Australian Banking Association

16 September 2021

Mr Chris Dreverman

Principal Analyst

Australian Prudential Regulation Authority

By email

Dear Chris,

Follow up to CPG 511 discussion

The Australian Banking Association (**ABA**) thanks the Australian Prudential Regulation Authority (**APRA**) for the meeting on 8 September 2021 to discuss the remaining matters of concern held by the ABA in respect to Prudential Practice Guide CPG 511 – Remuneration (**CPG 511**). In this letter we revert on two of the matters discussed at the meeting for consideration by APRA in finalising the guidance.

Arrangements for employees commencing post 1 January 2023 but before the commencement of the new performance period

The ABA notes APRA's position that the variable remuneration deferral arrangements of new employees commencing post 1 January 2023 and before the commencement of the ADI's new performance year in 2023 (the '**in-between period**') are to be in accordance with Prudential Standard CPS 511 – Remuneration (**CPS 511**). That is, new employees that commence in the in-between period are to be subject to the deferral obligations before the ADI's existing employees and before the obligation for the entity to defer the variable remuneration under CPS 511 commences.

Practically, this would require the ADI's entire remuneration framework to be implemented before 1 January 2023 to comply for a small group of employees. Realistically, for some ADIs, this would mean they would need to be prepared by 1 July 2022. This has the effect of bringing forward compliance with the deferral obligations and counteracting APRA's position to commence the deferral period at the beginning of the new performance period commencing in 2023.

Each ADI manages their performance period on a different time frame (i.e., by calendar year or financial year). The implementation of CPS 511 would need to be flexible to accommodate the different time periods which an ADI can practically and effectively manage, implement, and comply with the changes organisational-wide, particularly for deferral obligations. APRA's position to apply the deferral rules to employees commencing in the in-between period reverts to a single set effective date that would apply across the industry.

The ABA position for deferral requirements to commence with the performance year commencing on or after 1 January 2023 has some overseas precedent. For example, the recent implementation of Capital Requirements Directive V (CRD V) introduced similar changes to deferral obligations in the UK and Europe, which were made effective from the first performance period after the effective date. This aimed to cater to the different performance periods that apply across entities and for these obligations to be implemented consistently and prospectively (after the effective date) for practical implementation in alignment with the entity's performance period for all employees.

The ABA strongly recommends that the start date for variable remuneration deferral obligations of employees commencing in the in-between period align to the ADI-wide commencement of the deferral obligations, namely the date at which the ADI's performance year commences in 2023.

As deferral obligations are closely linked to the remuneration and governance frameworks and for the avoidance of doubt, the ABA continues to strongly recommend that the start date for **<u>all</u>** the CPS 511 obligations (and not just the deferral requirements) be aligned to commence at the beginning of the ADI's 2023 performance year.

Buyouts

The ABA continues to express concern that APRA considers buyout payments to be an equivalent form of variable remuneration to other forms of variable remuneration which an employee would be entitled to under their remuneration arrangements. We consider the recommencing of the deferral period for buyouts to be a significant deterrent to talent acquisition and an unfair burden on the new employee who will be required to forgo a significant portion of their entitlements for a significantly longer time period because they changed employers. Further, the buyout amount does not relate to the employee's objectives at their new employer.

We refer to the requirements of the Prudential Regulation Authority (PRA) which has taken the position that the deferral period of buyouts at the new employer can continue per the original timeline for deferral at the former employer. The PRA also limits the value of the buyout paid by the new employer to the unvested amount of the deferred variable remuneration with the former employer (See annexure). In the Australian context, clause 26(3) of the Financial Accountability Regime Bill 2021 (Exposure draft) Exposure Draft appears to enable APRA to similarly prescribe alternate deferral timeframes for types of payments such as buyouts.

The ABA strongly recommends that CPG 511 specifies the distinctiveness of the buyout, particularly in respect to the continuation (and not recommencement) of the deferral period, and in alignment with the policy of the PRA.

We would be pleased to discuss the above if APRA wishes. Additionally, we look forward to the discussion relating to termination payments with APRA.

Kind regards,

Emma Penzo

Policy Director

Australian Banking Association

Annexure: PRA Rulebook

15A.1 This Chapter applies where:

(1) a ***firm*** agrees with an ***employee*** to pay or provide a ***buy-out***;
(2) the ***buy-out*** relates to employment with, or provision of services to, a previous ***firm*** that was subject to the ***remuneration requirements***; and
(3) the ***employee*** was a ***material risk taker*** in that previous ***firm***.

15A.3

01/01/2017

(1) A ***firm*** must ensure a ***buy-out*** aligns with the long term interests of the ***firm*** including appropriate retention, deferral, performance and clawback arrangements.
(2) The duration of retention, deferral, performance and clawback arrangements applied to a ***buy-out***, or part of a ***buy-out***, must be no shorter than such duration as was applied and remained outstanding in relation to unvested variable ***remuneration*** awarded by a previous ***firm*** to the person as an ***employee*** of that previous ***firm***.

15A.4

01/01/2017

(1) A ***firm*** must obtain ***remuneration statements*** from the ***employee*** before agreeing to provide the ***employee*** with a ***buy-out***.
(2) The amount of a ***buy-out*** may be no greater than the aggregate amount of unvested variable ***remuneration*** referred to in the ***remuneration statements*** provided to the ***firm*** by the ***employee***.

15A.10

01/01/2017

A ***firm*** must not:
(a) structure any element of an ***employee's remuneration*** in a way that could result in ***remuneration*** which otherwise would be characterised as part of a ***buy-out***, not being characterised as such; or

PRA Supervisory Statement (July 21) - Buy-out awards:

5.35 Buy-out awards differ from guaranteed variable remuneration and represent a practice whereby firms buy-out outstanding deferred bonus awards for staff that have been cancelled by their previous employer. The PRA expects firms to structure buy-outs so that they vest no faster than the awards they replace.