Chapter 1

Introduction and overview of the bill

1.1 On 19 October 2017, the Senate referred the provisions of the Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017 (the bill) to the Senate Economics Legislation Committee (the committee) for inquiry and report by 24 November 2017.[1]

1.2 The purpose of the bill is to amend the *Banking Act 1959* (Banking Act) to establish the Banking Executive Accountability Regime (BEAR). The BEAR is a strengthened responsibility and accountability framework for the most senior and influential directors and executives in authorised deposit-taking institution (ADI) groups. It requires them to conduct themselves with honesty and integrity and to carry out the business activities for which they are responsible effectively.[2]

1.3 The BEAR does this by creating a new definition of 'accountable person'. An accountable person is a board member with oversight over the ADI or a senior executive with responsibility for management or control of significant or substantial parts or aspects of the ADI group.

1.4 The Treasurer explained why this reform was necessary in his second reading speech:

> Banking executives share responsibility for the stewardship of the Australian economy and they make decisions that impact upon the lives of ordinary Australians who have no choice other than to engage with the system they help run. As a consequence, the community reasonably expects higher standards of accountability and integrity of banking directors and executives.
>
> The BEAR ensures that where these community expectations are not met, appropriate consequences will follow. It makes clear individual accountabilities so that it is clear where the buck stops in decision making and responsibility.[3]

1.5 This bill implements the accountability measures of the banking and financial services reforms announced in the 2017–18 Budget.[4] The measures in the bill will enhance the integrity, stability, resilience and competitiveness of the financial system.[5]

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1 *Journals of the Senate*, No. 67, 19 October 2017, p. 2138.

2 Explanatory Memorandum, p. 9.

3 The Hon. Scott Morrison MP, Second Reading Speech, *House of Representatives Hansard,* 19 October 2017, p. 1.

4 *Factsheet: Banking and Financial Services*, Budget 2017–18, http://budget.gov.au/2017-18/content/glossies/factsheets/html/FS_Banking.htm (accessed 6 November 2017).

5 The Hon. Scott Morrison MP, Second Reading Speech, *House of Representatives Hansard,* 19 October 2017, p. 2.

Conduct of the inquiry

1.6 The committee advertised the inquiry on its website and wrote to relevant stakeholders and interested parties inviting submissions by 1 November 2017. The committee received 20 submissions, which are listed at Appendix 1.

1.7 The committee held two public hearings for this inquiry:

- 14 November 2017 in Canberra; and
- 17 November 2017 in Canberra.

1.8 The committee thanks all groups and individuals who took the time to make written submissions and attend public hearings.

Overview of the bill

1.9 The Australian financial system is the backbone of the economy and plays an essential role in promoting economic growth. For it to operate in an efficient, stable and fair way, all participants must have trust in the system.[6]

1.10 Banks have a special role within our society:

- First, it is virtually impossible for an Australian to go about their daily lives without a bank account.
- Second, banks benefit from an extraordinarily privileged regulatory environment. Virtually all depositors in Australian banks are protected by a government guarantee, the Financial Claims Scheme.
- Third, banks are fundamentally important to financial stability, and financial stability is fundamentally important to Australia's economic wellbeing. Crises that begin in the banking sector generally spread throughout the entire economy.[7]

1.11 Consequently, ADIs must operate at the highest standards and meet the needs and expectations of Australian consumers and businesses. Participants need to be confident that financial firms will balance risk and reward appropriately and serve their interests.[8]

1.12 A key objective of the BEAR is to improve the operating culture of ADIs and increase transparency and accountability across the banking sector. By setting out accountability obligations in the Banking Act and providing guidance about them, the bill makes clear and enhances the obligations of ADIs and reinforces the standards of conduct expected of them by the community.[9]

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6 Explanatory Memorandum, p. 9.

7 The Hon. Scott Morrison MP, Second Reading Speech, *House of Representatives Hansard,* 19 October 2017, p. 3.

8 Explanatory Memorandum, p. 9.

9 Explanatory Memorandum, p. 9.

1.13 The BEAR:

- imposes a set of obligations to be met by ADIs and 'accountable persons';
- introduces a definition of 'accountable person' and requires their registration with the Australian Prudential Regulatory Authority (APRA) prior to the commencement in an accountable person role;
- requires that ADIs give APRA accountability statements detailing the roles and responsibilities of each accountable person;
- requires that ADIs give APRA accountability maps allocating the roles and responsibilities of each accountable person across the ADI and its subsidiaries; and
- gives APRA new and stronger enforcement powers.[10]

1.14 A comparison of key features between the new law and current law are listed in Table 1 below.

An ADI's obligations under the BEAR

1.15 The BEAR imposes strengthened obligations on both ADIs and their accountable persons. The obligations cover conduct that is systemic and prudential in nature. Where an ADI or an accountable person breaches its BEAR obligations, penalties will be imposed (see below).[11]

1.16 The BEAR obliges an ADI to:

- comply with its accountability obligations, which cover the way an ADI should conduct itself and how it should engage with APRA;
- meet its key personnel obligations, by ensuring all areas of an ADI's operations and those of its group are attributable to accountable persons;
- give APRA accountability maps and statements, which explain who is responsible for all parts and aspects of the ADI; and
- defer the remuneration of accountable persons for a period of up to four years, have remuneration policies that allow for a reduction in remuneration in proportion to any failure to meet the BEAR obligations, and continue the deferral where there is a likely failure by an accountable person to meet the BEAR obligations.[12]

1.17 ADIs are responsible for their subsidiaries and are obliged to take reasonable steps to ensure that the subsidiaries within the ADI group meet the obligations under the BEAR.[13]

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10 Explanatory Memorandum, p. 9.

11 Explanatory Memorandum, p. 14.

12 Explanatory Memorandum, p. 14.

13 Explanatory Memorandum, pp. 15, 17.

Table 1: Comparison of key features of new law and current law

New law	***Current law***
Establishes the BEAR which places new obligations on an ADI, including for the conduct and operation of its subsidiaries.	No equivalent.
Accountable persons	
The Banking Act defines an 'accountable person' with respect to the responsibilities undertaken in the ADI and, where relevant, the ADI group. A list of prescribed responsibilities in ADIs is also included.	No equivalent.
Accountable person roles must be filled at all times and registered with APRA.	No equivalent.
Obligations under BEAR	
Obligations with regards to the prudential conduct of an ADI group and 'accountable persons' under BEAR are prescribed in legislation.	No equivalent.
ADIs must give APRA statements which detail the roles and responsibilities of each accountable person.	No equivalent.
ADIs must give APRA accountability maps which identify the lines of responsibility through the ADI group.	No equivalent.
Penalties under BEAR	
APRA may seek civil penalties of up to 1 million penalty units where an ADI breaches the obligations under BEAR.	APRA may seek civil penalties in specified circumstances.
APRA may disqualify an 'accountable person' for breaching the obligations of BEAR.	APRA may apply to the Federal Court to have a director, senior manager or auditor disqualified from being or acting in that position.
Deferral of remuneration	
An ADI must defer a proportion of the remuneration of an accountable person for a period of four years. The proportion to be deferred depends on the size of the ADI. There are circumstances where APRA may allow an ADI to defer a person's remuneration for a shorter period. An ADI must have a remuneration policy which is consistent with the requirements under the BEAR.	No equivalent.
Insurance	
An ADI must not take out insurance against the consequences of breaching the BEAR for itself or an accountable person.	No equivalent.
Examination powers	
Examination powers allow an APRA investigator to require a person to give information relevant to an investigation, set out how the person's lawyer may participate during the examination and how examination records must be kept and shared.	Section 61 allows APRA to conduct an investigation and require an ADI to give certain information.
Statements and evidence are admissible during a proceeding unless the evidence would self-incriminate an individual or the other party to the proceedings has not had sufficient time to examine the material. Section 52F is also expanded to apply to production of a book, account or document or signing of a record.	Section 52F sets out self-incrimination provisions in relation to information given by a person

Source: Explanatory Memorandum, pp. 11–13.

1.18 A foreign ADI is not subject to the BEAR for its offshore operations or for any locally incorporated non-ADI subsidiaries. However, its Australian branch operations are obliged to comply with BEAR to the extent required by their operations and presence in Australia.[14] The BEAR imposes a statutory obligation on an ADI (including its subsidiaries) to defer a percentage of an accountable person's variable remuneration. It ensures that accountable persons have clear incentives to make decisions which account for longer term effects. It also ensures that accountable persons are properly held to account for those decisions that have negative future consequences.[15]

1.19 If an accountable person engages in behaviour in breach of their BEAR obligations then the ADI is obliged to withhold all or part of the accountable person's variable remuneration that is deferred under the BEAR. The amount withheld is to be proportionate to the severity and consequences of the breach.[16]

1.20 An ADI must implement a remuneration policy that is consistent with an ADI's BEAR obligations. This updated remuneration policy will be required to be in effect by 1 July 2018. The ADI should defer the variable remuneration of accountable persons for all accountable persons for the minimum period (four years or a shorter period approved by APRA).[17]

1.21 The amount of an accountable person's remuneration to be deferred by an ADI will depend on the size of the ADI (see Table 2). ADI size is defined as:

- a large ADI would have greater than or equal to $100 billion of a three year average of total resident assets;
- a medium ADI would have between $10 billion and $100 billion of a three year average of total resident assets; and
- a small ADI would have less than $10 billion on a three year average of total resident assets.

All amounts, once finalised, will be indexed.[18]

14 Explanatory Memorandum, p. 15.

15 Explanatory Memorandum, p. 20.

16 Explanatory Memorandum, pp. 20–21.

17 Explanatory Memorandum, p. 21.

18 Explanatory Memorandum, pp. 22–23.

Table 2: Minimum amounts of remuneration to be deferred

If the accountable person is …	**the amount is …**
The CEO of a large ADI.	The lesser of 60 per cent of the CEO’s variable remuneration for the financial year or 40 per cent of the CEO’s total remuneration for the financial year.
An accountable person (other than the CEO) of a large ADI, or of a subsidiary of a large ADI.	The lesser of 40 per cent of the person’s variable remuneration for the financial year or 20 per cent of the person’s total remuneration for the financial year.
An accountable person of a medium ADI, or of a subsidiary of a medium ADI.	The lesser of 40 per cent of the person’s variable remuneration for the financial year or 20 per cent of the person’s total remuneration for the financial year.
An accountable person of a small ADI, or of a subsidiary of an ADI.	The lesser of 40 per cent of the person’s variable remuneration for the financial year or 10 per cent of the person’s total remuneration for the financial year

Source: Explanatory Memorandum, pp. 21–22.

Who is an accountable person?

1.22 A key objective of the BEAR is to ensure that an ADI allocates responsibilities to accountable persons across the ADI group. The bill inserts the term 'accountable person' into the Banking Act. 'Accountable person' is defined by reference to a general principle and by reference to listed functions or responsibilities. A person in an ADI will be an accountable person where the person is in a position that undertakes a particular responsibility as listed in the Banking Act. An ADI, particularly small and medium ADIs, may not necessarily have a separate person corresponding to each of the listed functions.[19] A table of listed functions and typical roles that may correspond to those functions is presented below (Table 3).

1.23 Unless exempt, an accountable person must meet their accountability obligations under the BEAR. The accountability obligations make clear the behaviour and conduct expected of an accountable person—they relate to conduct or behaviour that is systemic and prudential in nature both because of the seniority of accountable persons and because the content of the obligations relates to prudential matters, such as integrity, professional conduct and governance arrangements. While the obligation to have integrity and honesty, and be open with APRA is absolute, an accountable person has met their accountability obligations if they can show APRA they have taken reasonable steps to prevent other matters that could affect the prudential reputation or standing on an ADI.[20]

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19 Explanatory Memorandum, pp. 24–25.

20 Explanatory Memorandum, pp. 28–29.

Table 3: Particular responsibilities covered by the BEAR

Particular responsibility	Typical role(s)
Responsibility for oversight of the ADI as a member of the Board of the ADI.	Chairman/Non-executive board member
Senior executive responsibility for management or control of the business activities of the ADI, including allocating to accountable persons responsibility for all parts or aspects of the ADI group and reporting directly to the Board of the ADI.	Chief Executive officer
Senior executive responsibility for the management of the ADI's financial resources.	Chief Financial Officer
Senior executive responsibility for the overall management of the risk controls and/or risk management arrangements of the ADI.	Chief Risk Officer
Senior executive responsibility for the management of the operations of the ADI.	Chief Operation Officer
Senior executive responsibility for the information management, including information technology systems in the ADI.	Chief Information/Technology Officer
Senior executive responsibility for the management of the internal audit function of the ADI.	Head of Internal Audit
Senior executive responsibility for the management of the compliance function of the ADI.	Head of Compliance/Chief Compliance Officer
Senior executive responsibility for the management of the human resources function of the ADI.	Chief Of People Officer/Head of Human Resources
Senior executive responsibility for the management of the anti-money laundering function of the ADI.	Anti-Money Laundering Officer

Source: Explanatory Memorandum, pp. 25–27.

Notification obligations

1.24 The BEAR obliges an ADI to give APRA accountability statements and an accountability map. These documents show the governance and management controls in an ADI and show the organisation's lines of accountability. The accountability maps and statements are intended to be viewed as tools of good governance which illustrate that the ADI has appropriate accountability checks and balances and accountable person roles are allocated appropriately according to the size, complexity and customer base of the ADI.[21]

21 Explanatory Memorandum, p. 32.

1.25 An accountability statement is a description of the areas of responsibility attributable to each accountable person, including a comprehensive description of that part of the ADI or its subsidiaries operations over which the accountable person has actual or effective management or control. An accountability statement should align with the accountable person's functions and responsibilities.[22]

1.26 All ADIs must complete accountability maps which accurately show lines of reporting and responsibility in the ADI. Accountability maps can assist APRA to identify accountable persons when an issue arises and may assist ADIs to show the reasonable steps it has taken to avoid any breach of its BEAR obligations.[23]

Consequences of breaching the BEAR

1.27 In addition to its existing powers, APRA may seek pecuniary penalties where an ADI has not:

- met its BEAR accountability obligations;
- met its key personnel obligations, including ensuring that each significant and substantial part or aspect of the ADI's operations are covered by an accountable person;
- met its obligations to register an accountable person and give APRA an accountability statement for that person;
- met its obligations to give APRA an accountability map; and
- met its remuneration obligations, including by deferring variable remuneration as required and having a remuneration policy that meets the BEAR requirements.[24]

1.28 A civil pecuniary penalty must be imposed by a court. The maximum penalty available will depend on the size of the ADI:

- for large ADIs, the maximum civil penalty will be 1 million penalty units (currently $210 million);
- for medium ADIs, the maximum penalty will be 250 000 penalty units (currently $52.5 million); and
- for small ADIs, the maximum penalty will be 50 000 penalty units (currently $10.5 million).[25]

1.29 If an accountable person breaches the BEAR, APRA may disqualify an accountable person from acting as an accountable person of an ADI or in a subsidiary, or a class or classes of ADIs or their subsidiaries. APRA can make this disqualification for a period that APRA considers appropriate. An accountable person

22 Explanatory Memorandum, p. 33.

23 Explanatory Memorandum, p. 34.

24 Explanatory Memorandum, pp. 35–36.

25 Explanatory Memorandum, p. 36.

has protections and rights to procedural fairness under the BEAR. APRA's powers concerning disqualification are subject to merits review.[26]

Examination powers

1.30 The bill gives APRA additional examination powers to investigate potential breaches of the BEAR and extends these powers to all of APRA's supervisory functions under the Banking Act. Applying these powers to the banking sector would mean it was regulated consistently with other industry sectors regulated by APRA.[27]

Indemnification of ADIs and accountable persons

1.31 Indemnification against the financial consequences of breaching the BEAR is prohibited to ensure that breaches of the BEAR have meaningful consequences on ADIs and accountable persons.[28]

Review of the BEAR

1.32 The Minister must initiate a review of the operation of the BEAR three years after the regime comes into effect. A written report must be tabled in Parliament 15 sitting days after the Minister has received a copy of the report.[29]

Financial implications

1.33 The 2017–18 Budget included additional funding for APRA of $4.2 million over the four years from 2017–18 to implement the BEAR. A further $1 million per year will be provided to APRA to enforce breaches.[30]

1.34 The cost of the additional funding to APRA is offset by an increase in the APRA Financial Institutions Supervisory Levies of $8.2 million over four years from 2017–18.[31]

1.35 The Budget also included $1.1 million in additional funding to Treasury to oversee the implementation of *A More Accountable and Competitive Banking System*, of which BEAR is a part.[32]

1.36 The regulatory impact statement indicates that the BEAR will increase compliance costs on ADIs by $11.5 million per year.[33]

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26 Explanatory Memorandum, pp. 37–38.

27 Explanatory Memorandum, p. 38.

28 Explanatory Memorandum, p. 41.

29 Explanatory Memorandum, p. 41.

30 Explanatory Memorandum, p. 7.

31 Explanatory Memorandum, p. 7.

32 Explanatory Memorandum, p. 7.

33 Explanatory Memorandum, p. 67.

Standing Committee for the Scrutiny of Bills

1.37 The Standing Committee for the Scrutiny of Bills reviewed the bill in *Scrutiny Digest 13 of 2017* which was tabled on 15 November 2017. That report identified a number of areas of concern with regard to the bill, including:

- reversal of evidential burden of proof;
- privilege against self-incrimination; and,
- procedural fairness.[34]

1.38 The Standing Committee for the Scrutiny of Bills sought responses on these concerns from the relevant Minister.

Human rights

1.39 According to the Explanatory Memorandum, the bill engages the following human rights and freedoms:

- the imposition of strict liability for an offence;
- the right against self-incrimination under article 14(3)(g) of the International Covenant on Civil and Political Rights (ICCPR); and
- the right to protection from arbitrary or unlawful interference with privacy under article 17 of the ICCPR.[35]

1.40 However, the bill is compatible with human rights because:

- the strict liability offences are appropriate and consistent with the requirements of the Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers;
- the information gathering powers are consistent with the right against self-incrimination under article 14(3)(g) of the ICCPR; and
- the information gathering powers are consistent with the right to privacy under article 17 of the ICCPR.[36]

1.41 The bill is compatible with human rights because to the extent that it may limit human rights, those limitations are reasonable, necessary and proportionate.[37]

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34 Standing Committee for the Scrutiny of Bills, *Scrutiny Digest 13 of 2017*, 15 November 2017, pp. 50–55.

35 Explanatory Memorandum, p. 77.

36 Explanatory Memorandum, p. 81.

37 Explanatory Memorandum, p. 81.