

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates

2017 - 2018

Division/Agency: Australian Prudential Regulation Authority

Question No: 68

Topic: Bank executive remuneration questions

Reference: Written

Senator: Ketter, Chris

Question:

What assessment does APRA do of the remuneration disclosures for superannuation fund executives and directors?

1. Could APRA provide the number of reviews they have done by number of executives and type of super fund? What was the outcome of these reviews – were any concerning practices identified?
2. Is it the case that the executives that do the work for the super funds within the large banking groups are employed and remunerated by the parent bank rather than the super fund, and that these executives generally only do a portion of their work for the super fund, with the rest of their work being performed elsewhere in the banking group? What is APRA's view of this arrangement and whether it may lead to conflicts of interest?
3. Is it correct that the remuneration for the work executives do for the parent bank outside the super fund entities is unknown or not reported? What is APRA's view of this?
4. Where the banks have multiple superannuation entities running different groups of funds (this is the case for CBA, Westpac and ANZ), these various entities usually have the same directors and are often run by the same executives, in this case are there multiple remuneration disclosures each with the portions of director and executive remuneration attributable to that superannuation entity?
5. Is it the case that the executives working for the bank super funds receive performance bonuses? What are the hurdles for these bonuses?
6. Is APRA concerned that super fund executives being paid bonuses based on the group achieving certain ROE, TSR, growth in cash earnings and so on may lead to conflicts between the interests of the banking group and the interests of shareholders?
7. How does APRA satisfy itself that these remuneration practices don't breach the sole purpose test and other trust obligations?
8. Has APRA looked at the possible related party conflicts that arise from the roles performed by these executives inside and outside the super fund?
9. The executives on this disclosure do their "outside super" work for the bank group in areas like investment and insurance. Can ARPA see serious conflicts arising if these functions are insourced to other parts of the group where these executives work?

Answer:

Prudential Standard SPS 510 Governance (SPS 510) requires a registrable superannuation entity (RSE) licensee to establish and maintain a remuneration policy that outlines remuneration objectives and the structure of remuneration arrangements. Similar to *Prudential Standard CPS 510 Governance* that applies to other APRA-regulated industries, SPS 510 requires any performance-based remuneration to be designed so that it encourages

behaviour that supports protecting the interests of beneficiaries and the long term financial soundness of the RSE licensee and its RSEs. In addition, RSE licensees are expected to act in a manner consistent with APRA's expectations detailed in *Prudential Practice Guide SPG 511 Remuneration* (SPG 511); these documents both explicitly mention the setting of performance-based remuneration.

Reporting Standard SRS 600.0 Profile and Structure (RSE licensee) (SRS 600.0) collects data relating to director remuneration. *Prudential Standard SPS 521 Conflicts of Interest* (SPS 521) requires an RSE licensee develop, implement and review a conflicts management policy that is approved by the Board, identifies all relevant duties and interests and develops a register of relevant duties and interests.

Through the course of APRA's normal supervisory practices, APRA has regular discussions with RSE licensees on their approach to meeting the requirements in SPS 510 and other prudential standards. Remuneration practices of superannuation entities were also considered as part of APRA's 2014 thematic review relating to conflicts of interest. APRA's primary focus is on being satisfied that:

- the remuneration policy covers all the relevant persons and has been effectively implemented; and
- conflicts are effectively managed, in part by ensuring remuneration arrangements are transparent, disclosed and appropriately managed.

APRA reviews RSE licensee practices using a risk-based approach and, where specific concerns with practices are identified, these will be communicated to the RSE licensee for remediation.

Executives that are employed within banking groups may have a portion of their time and subsequent remuneration dedicated to their role as a superannuation director. The trustee covenants of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) require all RSE licensees to perform their duties in the best interests of beneficiaries and, where there is a conflict of interest, to give priority to the interest of beneficiaries.

APRA's experience is that the registers of duties and interests record relevant remuneration payments. In a letter to RSE licensees ('Managing conflicts of interest in superannuation', dated 19 March 2015), APRA noted that there was room for improvement in conflicts management practices with regards to remuneration disclosure and the on-going management of registers of duties and interests. APRA continues to monitor progress in this regard.

The work that executives perform outside their capacity as director of an RSE licensee is not required to be reported to APRA. *Prudential Standard APS 330 Public Disclosure* (APS 330) requires the public disclosure of certain information, including the remuneration of 'senior managers' and 'material risk-takers' in accordance with an authorised deposit-taking institution's remuneration policy. Further, the *Corporations Act 2001* includes comprehensive disclosure requirements for the remuneration of 'key management personnel' in the Annual Director's report. APRA's experience is that directors serving on multiple boards disclose the portion of remuneration attributable to their role as director of each particular RSE licensee.

Director remuneration may comprise fixed and variable components, and variable components may comprise short-term and longer-term incentives. APRA expects that an RSE licensee will consider how the balance between these components and any hurdles set will

encourage behaviour that supports protecting the interests, and meeting the reasonable expectations of beneficiaries, and the long term financial soundness of the RSE licensee, any of its RSEs or connected entities. Hurdles may include, but not be limited to, measures relating to financial performance, member satisfaction, compliance with the risk management framework and satisfaction of corporate values.

Where a director is employed by another entity in a group and their remuneration and performance is tied to the performance of this entity, the RSE licensee is required to manage these potential and actual conflicts in line with their conflicts management framework (as required under SPS 521).

APRA seeks remuneration information from RSE licensees through the normal course of supervision, including the regular reporting under SRS 600.0, for the purposes of:

- ensuring that the RSE licensee's remuneration policy complies with the requirements of SPS 510;
- ensuring that the RSE licensee manages any conflicts in accordance with SPS 521;
- understanding how the remuneration policy supports the risk culture of the RSE licensee; and
- ensuring that the RSE licensee has formal and transparent remuneration policies and procedures.

APRA is currently undertaking a further conflicts management thematic review focusing specifically on, for a sample of superannuation entities across all industry segments, practices in relation to the management and oversight of different types of related party arrangements. APRA expects to report on the findings from this review later in 2017.

APRA's view is that there is the potential for conflicts of interest in all business models where there are relationships with third parties, related or otherwise. APRA expects an RSE licensee to ensure that decisions about insourcing are made in accordance with the strategic direction and business plan of the RSE licensee's business operations. RSE licensees must be able to demonstrate that such decisions are made on an arms-length basis and based on appropriate benchmarking, such that priority is given to the best interests of beneficiaries. APRA also expects RSE licensees to review such arrangements on an on-going basis to ensure they continue to operate in the best interests of beneficiaries.