14 February 2020

Manager
Redress and Accountability Unit
Financial System Reform Taskforce
The Treasury
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By email: far@treasury.gov.au

Dear Manager

Financial Accountability Regime Proposals Paper

The Australian Financial Markets Association (AFMA) welcomes the opportunity to comment on the Financial Accountability Regime Proposal Paper of January 2020 (Proposals Paper).

AFMA is a member-driven and policy-focused industry body that represents participants in Australia's financial markets and providers of wholesale banking services. AFMA's membership reflects the spectrum of industry participants including banks, stockbrokers, dealers, market makers, market infrastructure providers and treasury corporations.

AFMA members include Australian-owned banks, foreign subsidiary banks and branches of foreign banks who will be required to comply with the Financial Accountability Regime (FAR). AFMA was closely engaged with the issues arising for our members with regard to the implementation of the Banking Executive Accountability Regime (BEAR) and its oversight by APRA.

1. General Remarks

The accountability proposals raise fundamental issues about the relationship of an individual to the organisation employing them that we do not think are fully resolved into a coherent conceptual framework. In taking policy work forward on this legislative project, AFMA believes that there should be alignment with the concurrent policy work of the Australian Law Reform Commission (ALRC). The ALRC is currently considering

responses to its Discussion Paper 87 on Corporate Criminal Responsibility. There is still substantial work required to develop a more consistent regime for individual liability for corporate misconduct. AFMA has said to the ALRC that this should be undertaken through a collaborative process over a longer time period that works openly with multiple stakeholders to agree on principles, aims, and agreed standards of justice and fairness, prior to developing a final recommendation for law reform.

Overall, at a basic policy level AFMA agrees with the objective of increasing transparency and accountability of financial service entities and improving risk culture and governance for both prudential and conduct purposes. The pace of development in financial services with the attendant IT and operational systems to support their delivery has been great over the last thirty years. Financial organisations have grown so much in size and complexity over this time that governance and risk management systems need to constantly evolve to meet more sophisticated needs. At the same time the level of regulatory intervention in the management of financial organisations has also greatly increased.

The FAR is directing business towards particular governance and risk management structures and reaching down into organisations at a micro level. An important feature of the Australian financial services industry is its organisational diversity. This is good for both customers and promoting healthy competition. It would be detrimental if the overriding determinant for organisational arrangements become the responsibility mapping set by the regulators. Over time regulators are likely to add layers of complexity and rigidity to responsibility mapping which will discourage innovation and growth. This risks ossifying financial services business in Australia, so that it falls behind developments in other parts of the world.

Reforms such as FAR are important drivers of governance and risk management change which are interacting with many aspects of running a financial organisation. AFMA is concerned with the difficulty of assessing whether the FAR measures will necessarily produce the desired beneficial outcomes in a complex and dynamic environment and not lead to excessively risk adverse behaviour which dampens commercial activity.

One of the greatest risks facing the industry is the pace of regulatory change. Regardless of the merits of the many new individual regulatory measures, they all require diligent implementation on tight timetables. This places a great burden on the governance and risk management of financial services entities to assimilate and integrate new requirements. Based on the industry experience with BEAR, the FAR will have priority in claiming management time and resources.

There is simply not enough capacity to commit the time and resources that would be required to implement all the new measures, nor is enough policy time being devoted to fully developing the measures flowing from the recommendations of the Royal Commission into misconduct into the financial services industry. Past experience has

demonstrated that there will be an accretion of sub-optimal and duplicative regulation that will compound the problem that Commissioner Hayne warned about when he said adding a new layer of regulation will not assist. Rather, it will add complexity to what is an already complex regulatory regime.

AFMA appreciates the need to hold financial institutions to high standards of accountability to ensure consumer confidence in the financial system, particularly in the wake of the Royal Commission findings. However, we are cautious that the FAR regime as currently proposed will make the provision of financial services more rigid and costly, which may have a negative impact on the efficient functioning of the financial system and the attractiveness of Australia as a place to conduct business.

2. Scope of the regime

AFMA understands that the BEAR regime enacted under Part IIAA of the *Banking Act 1959* (Cth) (Banking Act) will be repealed, with FAR to be implemented as a stand-alone piece of legislation alongside substantial regulatory guidance. AFMA welcomes this approach as it takes heed of our earlier preliminary comments about the need to rationalise the new regime with the existing BEAR.

While this approach will entail a higher degree of flexibility for change, a degree of caution should be exercised when providing the ability to further expand a regime through regulatory guidance without the same degree of scrutiny required by legislative approval. This detracts from proper democratic and governance processes. It is highly contradictory to demand improved governance standards for financial organisations while weakening regulatory governance standards. AFMA has long been on the record standing up for the principle that it is the role of the Government relying on the advice of its departments of state to make law, not for administrators to make law. Administrators need the scope to sensibly and flexibly apply the law within the boundaries set by Parliament.

To avoid regulatory overreach, the scope of the regime must be clearly articulated in the enabling legislation. The FAR proposal expands the BEAR regime to apply to all APRA-regulated entities, including ADIs, general, life and private health insurers, RSE licensees and authorised NOHCs. We note that the Minister, APRA and ASIC will have the power to exempt entities or classes of entities from the regime.

FAR will, as intended, have an important effect on entities operating in Australia that are subject to the regime. The future extension of FAR to Australian Financial Service Licensees (AFSLs) is being taken into account by the industry as part of its planning. Further on in these comments we raise questions about the extra-territorial application of FAR in respect of APRA regulated entities and the need to carry across BEAR provisions in that respect. There is another issue that arises out of the sequencing of a current ASIC regulatory proposal that is very significant from a FAR perspective. AFMA has previously raised with the Government the highly problematic implications of ASIC's proposals in the form of its Foreign Financial Service Providers (FFSPs) consultation (CP315) to require

licensing of foreign entities not operating in Australia. AFMA is of the view that extending the FAR to FFSPs when AFSLs are added would result in adverse outcomes to business and strongly recommends that FFSPs remain exempt, particularly as no reasons have been articulated to explain why the regime would be required to regulate activities unrelated to retail consumers. As the ASIC FFSP proposals are not part of the Government's policy priority regarding implementation of Royal Commission recommendations and they are consequent to outcomes of FAR implementation, the proposed changes should be delayed for further consideration until the FAR has been implemented with respect to AFSLs.

The FAR Proposal Paper lists the types of entity which will be subject to the FAR. For the purposes of the *Financial Sector (Collection of Data) Act 2001*, APRA maintains a list of "registered financial corporations" that are not otherwise regulated entities by APRA. To ensure clarity it should be made clear the FAR will not apply to any registered financial corporations.

2.1. Categorisation

AFMA supports replacing the distinction between small, medium and large ADIs under BEAR with a different approach that answers the need to account for a broad range of entities with greatly differing scale, complexity and footprint in Australia. The idea of having "core compliance" and "enhanced compliance" categories of entities under FAR, with the classification based on asset size over a three-year rolling period is a good starting point.

We think further work needs to be done on setting criteria for determining whether an entity is a core or enhanced compliance entity (with the consultation currently setting the threshold at $10 billion), as the current BEAR thresholds have proved problematic. For very complex banks or other regulated entities, there are benefits that may arise from having enhanced compliance. However, there are foreign ADI lenders which are simply large because of an asset test but with relatively simple business models. The benefit of applying enhanced compliance is unclear (especially with the administration costs of maintaining this documentation). We would suggest that other measures of complexity be added to justify the enhanced compliance obligations and periodic review for categorisation.

In relation to the power given to APRA and ASIC to reclassify a core compliance entity as an enhanced compliance entity if it is of the view that the entity would "benefit from the requirement to develop and submit accountability maps and statements", we request that guidance is issued on the circumstances that may arise to change regulator views on whether an entity needs to be classified as a core or enhanced compliance entity.

2.2. Meaning of accountable person

While retaining the "general principles" approach, FAR expands the scope of accountable persons by increasing the list of responsibilities defining who is an accountable person.

The indicative list provided with the proposal is numerous and could impact the number of accountable persons at an entity, with a related increase in the administrative burden to those designing and implementing compliance frameworks and expense incurred in making new appointments. While Treasury has indicated to us that it is ultimately up to industry to determine the number of accountable persons required at an entity, the reality is that each accountable person may only oversee so many functions, and the increase in specific responsibilities required to be allocated inevitably means more individuals may have to take on accountable person roles. APRA has previously accepted a "roll up" principle to be used to identify accountable persons - such that the new responsibilities may be rolled up into the existing responsibilities of members of a regulated entity's executive committee. AFMA would like to confirm that the "roll up" principle will be incorporated into the FAR.

AFMA has concerns with some of the very broad responsibilities listed in Attachment B of the proposal paper. Given that a list of responsibilities being prescribed by regulators carries the risk that it will not properly reflect governance structures at regulated entities, AFMA proposes that in order to alleviate these concerns, an independent process beyond consulting with ASIC and APRA is put in place to determine the prescribed list of responsibilities.

We are concerned that given the variance of organisational structures across institutions, the regime will not be able to appropriately account for the range of collective decision-making that takes place, particularly at large firms with offshore reporting lines. It may also be difficult for smaller firms to allocate certain functions due to their limited size. We believe this will continue to be an issue if the regime is expanded to solely ASIC regulated entities.

There are also issues with identifying just one person to be held accountable for a function, especially when it comes to functions that traditionally involve multiple persons in practice. Discussions with Treasury on this matter indicated that the approach to this issue has not been settled. It remains unclear whether accountability should be directed at overarching framework owners, for example, the owner of a breach reporting framework, or if it should go only to those with direct involvement in the process, such as a person with end-to-end management of a specific product.

We acknowledge the work on APRA's previous consultation on end-to-end product responsibility will be subsumed into FAR. As noted in AFMA's submission to APRA on Product Responsibility under the BEAR Regime, it needs to be made clear just how responsibility in relation to a product related service is to be applied in practice.

There is also a need for product responsibility to work with the detail of the Product Design and Distribution Obligations of the *Corporations Act 2001 (Cth)* (Corporations Act). It would be AFMA's expectation that product responsibility simply sets out a simple

requirement for specific accountability with regard to products, with the detail being left to Product Design and Distribution Obligations to provide the detail of the requirements.

Further, the prospect of an uneven playing field is particularly concerning in relation to non-financial services (such as human resources and information technology) which will still be subject to the same accountable person obligations. An entity not subject to the FAR regime will not be subject to the additional deferred remuneration obligations. The risk here is that firms will have difficulty attracting appropriately skilled people for senior manager roles, which is an undesirable result.

AFMA has previously commented in relation to the BEAR remuneration proposals that there is real concern about the effects of increased costs and inefficiencies in attracting and retaining staff in a global market place for senior executives, which appears to be incompatible with the Government's interest in Australia achieving its potential as an international financial centre.

The risks of the migration of talent and business to the less regulated non-ADI or shadow banking sector is highlighted along with the negative risks this creates for prudential regulation more generally. Competitive remuneration practices are an important feature of market economies. Remuneration attracts talent to successful firms and sectors allowing them to build on their success. Less successful firms can also invest in talented leadership and staff to improve their prospects. The result is a significant national good as remuneration practices can assist in attracting talent to where it is most valued within the economy, contributing to the efficiency of the economy.

Wholesale markets are also significantly different in nature to retail markets. Firms in these markets compete for business with regional and global firms. International business can just as readily be done from Singapore, Tokyo or Shanghai. There are risks that applying a solution for retail to the wholesale space may have unintended consequences. Unlike major global financial centres like the United Kingdom, Australia does not have the same degree of freedom in setting regulatory policy for business with an international dimension, as a presence in the United Kingdom for international banks is necessary for global business.

2.3. Foreign ADIs

The Proposals Paper leaves open the possibility that the scope of the FAR regime will expand the operation to foreign ADIs not just limited to ADI branches in Australia. Under BEAR, a foreign ADI is not subject to the regime for offshore operations or for any locally incorporated non-ADI subsidiaries. A foreign ADI should not be subject to FAR for any "significant or substantial" subsidiaries of APRA regulated entities.

The current provision in section 37(2)(b) of the Banking Act, which states that the BEAR "will not apply to a foreign ADI, except to the extent that it operates a branch of the foreign ADI in Australia', should be carried over to the FAR.

The proposed list of particular accountable person responsibilities for a foreign ADI branch now specifically includes the Senior Officer Outside Australia (SOOA), in addition to the senior executive responsibility for the conduct of all the activities of an Australian branch of the foreign ADI.

We note that APRA and ASIC will be empowered under FAR to prescribe further particular responsibilities for a foreign ADI branch including those listed under Items 1 and 3 in Attachment B of the proposal. This is a problematic approach, given that key responsibilities as they relate to Australian operations of a foreign ADI will already be covered by existing accountable persons, namely the person with senior executive responsibility for the conduct of all activities of an Australian branch.

Foreign ADIs would encounter significant practical difficulties allocating many of the other responsibilities being applied. For example, Item 1(f) prescribing an Australian branch of a foreign ADI to allocate senior executive responsibility for information management will be incredibly difficult to implement in the context of an ADI's global information technology systems and brings with it the risk of unnecessary interference in the governance structure and management arrangements of the wider firm. Accordingly, AFMA recommends limiting the responsibilities that can be prescribed to foreign entities.

No mention is made in the proposal paper of including a provision equivalent to sections 37AA and 37BC of the *Banking Act 1959* to handle inconsistency with corresponding foreign laws. It is important that such provisions be included in the legislation. AFMA in this context reminds the Government of the importance of cross-jurisdiction regulatory coordination, our international trade in services obligations under trade agreements and the need for deference in the case where regulation has an extra-territorial effect. Other major financial services jurisdictions already have accountability regimes in place, such as the United Kingdom and Hong Kong, with others looking to implement such a regime. The legislation must allow for deference and sensible outcomes between regulators when dealing with the intersection of their regimes.

3. Accountability and key personnel obligations

3.1. Entities

We note that accountability obligations of an entity under FAR remain essentially the same as under BEAR, save for the requirement for an entity to deal with both ASIC and APRA openly, constructively and cooperatively, and that an APRA-regulated entity must ensure that only "significant or substantial" subsidiaries (as opposed to all subsidiaries as under BEAR) must comply with FAR.

Our comments in Section 2.3 respect of carrying over section 37(2)(b) of the Banking Act for foreign ADIs is important here also.

3.2. Key personnel obligations

While the extension of registration of temporary vacancies to 90 days will be helpful, clarification is sought on what this means for officers filling temporary vacancies. For example, the proposal paper specifies that even though the individual is not required to be registered they are "taken to be" the accountable person, but it is unclear if the person temporarily filling the role is subject to their remuneration being deferred, or whether the individual civil penalties apply to them. If the latter is the case, the question also arises of whether the deferral applies only in respect of so much of their remuneration as is attributable to their role as an accountable person.

3.3. Accountable persons – "reasonable steps"

The accountability obligations of an accountable person under FAR will be the same as under BEAR, other than the requirement to deal with both ASIC and APRA in an open, constructive and cooperative way (subject to legal professional privilege), and the requirement that an accountable person must "take reasonable steps in conducting their responsibilities as an accountable person to ensure that the entity complies with its licensing obligations".

Substantial clarity and guidance are needed on what will constitute "taking reasonable steps" and what factors will be taken into account by APRA and ASIC in assessing this, given the serious legal consequences that flow from it. AFMA is of the view that the inclusive definition of reasonable steps under BEAR (section 37CB of the Banking Act) overlaps with the general concept of due skill, care and diligence. There is no clear distinction between the obligation to act with due skill, care and diligence, which would implicitly require reasonable steps to prevent the entity from undertaking any activities non-compliant with relevant law, and "reasonable steps" in relation to licencing obligations as a standalone requirement.

Any penalty system should focus on systemic conduct and not capture one-off events that are not the result of systemic issues, misconduct or irresponsible management.

With the current wording, a one-off, minor breach of a licence condition of an entity that may have occurred without an accountable person's knowledge may trigger a breach of the accountable person's obligations, as they would have failed to ensure the entity complied with its obligations. We consider that given the role of an accountable person as senior executive, a lower level licensing breach should not go all the way up to the top without serious systemic failings being apparent. Ultimately, this will depend on how "reasonable steps" is understood and how regulators decide to enforce the provision. However, the word "ensures" leaves open the possibility that an individual may be liable if they cannot guarantee that an entity has complied with all licensing obligations and should be removed.

It also needs to be made clear that the obligation to take reasonable steps is limited to those license obligations that directly relate to the accountable persons responsibilities, not the AFSL's full suite of obligations. As drafted the proposals appears to apply to all accountable persons when it should be limited to those with responsibilities that actually encompass oversight of an entity's licence. The prescribed list of particular responsibilities includes responsibilities over the entity's human resources function and information technology systems. It is not apparent what, if any, steps a senior manager charged with responsibility of the entity's human resources function should take to ensure the entity complies with its licencing obligations. The obligation should only apply to those accountable persons where oversight of an entity's licencing obligations is relevant to their responsibilities.

The accountability obligations of an accountable person are currently prefaced in section 37CA(1) of the Banking Act by the following words: "to conduct the responsibilities of his or her position as an accountable person by". An accountable person's obligation to take reasonable steps to comply with licensing obligations is accordingly confined to those parts of an institution's operations that fall within the scope of the individual's responsibilities. We see confirmation that this confinement will apply under FAR.

4. Deferred remuneration obligations

AFMA is generally supportive of the move to simplify the deferred remuneration obligations under FAR to limit the obligations to variable remuneration, with regulated entities required to defer 40% of variable remuneration for all accountable persons for a minimum of four years, only where the amount that would be deferred is greater than $50,000.

We note that APRA's guidance on deferred remuneration under BEAR *(Banking (executive accountability regime) determination No. 1 of 2019)* clarifies that the deferred remuneration obligations only apply to an accountable person's variable remuneration connected to their role as an accountable person. It also contains a concession acknowledging that an accountable person of a foreign ADI does not spend all their time in Australia. Accordingly, the amount forming the basis for calculating variable remuneration for an accountable person of a foreign ADI to be deferred is reduced in proportion to the time spent managing the Australian branch, with any remuneration payable to the accountable person for activities outside of Australia being exempt from the calculation. We note that this has not been specifically provided for in the current proposal paper. For the purposes of consistency, we ask that this is replicated under FAR.

AFMA acknowledges that for regulated entities affected by CPS 511, firms will need to comply with heightened deferred remuneration requirements, and that those complying with CPS 511 will be taken to have complied with the FAR requirements. We propose that the commencement of obligations under CPS 511 and FAR are aligned to allow firms to minimise the administrative burden of compliance.

There remains a concern with the impact of deferred remuneration obligations on competitiveness of firms with respect to staff retention, particularly where there are businesses not affected by the FAR regime carrying out similar activities that will not have to comply with the same obligations. The result may be to deter appropriately skilled people from taking roles with FAR entities, with business addressing this by increasing fixed income to maintain competitiveness with non-FAR entities.

A further issue with the impact on foreign firms is that compliance with FAR and CPS 511 will impact on existing remuneration deferment schemes in place in overseas jurisdictions. As such, there is a need to ensure an appropriate timeframe is given pre-implementation to allow entities sufficient time to change their remuneration policy/procedures.

5. Accountability maps and statements

Under the new regime, enhanced compliance entities must submit accountability maps and statements to APRA and ASIC. AFMA is supportive of the introduction of a materiality threshold reducing the administrative burden on regulated firms by only requiring the notification of material changes to accountability maps and statements within 30 days, with all other changes to be notified on an annual basis. We support the production of guidance on what is meant by “material” changes, as well as certainty on the form of documents.

6. Notification obligations

AFMA recommends the introduction of a materiality threshold for breach reporting under the FAR regime similar to section 912D of the Corporations Act.

Given the expanded nature of the FAR regime, both in terms of scope and increased obligations on entities and accountable persons, to prevent the overreporting of potentially inconsequential breaches a materiality threshold should be introduced to limit notifications to significant breaches.

The notification obligation is set out in isolation from changes to the breach reporting obligations in the draft legislation concerning implementation of the Royal Commission recommendations concerning breach reporting. There needs to be reconciliation of reporting obligations and clear mechanisms regarding how breach reports are to be made where there are two regulators and ensuing investigations are to be handled to avoid duplication and confusion for all parties involved. Given the very serious consequences that flow from the revised breach reporting obligations in the draft legislation these questions must not be left to doubt.

7. Aspects of the FAR to be determined by regulators

While flexibility of FAR is encouraged to ensure that the regime can adapt to the ever-changing financial services environment, a degree of caution is advised when leaving key determinations to administrative rules, rather than prescribing in legislation. To guarantee a level of certainty for affected stakeholders, fundamental aspects of the regime should be covered by legislative provisions, with regulatory guidance serving only to provide further detail on the operation of the provisions in practice, such as details regarding the classification of entities and the circumstances in which an entity may be made exempt from the regime.

8. Penalties

8.1. Penalties for entities

We note that FAR significantly increases the maximum penalty that may be imposed on an entity for breaches of its obligations under FAR, to align with the increase in certain corporate and financial sector penalties introduced in 2019 in the Corporations Act.

Given the potential maximum penalty of 2.5 million penalty units or $525 million, there is a need to ensure proportionality between seriousness of the contravention and the quantum of penalty. Accordingly, AFMA recommends the production of guidance setting out expected penalty ranges for different categories of breach.

Clear guidance is also required as to how the regulators will use the civil penalty power. Section 37J of the Banking Act requires the APRA to have regard to the seriousness of the non-compliance in justifying the disqualification. An equivalent requirement should be included in the FAR legislation along with indication on what degree of seriousness is considered justification. There should also be specification around the question of which regulator is expected to take enforcement action to prevent the unnecessary duplication of resources for investigations by both regulators. At present it is unclear whether enforcement of the FAR regime will be split between regulators or if it will involve setting up a joint taskforce.

8.2. Penalties for individuals

Under FAR, accountable persons remain subject to disqualification by either APRA and ASIC, however the regime also imposes significant civil penalties on individuals for breaches of their obligations. The Proposals Paper gives no indication as to why there is a policy deviation from the applicable Royal Commission recommendations. The existing BEAR provisions do not include civil penalties and the Royal Commission did not recommend that they be extended in this way, nor did the Government's further commitments with respect to the recommendations include this proposal. The introduction of civil penalties is a major development which should not be done in haste bypassing the policy development process.

As the extension of a civil penalties to individuals is outside the agreed policy scope of the Government and has received no proper policy consideration AFMA cannot see any reason for moving forward with this aspect of the proposals. There is already enormous complexity in assimilating the current stock of recommended measures in a highly abbreviated process, where few problems can be thoroughly considered and solved before finalisation of the legislation.

The problem of resolving questions around civil penalties as proposed for FAR is not trivial, as it is likely to raise serious conflicts of law with existing duties and obligation of corporate officers. Under Australian law, the duties of directors and other corporate officers to the company in which they hold office are primarily found in the general law. However, the Corporations Act takes matters considerably further than these equitable and common law principles. In some instances, the Corporations Act imposes duties not only on directors, but on other officers of corporations (see the section 9 definition of "officer"), and in some circumstances on employees.

Statutory duties to which directors and corporate officers are subject include:

- a duty to exercise their powers and discharge their duties with a degree of care and diligence that a reasonable person would exercise (s 180);
- a duty to exercise their powers and discharge their duties in good faith and for a proper purpose (s 181);
- a duty on directors, officers and employees proscribing them from improperly using their position to gain an advantage for themselves or someone else, or cause detriment to the corporation (s 182);
- a duty of confidentiality on directors, officers and employees of corporations, proscribing them from improperly using information they have obtained in their position to gain an advantage for themselves or to cause detriment to the corporation (s 183).

Section 185 of the Corporations Act provides that these statutory duties supplement, rather than supplant, their equivalent duties in equity and at common law.

In defence against the imposition of a civil penalty under FAR, an "officer" may therefore inadvertently impugn the obligations contained in section 181 (by raising as a defence the entities own wrong-doing / policy of wrong-doing), or equally the obligations in section 182 and 183.

The absolute priority should be on implementing the Royal Commission recommendations as decided by the Government and not on introducing novel policy elements through the current legislation.

We also note that the proposed maximum penalty aligns with the increase in the penalties that may be imposed on directors and officers under the Corporations Act. While not

specified in the proposal paper, AFMA has previously stated the view that any provision relating to the quantum of penalty needs to clarify that the calculation of the benefit derived, or detriment avoided because of the contravention relates to the benefit derived or detriment avoided by the individual personally (rather than the entity as a whole). This would ensure alignment with the meaning of *benefit derived and detriment avoided* under section 1317GAD of the Corporations Act.

Further, guidance should prescribe that the removal and disqualification powers will only be exercised where there is a systemic failing that will have a material impact on the entity, and the procedural fairness arrangements that should be put in place to consider such matters.

8.3. Insurance

We acknowledge Treasury's proposal to align the maximum civil penalty for individuals under FAR with the newly-introduced maximum penalties for individuals under the Corporations Act, ASIC Act, Credit Act and Insurance Contracts Act. We note that the prohibitions relating to insurance in respect of such civil penalties are not proposed to be aligned.

Under FAR, it is proposed that entities will be prohibited from indemnifying or paying the cost of insuring accountable persons against the consequences of breaching the FAR. Whilst an accountable person is permitted to purchase their own insurance to cover themselves against the consequences of breaching the FAR, we understand that such insurance coverage is not currently available in the market and, if it were, that for many individuals it may be prohibitively expensive.

We suggest that entities be permitted to pay the premium for a contract of insurance to cover an accountable person for breaches of FAR, other than in respect of wilful breaches. We note that insurance policies invariably exclude cover for liabilities arising from the wilfully wrongful acts or omissions of the claiming insured and, such cover may in any event be void on grounds of public policy. This approach would not undermine the policy objective of deterring individuals from breaching FAR, which is already achieved through:

- the risk of disqualification by APRA or ASIC without the need for either regulator to commence civil proceedings;
- potential reduction in variable remuneration;
- adverse reputational consequences associated with any public enforcement action against the individual;
- adverse impacts on future employment prospects, including in view of the proposed APRA “no objections” power.

This approach also aligns with the prohibition on the payment of insurance premiums by a company for the benefit of its officers in section 199B of the Corporations Act while ensuring that wilful breaches of their duties will not be insured.

9. Non-objections power

AFMA does not agree with the proposal to give APRA the power to veto the appointment of senior executives and directors of regulated entities when APRA is "of the opinion" that a person is not suitable to hold a position as an accountable person. This proposal is highly subjective, with it looking to considerations such as whether a person "failed to deal with APRA in an open, constructive and cooperative way".

The law may state what attributes would make a person unsuitable in an objective way but should not introduce this level of interference in business judgment regarding human resources decisions. Over time it may lead to a regularised slow, bureaucratic pre-vetting process akin to those that are the subject of regular criticism in dealing with business appointments in centrally controlled economies.

10. Extending the regime to solely ASIC regulated entities

AFMA understands that the proposed extension of the regime to solely ASIC regulated entities will be delayed until after FAR is implemented, and this expansion will be subject to a further consultation process.

There are a number of matters that should be considered at this point given the potential cover of the large cohort of ASIC regulated entities such as whether "limited compliance" entities should be contemplated, as has proved necessary under the United Kingdom regime, and the need to replace the responsible manager requirements under Chapter 7 of the Corporations Act.

11. Timeframes for implementation

AFMA recommends that Treasury, alongside ASIC and APRA, produce guidance on timeframes proposed for implementing the regime. As we noted at the start, the pace of regulatory reform is outstripping the capacity of industry to assimilate the change in accordance with prudent change and risk management requirements. The expansion to all APRA regulated entities requires more time to prepare for introduction of accountability frameworks. Experience shows that regulated entities and APRA are at their limit in terms of resource constraints. Accordingly, we propose that Treasury takes a staggered approach to implement the regime in phases across an at least 18-month period.

Any requirements affecting foreign ADIs should be implemented at a later stage to ensure that these entities have sufficient time to make any required changes to their accountability frameworks. Due to the nature of global organisations with multiple branches and complex governance and accountability structures, foreign ADIs face additional complexities in implementing changes which need to be considered.

Further guidance is also needed on the interaction of the FAR regime with other regulatory reforms coming into place over the next 18 months. To reduce confusion, this

should include guidance on transitional provisions ensuring obligations met under BEAR which will be the same under FAR will be taken to have been met. In particular, the new APRA prudential standard CPS 511 Remuneration needs to follow on from FAR implementation and not proceed under the current BEAR rules.

12. Joint administration of FAR

The way ASIC and APRA will operate to jointly administer the regime is of key concern to entities and individuals subject to the new regulations. The exact scope of each regulator in relation to FAR is not clear in the current proposal paper. To ensure that FAR is implemented as efficiently and effectively as possible, guidance should be produced to clarify the role of each regulator in the administration of FAR, outlining how the regime will interact with other statutory obligations and clarifying which regulator is responsible for undertaking investigations and enforcement action in relation to any issues of conduct.

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We have previously discussed with the Treasury the constraints imposed by the abbreviated consultation period, which limits the opportunity for thorough consideration in identifying issues with the proposals. These comments are initial in nature and we will look to take up the Treasury suggestion that we engage further while drafting instructions and the legislation are being prepared. Please contact David Love either on 02 9776 7995 or by email dlove@afma.com.au if further clarification or elaboration is desired.

Yours sincerely

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