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General Manager, Policy
Policy and Advice Division
Australian Prudential Regulation Authority

policydevelopment@apra.gov.au

Dear General Manager

Submission: Proposed amendments to CPS 511 and draft CRS 511.0

Guerdon Associates appreciates the opportunity to provide its submission on the proposed disclosure and reporting requirements in support of the introduction of CPS 511.

This submission provides summary comments, responds to consultation paper questions and the revisions in the draft regulation, and provides feedback and suggestions where we see the potential to improve the draft standard for better prudential supervision, compliance and effectiveness. A brief background on our firm is attached.

Summary comments

The stated premise for the introduction of enhanced disclosure requirements is that they will improve transparency, market discipline and reinforce accountability.

The reference to market discipline infers markets will respond to more disclosure. The inference is that stakeholders will provide capital to, and purchase services from, providers on a risk-adjusted basis. However, there is little evidence to support the contention that remuneration disclosures will be a primary driver of market behaviour:

- a) Bank customers are attracted by high deposit and low loan interest rates and availability
- b) RSE customers are attracted to superannuation fund returns
- c) Insurance customers by good coverage for low costs
- d) Investors are attracted to high risk-adjusted returns and TSR.

While remuneration governance may factor into investment algorithms for the latter, they are not primary drivers of investment decision making.

The rationale for transparency is sound enough. However, there is a danger of over-egging its importance relative to other, more relevant factors in which transparency can more discernibly enable APRA to prudentially supervise the market players. This is because prudential supervision is APRA's primary purpose rather than the collection of data to be available to the broader market for purposes that do not necessarily enable better prudential management/supervision.

Hence, we have reviewed the proposed amendments from the perspective the extent that the amendments *better enable the prudential supervision of capital markets by APRA*.

In assessing the proposals on this basis, Guerdon Associates have stood back and assessed what remuneration reporting and disclosure is important for prudential supervision and what

is unimportant. This analysis enabled us to suggest the unimportant or irrelevant aspects be deleted, and to make suggestions how the important and relevant aspects can be improved.

This resulted in a significant reduction in disclosure requirements. However, this reduction was moderated by recognising that Australia has made commitments as a member of the Basel Committee on Banking Supervision. Even so, scaling back disclosure requirements to that promulgated by the Basel Committee on Banking Supervision (with an allowance for the additional cohorts already required under Australian regulation) will significantly reduce costs of compliance, enhance consistency, result in fewer errors, increase reliability, and will not negatively impact prudential supervision.

Response to consultation paper questions

Consultation Questions	Response If blank, Guerdon Associates has no response.
Disclosure requirements	
1. Do the proposed disclosures provide sufficient information to support greater transparency and market discipline on remuneration practices, and if not, how could they be improved?	<p>More than sufficient for market discipline.</p> <p>Our response to Q2 lists those items that arguably do not enable improved market discipline but do impose additional costs for compliance and reporting.</p> <p>Improvement in terms of quality of reporting and industry cost effectiveness will come from removing some requirements and refining others.</p>
2. Are there any further items that should be disclosed, or items that should not be disclosed?	<p>CPS 511 remuneration reviews Table 1, row 3 requires disclosure of changes to the remuneration framework and reasons for changes arising from reviews of the framework. The reasons for any such changes will often be commercially sensitive, so an allowance should be made to circumscribe disclosure in this respect. Such disclosure to the broader market does not, of itself, better enable APRA to prudentially supervise.</p> <p>However, the requirements for fuller disclosure under CRS 511 rows 10 and 11 can remain for supervision purposes as this can potentially improve APRA's prudential supervision capacity.</p> <p>CPS 511 Table 2:</p> <ul style="list-style-type: none"> • add a new item – total assets (ADIs) FuM (RSEs), premium income (Insurers) • replace items 1 with FTE# • Delete items 3, 4¹, 5, 6, 7, 8, 10, 11, 12, 14, 15, 16, 17, amend 18

¹ Although deletion is suggested if retained it conflicts with the footnote definition, which suggests it is VR. The footnote definition does not accommodate fixed remuneration delivered as shares or share rights. In this it is inconsistent with other regimes (see the UK PRA's SUP 16 Annex 33AR Remuneration Benchmarking Report at https://www.handbook.fca.org.uk/form/sup/sup_chapter16_annex33AR_20150630.pdf?date=2016-03-07), making international comparisons impossible.

	<p>There is no clear rationale how the public disclosure of this information can improve market discipline or better enable APRA to prudentially supervise the market participants.</p> <p>Yet, the collection and collation of this data will be a significant cost for the entity and potentially obfuscate the more important and relevant data.</p> <p>Paragraph 45 and Footnote 13 refer to specific exemptions and include an exemption <i>"to enable the person to cover taxation obligations arising from the deferred variable remuneration at termination."</i> Termination of employment is no longer a taxing point. Suggest this reference be excluded.</p> <p>Table 3 item 1:</p> <ul style="list-style-type: none"> • Add a Footnote to define "Special payments are sign-on awards or severance payments" • Item 2: delete item 2 • Item 4: add footnote defining sign-on awards, clarifying if it is an inducement to be employed, a buy-out of forgone benefits, or both • Item 6: add a footnote defining severance payments. <p>Table 4, delete items 1, 2, 3, 4, 5. If retained footnote a definition of cash linked instruments, as share-based payments are usually inclusive of a cash settlement alternative.</p> <p>Similarly, delete items 7 to 10, 12 to 15, 17 to 20, 22 to 25. Amend 26.</p>
<p>3.What are the implementation challenges of APRA's disclosure proposals?</p>	<p>A significant challenge for the disclosure proposals is that noted above in the absence of clear definitions and understanding of the various components of remuneration. This will lead to unreliable and inconsistent reporting of data, as well as significant compliance costs for the entities seeking to accurately disclose that which is required.</p> <p>The disclosure requirements do not cater for SFI structures where reportable roles may span divisions or subsidiaries that are not APRA-regulated and not captured by the requirements. Pro-rating remuneration according to relative division size (total assets) would be one approach.</p> <p>Consequence management adjustments would be reported in full where they occurred within the regulated subsidiary. In some circumstances, the VR adjustment could exceed the reported remuneration pro-rated by reportable entities. The complexity presented by multiple business units and reporting structures will require additional administration and time to complete to ensure accurate reporting.</p> <p>The reported data will also not be transparent and there is little value in its public disclosure enabling better prudential supervision by APRA – refer our earlier comments.</p> <p>Guerdon Associates' suggestion:</p> <ol style="list-style-type: none"> 1. Clear and specific definitions of all components of remuneration 2. APRA liaise with those SFIs where the business mix includes non-APRA regulated entities to map the

	<p>complexity of captured roles and cohorts and the implications to the reporting requirements.</p> <ol style="list-style-type: none"> 3. Pro-rate the remuneration for captured roles based on total assets for those regulated entities falling within the position scope (consistent with the classification used by APRA to define the scale of reporting entities). 4. Downward adjustments if occurring within the APRA regulated entity would be reported in full.
4.How would RSE licensees seek to address the disclosure proposals in CPS 511 in a manner consistent with existing SIS Act obligations, particularly in relation to CEO disclosures?	Given that superannuation assets tend to be more mobile than bank assets, and respond to market forces more readily, there do not appear to be any requirements for differences in treatment, especially with simplification suggested above.
5.What is the appropriate level of assurance over disclosed information?	As indicated above, there is a high likelihood of unreliable and inconsistent data for some disclosures in the absence of clear definitions and consistent practices across entities.
6.What are the compliance costs of APRA's proposed disclosure requirements in CPS 511 and how could APRA reduce compliance costs and impacts?	
Reporting requirements	
7.Are there any systems or implementation challenges with reporting remuneration data?	<p>There are inconsistencies between CPS 511 and CRS 511.</p> <p>Specifically, there are regulatory reporting and disclosure requirements not sought by the reporting standard. It would be expected that the higher standard should be for reporting to APRA, rather than public disclosure.</p> <p>An example is CPS 511 row 6 of table 1. This is not required in CRS 511. Other examples are as described above.</p>
8.What are views of interested parties on declaring CRS 511.0 to be non-confidential?	Much of the data will be commercially sensitive.
9.What is the appropriate level of external assurance over remuneration data reported to APRA?	<p>CPG 511 references annual compliance and effectiveness reviews, but relates these to CPS 511. While one could assume compliance also means compliance with CRS 511, CPG 511 could make this more explicit.</p> <p>CRS 511 Valuation – The share based payments valuation methods proposed are:</p> <ul style="list-style-type: none"> • Inconsistent between variable remuneration that is "share based payments" on grant date and that which is share based options plans on grant date

	<ul style="list-style-type: none"> Includes a method that, while used by proxy advisors and some investors, does not reflect fair value or intrinsic value, and lacks validity. It may reflect poorly on the technical abilities of data users not to understand or use fair value measures consistently for all applications. Unnecessary to have 2 different bases where the fair value based method for options plans could be applied to both Is comprised of a method for "share based payments" on grant date that is inconsistent with accounting standards Is comprised of a method for "share based payments" on grant date that is inconsistent with a valid method of determining value Is comprised of a method for "share based payments" on grant date that makes comparison invalid, and therefore does not support the reason for reporting Is comprised of a method for "share based payments" that overstates value on grant date for dividend paying organisations <p>All of these observations potentially lead to an unreliable understanding by those charged with supervision of the remuneration frameworks across entities and can result in invalid findings.</p>
10.What are the compliance costs associated with the proposed CRS 511.0? Do the reporting proposals meet APRA's objectives in an efficient and least-cost manner for industry?	
APRA publication	
11.Is the proposed publication sufficient to provide comparability of remuneration outcomes across entities?	<p>More than required. See response to 2.</p> <p>It is difficult to see how the publication of much of the data can improve the prudential supervision of the participants.</p>
12.What other remuneration data should APRA publish for all entities?	See response to 2.
13. Is the masking of small cohort sizes sufficient to address the risk that remuneration outcomes of individuals are discernible from published data?	This could occur. Provide a safe harbour for cohorts less than 5. Data will still be received by APRA though CRS 511 for supervision purposes.

Concluding remarks

Guerdon Associates trusts that our observations and suggestions are of value, and appreciate the opportunity to make this submission.

We would be pleased to respond to any queries you may have in relation to this submission.

Attachment: About Guerdon Associates

Guerdon Associates is an independent board and executive remuneration and ESG consulting firm. Our clients include a significant proportion of companies in the ASX 300, large private companies and pre-IPO companies. Offices are located in Melbourne and Sydney, with affiliate offices in London, Zurich, New York, Toronto, Los Angeles, Singapore and Johannesburg. The firm has worked with the boards of many of Australia's largest ASX-listed financial services providers including banks, insurers, superannuation funds and other APRA-regulated entities.

The firm's submissions were among the most cited in the Productivity Commission's review of executive remuneration and, over the years, it has contributed to Treasury, ASIC, APRA, Australian Taxation Office and CAMAC consultations on numerous Corporations Act and taxation legislation changes, as well as regularly engaging with APRA and ASIC on remuneration matters.

As a provider of remuneration and governance advisory services and an expert observer of the impact of executive remuneration internationally, the firm can provide useful insight into:

- the effects of various remuneration frameworks; and
- alternatives or modifications that may more effectively contribute to sound prudential management.