and performance payments are deemed not conflicted for the period that the existing arrangement is in place. The regulation should ensure that if an arrangement might be conflicted remuneration after the commencement date, that the salary and performance payments are not to be deemed conflicted while the existing arrangement is in place, however, at the time when the arrangement is renegotiated, those salary or performance payments that might be conflicted remuneration should not be renegotiated into a future or new employment arrangement.

In the absence of clarification, banks and banking groups would face significant legal and practical issues, including:

- Legal implications of having to modify agreements or contracts;
- Operational implications, including risk of losing employees, reduction in productivity, risk of confusing customers, or reduction in availability of products and services;
- Practical implications and change management, including modelling of new arrangements, redesign of incentive plans and reward programs, redevelopment of remuneration policies, and modifications to systems used to calculate bonus pool arrangements;
- Employee expectations with regards to access to base salaries and performance pay increases, bonus pool arrangements and performance/incentive payments, communications with employees, and negotiations with employee and union representatives on proposed changes; and
- Shareholder expectations with regards to bank staff performance and contribution to company value and communications with shareholders, stakeholders and other interested parties in banks' financial performance.

Furthermore, it is essential that banks and banking groups are not exposed to potential action where banks are taking reasonable steps to ensure future or new salary and performance payments are compliant, yet seek to ensure no prejudice or disadvantage for their bank staff by changing (or being forced to change) existing arrangements or contracts. It is also essential that banks have grandfathering protection so there is no legal or regulatory uncertainty with regards to the anti-avoidance provisions.

The ABA notes that we are seeking clarification of the treatment of performance benefits paid to bank staff subject to balanced scorecard arrangements which should allow banks and banking groups to identify payments which might be conflicted remuneration and/or establish evidence that existing payments may be retained in new or future employment arrangements.

Recommendation: Insert a new regulation which clarifies that the renewal of employment arrangements where payments made for work carried out (not already specifically excluded), salary and performance pay increases and conditions are set and the terms of the agreement are set does not require payments to be changed, even if these payments might be conflicted remuneration after the commencement date, until these existing arrangements are renegotiated.

Treatment of bank staff

Additionally, under the laws and regulations proposed to date, it is unclear whether an employment arrangement includes all workplace arrangements, including employment agreements, enterprise agreements and contracts. It is also unclear whether the grandfathering arrangements cover the terms of an incentive plan or reward scheme or an annual payment (i.e. performance pay subject to a balanced scorecard arrangement) discretionary or otherwise.

Due to these factors, currently there is significant doubt over whether banks and banking groups can rely on the grandfathering provisions with regards to existing payments made for work carried out (other than salary) for existing employees and whether new employees who join post 1 July 2013, or employees who are transferred within an organisation after 1 July 2013, would be able to receive the benefit of grandfathering (i.e. would they fall under the existing arrangements/schemes? would this depend on the performance year?).

Without clear grandfathering protections for these arrangements or situations and in the absence of clarification, banks and banking groups would face substantial legal uncertainty and operational and compliance risk. For example, existing bank staff and new bank staff operating under the same workplace arrangement may be required to have different payments and conditions. Not only would this expose banks to unnecessary compliance complexity, it would result in employees being on different arrangements for comparable roles and positions, which would be unfair to bank staff. In practice, banks and banking groups would need to implement and monitor different employment arrangements, payment structures and rules for

different employees for different periods of time, or alternatively, be required to move existing employees to new arrangements part way through their performance year (and questionably whether this is legally possible).

If the treatment of bank staff is not addressed, banks and banking groups will have less than 3 months from now to develop new payments, structures and schemes for new employees or existing employees who shift to a new role or position within the institution and covered by an existing arrangement – which will result in different payment structures (i.e. salary and performance pay increases), remuneration strategies, compliance frameworks and potential financial outcomes for different classes of employees performing the same roles or positions.

Recommendation: Insert a new regulation which provides that remuneration arrangements will not have to change for new or transferring employees (i.e. new employees or existing employees who change roles or positions or have new requirements for their existing role or position covered by the existing employment arrangement) and in these situations banks and banking groups can rely on the grandfathering protections with regards to those payments, structures and schemes as contained in existing employment arrangement.

Grandfathering is not clear where a clients' interest in a financial product changes in a non-platform environment

Additional provisions have been drafted which would have the effect of allowing clients to increase their interests in managed investment schemes or superannuation schemes without being taken to have acquired a new financial product. However, similar provisions have not been inserted for products that would be appropriate in a non-platform environment.

The ABA believes that there is legal uncertainty as to whether a rollover of a term deposit would constitute the replacement of one financial product with another, and therefore would result in a loss of grandfathering protection. We consider that a specific exemption is required to ensure grandfathering is not lost in this and similar situations. As drafted, the regulations will result in the loss of grandfathering despite the fact the client's account is still active and the client is still "invested" in the financial product or fund.

Recommendation: Clarify the application of the regulation to non-platform operators. For example, insert a new regulation or sub-regulation to provide that "rollovers" or "reinvestment" into term deposits (on maturity) held via a custodial, non-custodial or other fund structure is not an acquisition of a new financial product provided the client is still invested in the same financial product or fund.

The regulation or sub-regulation should also clarify that:

- during 1 July 2013 – 30 June 2014, grandfathering will apply to new clients and new financial products where benefits are given under an arrangement entered before 1 July 2013; and
- new clients and new financial products post 1 July 2014 will not be grandfathered.

The ability of a party to enforce a term or condition even though it may be conflicted remuneration is problematic

Draft sub-regulation 7.7A.17 appears to have the effect of enabling a party with in an interest to the arrangement to demand a payment or payments be made despite the fact that these might be unlawful due to being deemed conflicted remuneration (by way of its impact on Division 4 of Part 7.7A of Chapter 7 of the Corporations Act).

The ABA believes that draft sub-regulation 7.7A.17 is a complicated regulation made under s1101H(3) and may impact the common law presumption that parties intend for an agreement or contract to terminate where there has been a material change in its terms as a result of a change in the law.

The ABA notes that this matter is related to legal uncertainty with existing employment arrangements and a new regulation should operate seamlessly with grandfathering protection for existing arrangements and treatment of bank staff.

Recommendation: Insert a new regulation to allow for the extension of grandfathering protection to new arrangements replacing existing arrangements terminated as a result of the FOFA reforms.

The ABA hopes that these comments and drafting suggestions assist you in finalising these regulations. We would be happy to discuss any aspect of our submission with you.

Yours sincerely



Dade Edwards