

30 August 2019

Ms Heidi Richards
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Australian Prudential Regulation Authority
By email ADIpolicy@apra.gov.au

Dear Ms Richards

The Banking Executive Accountability Regime – Consultation on Product Responsibility

Thank you for the opportunity to provide feedback on this measure.

We note that this consultation is centred on APRA's proposal, in implementing recommendation 1.17 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, to make a determination under section 37BA(4) of the Banking Act 1959, as follows:

“For the purposes of paragraph 37BA(2)(b)(ii) of the Banking Act 1959, a particular responsibility includes senior executive responsibility for end-to-end product management of a product or product group offered by the ADI or the relevant group of bodies corporate that is constituted by the ADI and its subsidiaries, including but not limiting to all steps in the design, delivery, maintenance and any necessary remediation of customers in respect of any such product or product group.”

In this submission we will refer to this as “the new responsibility”.

Key points

- The ABA endorses recommendation 1.17 of the Financial Services Royal Commission and APRA's core objective of heightened and clarified end to end accountability among senior executives for an ADI's products.
- Designing the new responsibility in a way that accords with the existing BEAR and does not disrupt existing business models will be difficult and involve complex considerations.
- In particular, it will be challenging to determine the scope of the new responsibility so that it substantially adds to the existing responsibilities under the BEAR but is also distinct from them.
- APRA should include in its guidance that the expectations under the new responsibility relate essentially to governance considerations.
- In designing the scope of the new responsibility, APRA should also have regard to how the joint accountability provisions in the Banking Act will apply so that unfair outcomes will not occur as a result.
- We note with approval that APRA has, informally, confirmed that it is not seeking that ADIs capture all products in a 'catalogue' for the purposes of the new responsibility, but that it is intended to leave to ADIs the task of assigning responsibility for products or groups of products.
- While understanding APRA's desire for the new responsibility to have broad application in terms of products, we ask APRA to consider whether there are some products which need not be brought within the regime, either because they are amply regulated elsewhere, or they are not products or services that have a bearing on prudential considerations – the core of the BEAR.

Heightened and clarified end-to-end accountability among senior executives for their products offered

We note that the core objective of APRA's proposal is expressed to be "Heightened and clarified end to end accountability for each product offered by the ADI or ADI group", and that APRA seeks feedback on any area that may impact this objective.

We believe this to be a worthy goal but in our view care needs to be taken to achieve it in an effective manner. A regime under which the limits of the new responsibility were unclear in terms of their relationship to the existing responsibilities under the BEAR would do little towards achieving heightened and clarified end to end accountability and may well be counterproductive in terms of that goal.

We note further that APRA has clarified that it does not, by implementing the Royal Commission's recommendation and introducing this new responsibility, intend to bring about changes to existing business models or prescribe particular business models.

Again, in our view, care is needed to ensure that the effect of the measure is consistent with APRA's intent in this regard. If uncertainties in the application of the new responsibility cannot be resolved, ADIs may well consider that they require internal restructures to comply with the new responsibility.

We expand on these issues below under the same headings that APRA adopted in its consultation document.

Scope of accountability

The concept of end-to-end accountability is inherently broad. While we note that APRA is comfortable with a broad interpretation of the term, in our view it is necessarily limited by reference to the enabling legislation. Under that legislation, APRA's ability to prescribe new responsibilities is not unfettered. It cannot, for example, prescribe responsibilities that, in effect, replicate the other responsibilities listed expressly in the Banking Act.¹

The new responsibility cannot, therefore, be taken to replicate the role of the senior executive responsibility for information management or information technology systems, or that of the senior executive responsible for carrying out the business activities of the ADI.

Rather, the new responsibility must be carefully delineated, and relate to responsibilities of a distinct kind. In this regard we note that APRA seeks to distinguish the new responsibility by proposing that it attach specifically to products, as opposed to the broader responsibilities that relate to the ADI's operations more broadly e.g. IT systems that support relevant products, not IT systems across the ADI.²

However, uncertainties remain about the scope of the new responsibility. Determining whether a problem with an IT system that resulted in a negative outcome for a product or product group was a systemic problem with the ADI's IT system as a whole, or a problem specifically related to a product, and so within the remit of the end to end accountable person, would not necessarily be straightforward. This is the kind of issue which, in our view, APRA needs to give careful consideration, and potentially further guidance, in its roll out of the new responsibility. We will return to this issue under the discussion on joint accountability below.

The new responsibility should, in essence, relate to governance

Although the responsibility will have a product-specific perspective, in our view it should be made clear that the new responsibility is, consistent with the rest of the BEAR framework, directed at governance responsibility rather than, for example, attempting to attribute to an accountable person responsibility for actually controlling every stage of the product cycle. The latter would be impractical and inconsistent with the overarching principles behind the BEAR.

¹ Section 37BA(4) expressly excludes other responsibilities set out in 37BA(3) from the scope of APRA's power to determine a new responsibility.

² APRA information slides page 7.

This is because the BEAR provides that an accountable person is one who, among other things, 'has actual or effective control of... a significant or substantial part or aspect of the operations of the ADI'.³ In order to maintain consistency with that broad principle, any prescription of a responsibility for end to end accountability would, in our submission, need to be cast in such a way as to avoid artificial or impractical attributions of responsibility to particular individuals. This would be avoided if it is accepted that the new responsibility is aimed essentially at governance. This approach would also be consistent with the nature of the accountability obligations of an accountable person as set out in section 37CA of the Banking Act, and the 'reasonable steps' to achieve those as set out in section 37CB.

We acknowledge that APRA has confirmed, informally, that it is not the intent that the accountable person have direct and total control over every aspect of the product cycle to be in a position to hold end-to-end product accountability, and that 'An individual with suitable seniority supported by robust governance arrangements remains the key',⁴ but further clarity around this would be welcome, potentially in the form of guidance issued by APRA.

APRA should include in its guidance that the expectations under the new responsibility relate to governance and do not overlap with existing accountabilities.

Assigning responsibility: Products or product groups

We note that APRA has, informally, confirmed that it is not seeking that ADIs capture all products in a 'catalogue' for the purposes of the new responsibility, but that it is intended to leave to ADIs the task of assigning responsibility for products or groups of products.

In our submission, it is important that this flexibility be made clear. This is important both for practical purposes, and to accommodate different business models across the industry.

The limits of 'end to end' accountability

We note that it is not always the case that the entire value chain for a given product occurs within one ADI, or, for group operations, within one country. For example, a product might be designed in a foreign headquarters of an international banking group, and then distributed by the group's Australian entities. In that circumstance, in our view, the regime ought to take account of the exclusion of foreign ADIs from the BEAR and the practical implications of seeking to extend end to end accountability to operations carried by entities not caught by the regime.

Similarly, where one step in the value chain is completed outside the ADI – by a separate business – end to end accountability should be confined, for the purposes of this regime, to the stages that are completed within the ADI.

For example, consider the case with home loans that are originated in an ADI but distributed by independent brokers. Banks' control over external entities such as brokers is limited, and this should be recognised when setting the boundaries of end to end accountability.

In this regard we note also that APRA should consider the potential overlap with other regimes, such as the Design and Distributions Obligations (DDO) regime under which banks will be required to take reasonable steps to ensure distribution is in accordance with target market determinations. Accountabilities under the BEAR need not seek to replicate obligations under the DDOs.

Overall, the appropriate way to deal with the above examples is, in our submission, to recognise that the concept of end to end accountability requires some flexibility in its application.

Coverage of products

We note that APRA's starting point is that all products of an ADI ought to be covered by this new responsibility. While we note APRA's view that the BEAR is a prudential regime and for that reason, the responsibility need not be confined to retail products albeit that that was the focus of the Hayne recommendation that motivated this measure. We do not disagree with the broad principle expressed

³ Banking Act 1959, section 37BA(1)(b)(ii)

⁴ APRA information slides, page 8.

by APRA, however, we question whether there is any real benefit in applying the responsibility indiscriminately to every product of an ADI.

In particular, products such as equities and securities, comprehensively governed by parallel regimes, in our view need not be subject to this new responsibility. Similarly, products that fall within a category that are neither banking products that have prudential implications, nor retail financial products within that definition under the Corporations Act or ASIC Act, should not, in our view, be captured by this new responsibility. Phone and internet banking applications are examples. It is unclear that extending the accountability obligations of an accountable person – which are ultimately directed at preserving the prudential standing or prudential reputation of the ADI – has a tangible purpose in respect of such products. We question whether there is a good reason to depart so substantially from the scope (i.e. retail products) that motivated the Commissioner’s recommendation in this respect.

Mechanism

Other than the comments made above under Scope of accountability, we do not have comments on the mechanism proposed by APRA at this stage.

Joint accountability

We note APRA’s proposal, in the consultation letter of 28 June, that “where more than one accountable person is identified as accountable for a given product or product group, joint accountability is applied to the accountable persons involved to ensure no gaps or dilution in the end-to-end accountability.” This is further qualified by the statement that “This joint accountability should not be taken to apply automatically across different identified products or product groups.”

In our view, to be consistent with the Banking Act, as well as APRA’s intentions as outlined above, joint accountability should:

- apply so that individuals are held to account for their governance of the product (or product group) cycle within their purview;
- not artificially attribute responsibility to individuals where they do not have control over a stage in the product cycle;
- not effectively duplicate responsibility so that holders of the new responsibility would share accountability with holders of existing responsibilities under BEAR; and
- not result in one accountable person, who had taken reasonable steps to discharge their duties under the Banking Act, being held responsible for the failures of another accountable person who had primary responsibility for the relevant stage in the product cycle.

We note that a strict application of joint accountability that does not take these factors into account may have unintended negative impacts on the ability of ADIs to attract and retain executive talent.

If you have any questions regarding the above, please do not hesitate to contact us. Thank you again for the opportunity to comment on this proposal, and for APRA’s willingness to engage with interested parties during the process.

Yours faithfully



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