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## The Financial Accountability Regime - Consultation

Dear Manager,

The Westpac Group (**Westpac**) supports extending the principles of the Financial Accountability Regime (**FAR**) to all APRA regulated entities and is pleased to provide a submission in response to Treasury's Proposal Paper (**Paper**) on the FAR. Westpac was one of the first authorised deposit taking institutions (**ADI**) required to implement the Banking Executive Accountability Regime (**BEAR**), the legislation on which the FAR is based and we would like to take the opportunity to share some of the key learnings from our implementation of the BEAR, to support Treasury in their implementation of the FAR.

Our submission focuses on three key aspects of the FAR, namely:

- the proposed scope of the FAR, and how flexibility is required to apply the entity based model to corporate group structures with multiple arms (i.e. ADIs, RSEs or insurers) such as Westpac;
- the joint administration of the FAR by the Australian Prudential Regulation Authority (**APRA**) and the Australian Securities and Investments Commission (**ASIC**); and
- the timing and implementation of the FAR,

which are summarised below. Additionally, we have identified some of the practical challenges we foresee in the implementation of the FAR, and areas where we would appreciate some further guidance from Treasury, APRA and ASIC. These matters are set out in more detail in Appendix A.

### Scope of the regime

In Westpac's experience, a positive aspect of the BEAR was that it recognised that each ADI has a unique organisational structure, and therefore the ADI retained a high level of discretion and flexibility in the appointment of accountable persons within their organisation (following consultation with APRA or ASIC, where relevant).

It is unclear from Westpac's reading of the Paper how the entity model is expected to apply to corporate group structures with multiple arms (i.e. ADIs, RSEs or insurers) such as Westpac.

In our view, it is important that organisations can continue to retain the flexibility to appoint accountable persons at both a group level and an entity level, as appropriate. Maintaining flexibility for organisations to apply accountability in a way that reflects both the principles of the FAR and allows existing group structures and governance arrangements to be retained is critical to strengthening the responsibility and accountability framework within APRA regulated entities.

This flexibility around the implementation of the FAR should also apply to an organisation's approach in allocating 'particular responsibilities', as outlined at Attachment B of the Paper.

### **Joint administration by APRA and ASIC**

Westpac supports APRA and ASIC's joint role in overseeing the FAR. However, Westpac would appreciate further guidance on how this will operate in practice. Examples of areas where further guidance would be beneficial include the joint principles between APRA and ASIC which will govern the FAR's administration, and the approach which will be adopted by the regulators for any enforcement proceedings. Coordination between ASIC and APRA will be critical to ensuring the efficient administration of the FAR.

### **Timing and implementation**

While recognising the importance of implementing the FAR in a timely manner, Westpac considers that Treasury, APRA, ASIC and the APRA regulated entities should have appropriate time to develop and consider the new legislation. A considered view of the exposure draft of the legislation and the draft joint regulatory guidance to be released by APRA and ASIC will be important to assess the legislation against the overall system of regulation for APRA regulated entities. This is particularly relevant given the number of consultations currently being coordinated by Treasury and other government agencies which impact the financial services industry, and which may have implications for the FAR<sup>1</sup>. A coordinated approach to legislative and regulatory change is necessary to avoid unintended consequences such as duplication, differing and potentially conflicting standards and resulting lack of clarity for APRA regulated entities, non-executive directors and senior management.

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<sup>1</sup> For example, the APRA consultation relating to the draft Prudential Standard and discussion paper for CPS 511 Remuneration that was released for consultation on 23 July 2019; the Treasury consultation on 'Strengthening breach reporting' that was released for consultation on 31 January 2019 and the Australian Law Reform Commission's discussion paper 87 on corporate criminal responsibility that was released on 15 November 2019.

We appreciate the consultative approach that Treasury has taken to date to work with APRA regulated entities to ensure that the FAR is appropriate, workable and achieves the right outcomes.

We would welcome the opportunity to meet with Treasury to discuss this submission.

Yours sincerely

A handwritten signature in black ink, appearing to read 'M Choueifate', written in a cursive style.

Michael Choueifate  
Group Head of Government & Industry Affairs

## Appendix A – Feedback on specific aspects of the Paper

Key area	Submission
<b>Key submissions</b>	
<b>Scope of the regime - Entity versus group classification</b>	<p>Westpac is supportive of expanding the FAR to include all APRA regulated entities as recommend by the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (<b>Royal Commission</b>). In our view, however, it is unclear how the entity model would apply to corporate group structures such as Westpac, which has APRA regulated entities as subsidiaries of the ADI (Westpac Banking Corporation).</p> <p>For example, if the expectation is that accountable persons be appointed at the APRA regulated subsidiary level (including both the management and directors of those subsidiaries), this may have the unintended effect of duplicating accountabilities at different layers of the organisation, given that management and directors of the ADI already have accountability for those APRA regulated subsidiary under the BEAR. It could also create additional complexity and confusion around accountability and appropriate hand offs at the group level versus the subsidiary level, resulting in ambiguity around decision making (for example where group functions may oversee certain aspects of a subsidiary's activities on a centralised basis such as human resources, information technology or finance). We are also concerned that this could have implications for existing delegation arrangements within a group structure. For example, certain subsidiaries of Westpac have delegated certain remuneration related functions to Westpac Banking Corporation, consistent with relevant prudential standards. If delegations are no longer effective as a result of the implementation of the FAR at an entity level, this could have a significant practical impact on the governance of large organisations.</p> <p>Given the examples outlined above, Westpac's view is that entities should continue to retain a certain level of discretion and flexibility under the FAR to appoint accountable persons as appropriate, having regard to their organisational structure and following consultation with APRA or ASIC, where relevant. This aligns with the approach taken in implementing the BEAR, and Westpac would be supportive of a similar approach being adopted under the FAR.</p>
<b>Joint regulation by APRA and ASIC</b>	<p>Coordination between ASIC and APRA will be critical to ensuring the efficient administration of the FAR, and further clarity on the following points should be set out in legislation:</p> <ul style="list-style-type: none"> <li>the joint principles which will govern the way ASIC and APRA jointly administer the FAR, including any differences in the principles that will govern APRA's approach as a prudential regulator and ASIC's approach as a conduct regulator;</li> <li>how organisations will be expected to engage with both regulators on a day-to-day basis. Westpac would be supportive of a 'single point of contact' model for submissions, registrations and notifications (including reporting a failure to comply with the FAR obligations) under the FAR, similar to the one adopted in the UK under the Senior Managers and Certification Regime; and</li> <li>the approach which will be adopted by the regulators to any enforcement proceedings under the FAR. Westpac submits that it would be appropriate for either ASIC or APRA to pursue any enforcement actions to be brought against an organisation on behalf of both regulators, rather than running two separate proceedings.</li> </ul>
<b>Other matters for Treasury's consideration</b>	
<b>Definition of accountable person</b>	<p><b>New particular responsibilities – application</b></p> <p>Attachment B of the Paper includes a number of new proposed particular responsibilities (<b>New Particular Responsibilities</b>). Under the BEAR, the particular responsibilities relate to centralised functions, such as human resources, finance and risk. Many of the New Particular Responsibilities</p>

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	<p>represent a shift away from centralised functions, to those responsibilities which are more closely related to the front line activities of an organisation and therefore may arise across different divisions of the organisation (e.g. remediation programs and outward facing incentives like loyalty programs).</p> <p>Westpac acknowledges that a key objective of the BEAR, and the FAR, is to establish single point accountability for the activities of APRA-regulated entities. Westpac submits that it would be extremely challenging to appoint a single accountable person for many of the New Particular Responsibilities.</p> <p>More fundamentally, in Westpac's view, the objectives of the FAR of furthering accountability may be best served by accountability for those functions identified under the New Particular Responsibilities sitting with the person who has accountability for the specific business or division in which they arise. For example, the Paper proposes that there is a New Particular Responsibility relating to "senior executive responsibility for the setting of incentives (including incentives for staff and outward facing incentives such as loyalty programs)". In Westpac's view, the responsibility for setting incentives for staff is distinct and separate from the responsibility for setting outward facing incentives. This is on the basis that one relates to internal human resources processes and the other relates to products offered to customers, meaning that these accountabilities should be appointed to different accountable persons.</p> <p>Further, in our view it is not necessary to introduce the New Particular Responsibilities given that there is a "key personnel obligation" imposed on the ADI to ensure that the responsibilities of accountable persons cover all aspects of the operations of the entity and its significant or substantial subsidiaries. In light of this existing obligation under the BEAR, Westpac already assigns accountable persons to cover all aspects of its operations, including in respect of the responsibilities which are included in the proposed New Particular Responsibilities. A key benefit to this approach is that it better aligns the objectives of the FAR with the organisation's broader governance and accountability structure.</p> <p>The Paper indicates that APRA and ASIC would be given power to determine the particular responsibilities for accountable persons under the FAR. For the benefit of certainty and efficiency, Westpac's view is that it would be more appropriate to include the list of particular responsibilities in the FAR legislation, with the ability for modifications to be made through regulation-making powers if necessary. This would be consistent with the Commonwealth Government's guidelines for drafting legislation, and it would be consistent with the approach used for BEAR.</p>
	<p><b>Distinction between accountability and responsibility</b></p> <p>One of Westpac's key learnings arising from the BEAR implementation is the importance of the distinction between "accountability" and "responsibility". We would suggest that Treasury considers reframing the "responsibilities" of accountable persons under the FAR as "<i>accountabilities</i>", to more clearly align with the broader objectives of the FAR. In addition, we think it would be helpful to provide clarity in the legislation around the general principles of "accountability" and "responsibility". We would suggest the following principles:</p> <ul style="list-style-type: none"> <li>• <i>Accountability</i> is the answerability of an individual for behaviour and outcomes within a designated zone of influence (such as a business unit or process); and</li> <li>• <i>Responsibility</i> is the obligation of an individual to perform a designated task with requisite competence and behaviours.</li> </ul>

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	<p><b>New Particular Responsibilities – points of clarification</b></p> <p>Westpac requests clarification on the following:</p> <ul style="list-style-type: none"> <li>• Remediation: This has been included both as a standalone responsibility under Attachment B.1.m, and as an element of the end-to-end product responsibility under Attachment B.1.n. In our view, remediation should not be a standalone responsibility for the reasons we have set out above. Instead, we consider that a product owner should have appropriate oversight of remediation as it relates to their products and therefore, we would propose that remediation remains as an element of end to end product responsibility and be removed as a standalone responsibility.</li> <li>• End-to-end product responsibility (Attachment B.1.n) / service provision and maintenance (Attachment B.1.q): Westpac has made submissions to APRA on the proposed new end-to-end product responsibility, including suggested definitions for key terms, including ‘products’ and ‘services’. These are as follows: <ul style="list-style-type: none"> <li>○ ‘Products’: In Westpac’s view, the scope of the definition of ‘products’ should include all products and services currently offered for sale and all legacy products and services not offered for sale which are manufactured, offered or sold by the organisation and made available to its customers through any type of distribution channel. Products and services should comprise those provided to customers in exchange for a fee. These include, but are not limited to, migrant banking, financial markets products (including foreign currency and exchange), insurance products, interest rate risk management products, investment and superannuation products, packages and bundles, trading services and transactional banking.</li> <li>○ ‘Services’: In Westpac’s view, ‘services that are attached to the provision of a product’ and ‘services for a fee’ should be captured under the definition of ‘services’. Where a service is a product feature or related to a distribution channel strategy, such as internet banking, this would be an appropriate service to be captured for the purpose of end-to-end product accountability. There are also a range of services that may be made available to a customer for a fee (such as data analysis). Westpac would accept that these types of services are appropriate to include in the definition of ‘services’ for the purpose of end-to-end product accountability. In Westpac’s view, ‘internal services’, being services that support products but are not directly attached to the provision of a product or provided for a fee, do not constitute ‘services’ for the purposes of the end-to-end product responsibility.</li> </ul> <p>Consistent with our previous submission, a clear definition of these terms should be set out in the legislation. This will provide organisations with certainty to determine how best to implement end-to-end product responsibility.</p> <li>• Breach reporting (Attachment B.1.q): We assume that Treasury’s intention is that this relates to responsibility for breach reporting to ASIC or APRA rather than breach reporting to other regulators, however we would appreciate confirmation on this point.</li> </li></ul>
<b>Accountability obligations</b>	<p>The Paper proposes the introduction of a new accountability obligation for accountable persons, which requires them to take reasonable steps in conducting their responsibilities to ensure the entity complies with its licensing obligations.</p> <p>In Westpac’s view, the introduction of this new accountability obligation is appropriately covered under the FAR and under other legislation, and is therefore not required. Under the FAR, this obligation appears to be captured under the ‘due skill, care and diligence’ limb, in which it is implied that an accountable person carries out his or her role in a manner which complies with any legal and regulatory requirements (which includes licensing obligations). More broadly, the requirement to comply with licensing obligations exists under other legislation, such as section 912A of the Corporations</p>

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	<p>Act 2001 (Cth) (noting that the obligation is framed slightly differently). Similar obligations under different legislative frameworks could give rise to confusion in their application. Indeed, such an outcome would be at odds with Commissioner Hayne's general recommendation that the law should be simplified so that its intent is met and uncertainty may be reduced.<sup>1</sup></p> <p>We assume that Treasury's intention is that this responsibility only captures APRA and ASIC licensing obligations, however we would appreciate confirmation on this point.</p>
Deferred remuneration obligations	<p>Westpac is generally supportive of the deferred remuneration obligations set out in the Paper, subject to the matters set out below.</p> <p>Westpac notes that it has previously provided a submission in response to the draft Prudential Standard and discussion paper for CPS 511 Remuneration (<b>CPS 511</b>) that was released for consultation on 23 July 2019. To avoid complexity, Westpac proposes that there is alignment under CPS 511 and the FAR between the definition of Variable Remuneration (<b>VR</b>), deferral, and the deferral start date. In addition, given the potential overlap of CPS 511 with the deferred remuneration requirements under the FAR, Westpac may have further submissions in relation to the deferred remuneration requirements once the revised version of CPS 511 has been released for consultation.</p> <p>Westpac suggests that the legislation for FAR should provide clarity on the following key areas:</p> <ul style="list-style-type: none"> <li>• Definition of variable remuneration: The Paper states that the definition of VR is "so much of an accountable person's total remuneration that is not guaranteed because it is conditional on the achievement of pre-determined objectives and can be forfeited if these objectives are not met". Westpac submits that the definition of VR should be expanded to also include any part of an accountable person's total remuneration which is not guaranteed because it remains "at risk and subject to forfeiture". Expanding the definition in this way would allow organisations to retain flexibility as to how they structure their VR, and it would mean that VR which does not have performance hurdles but remains 'at risk' due to malus provisions and continued service requirements could be captured under the definition. Off-cycle awards (excluding buyouts) could also be captured under the definition of VR depending on the conditions of the award.</li> <li>• Buyouts: When an executive ceases their existing employment to take a role with Westpac, the executive will typically forfeit any deferred remuneration on foot with that employer. In certain circumstances Westpac will provide a 'buyout' award to the executive. The buyout award is structured to be on a like-for-like basis (to the extent practical) as the award that was forfeited. Westpac proposes that the FAR legislation clarify that a 'buyout' award is not subject to the requirement to defer 40% of VR for four years, providing it vests no earlier than the original vesting date. Without making this amendment executives that change employment may be disadvantaged, as changing employment could be interpreted to re-start the deferral timeframe.</li> <li>• Calculation date for the purposes of variable remuneration: Westpac seeks confirmation that the decision to grant VR is made at the time the Board approves the award. For Westpac, the Board approves short term VR (<b>STVR</b>) outcomes (relating to performance in the previous year) and the grant of long term VR (<b>LTVR</b>) (on a prospective basis) shortly after the start of each financial year. As such, STVR awards attributable</li> </ul>

<sup>1</sup> At page 44 in volume 1 of the Final Report of the Royal Commission, Commissioner Hayne commented that "the more complicated the law, the harder it is to see unifying and informing principles and purposes. ... Boundary-marking and categorisation may promote uncertainty. Removing [complexity] encourages understanding and application of the law in accordance with its purposes. That is, 'its intent is met, rather than merely its terms complied with'. Like cases are more evidently treated alike. Uncertainty may be reduced."

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	<p>to the previous performance year and LTVR awards granted prospectively are subject to the deferred remuneration obligations for a relevant financial year.</p> <ul style="list-style-type: none"> <li>• Apportionment, including for part-year and/or temporary accountable persons: Westpac seeks confirmation that the deferred remuneration obligations only apply to the remuneration of an individual to the extent the remuneration is attributable to (or relates to) a period where the individual is an accountable person. This is a key determinant for our proposed approach to apportionment where, for example, an individual is appointed to an accountable person role for part of a year, noting our approach seeks to ensure consistent outcomes for individuals moving into and out of accountable person roles, whether internally or externally.</li> </ul>
<b>Accountability maps and statements</b>	<p>The Paper states that enhanced compliance entities must submit accountability maps and statements to APRA and ASIC, and Westpac is supportive of Treasury's proposal that updated accountability maps and statements only need to be provided in the event of 'material changes'.</p> <p>In order to minimise the administrative burden imposed on each enhanced compliance entity in meeting this requirement, Westpac proposes the following:</p> <ul style="list-style-type: none"> <li>• That there is a certain degree of flexibility in the form of an organisation's accountability map. For example, rather than an organisation having to submit an accountability map for each enhanced compliance entity, an organisation could present this information on a group level, rather than an entity level basis, if this achieves the overall objective of showing details of the reporting lines and lines of responsibility of each accountable person.</li> <li>• When considering the definition of the term 'material change', Westpac notes that in its experience implementing the notification requirements under the BEAR, examples of minor changes which have imposed an administrative burden on Westpac have included changes to committee names, minor updates to titles, and updates to cross references in statements. Capturing changes such as these resulted in Westpac making over 200 submissions in a 12-month period relating to changes in accountability maps and statements.</li> </ul>
<b>General feedback</b>	<p><b>Temporary Vacancy</b></p> <p>The Paper proposes an increase in the temporary vacancy period from 28 days to 90 days, and Westpac is supportive of this extended timeframe. However, we consider that the requirements under the FAR during a temporary vacancy period should be clarified, including:</p> <ul style="list-style-type: none"> <li>• deferred remuneration requirements;</li> <li>• application of the APRA non-objections power; and</li> <li>• application of accountability statements (noting that these would not be registered with APRA during the vacancy period).</li> </ul> <p><b>Indemnification and insurance</b></p> <p>Westpac understands that under the FAR, FAR entities will be prohibited from indemnifying or paying the cost of insuring accountable persons against the consequences of breaching the FAR. Westpac acknowledges that restrictions on indemnification and paying the costs of insurance for Directors and Officers currently exist under other legislation and recommends that, to the extent similar restrictions will apply in connection with the FAR, they closely track sections 199A and 199B of the Corporations Act 2001 (Cth). These sections set considered limits on what a person can be indemnified for, and what insurance policies a company can pay for, in a civil penalty context.</p>



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	<p><b>Review of the BEAR</b></p> <p>Section 37KC of the Banking Act 1957 (Cth) contains a mechanism that requires a review of the BEAR three years after commencement, and for this review to be provided to each House of Parliament. Westpac considers this review under the BEAR as crucial to ensuring that the FAR is effective, and that it addresses any limitations relating to the BEAR. We suggest that APRA carry out the review of BEAR prior to commencement of the FAR and that a similar mechanism of review is maintained under any new legislation.</p>