Westpac GROUP

EST. 1817

Colby Hannan
Senior Researcher
Senate Economics References Committee

Richard Gray
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Level 20, 275 Kent Street
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Dear Mr Hannan

I refer to your email correspondence to Mr Jim Tate in regard to questions taken on notice at the recent hearing of the Senate Economics References Inquiry into the post-GFC banking sector.

Senator Cameron asked for further information in relation to Westpac's introduction of risk-based and risk-related remuneration policies. The following is Westpac's response:

> The Westpac Group's remuneration strategy, executive remuneration framework, policies and practices all reflect the sound risk management that is fundamental to the way we operate. The performance of each division within the Group is reviewed and measured with reference to how risk is managed and the results influence remuneration outcomes.
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> We aim to integrate effective risk management into the remuneration framework throughout the organisation. The Chairman of the Board Risk Management Committee is a member of the Remuneration Committee and members of the Remuneration Committee are also members of the Board Risk Management Committee. In carrying out its duties, the Remuneration Committee can access personnel from risk and financial control and engages external remuneration advisors who are independent of management.
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> In addition to the overall risk-based approach to remuneration, Westpac is required to comply with the remuneration provisions of the APRA prudential standard CPS 510. This standard requires Westpac to maintain a formal Remuneration Policy which encapsulates the prudential requirements for remuneration. Particular clauses of this prudential standard which are relevant to the risk based requirement include:
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> Cl. 45: In addition to any other objectives, the Remuneration Policy's performance based components of remuneration must be designed to encourage behavior that supports:
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> - the regulated institution's long-term financial soundness; and
> - the risk management framework of the regulated institution.
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> Cl. 46: The performance-based components of remuneration must be designed to align remuneration with prudent risk-taking and must incorporate adjustments to reflect:
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> - the outcomes of business activities;
> - the risks related to the business activities taking account, where relevant, of the cost of the associated capital; and
> - the time necessary for the outcomes of those business activities to be reliably measured.
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> Cl. 47: The Remuneration Policy must provide for the Board, the senior officer outside Australia or the Compliance Committee, as relevant, to adjust performance based components of remuneration downwards, to zero if appropriate, in relation to persons or classes of persons, if such adjustments are necessary to:

- protect the financial soundness of the regulated institution; or
- respond to significant unexpected or unintended consequences that were not foreseen by the Board Remuneration Committee, the senior officer outside Australia or the Compliance Committee, as relevant.

Cl. 54: The Remuneration Policy must form part of a regulated institution's risk management framework.

In keeping with the requirements of the regulatory standard, and consistent with the Group philosophy, the executive remuneration framework also specifically includes features to take account of risk. The framework is composed of a mix of fixed pay and variable reward, a portion of which is deferred. Each year the Board determines the size of the variable reward pool. The primary financial indicator used is economic profit, which measures profitability adjusted for risk in the business.

Therefore, in summary, Westpac's remuneration policy is compliant with prudential standards, it is risk-based and risk-sensitive and the variable reward pool is primarily driven by a risk-adjusted profitability measure.

Yours sincerely

Richard Gray

Executive Director of Regulatory Reform

Westpac Banking Group