



FINANCIAL  
SERVICES  
COUNCIL

# APRA CAPABILITY REVIEW

Submission to the APRA Capability Review Panel

10 April 2019



## About the Financial Services Council

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in Australia's largest industry sector, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing almost \$3 trillion on behalf of more than 14.8 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

## Background

In 11 February 2019, the Treasurer announced a capability review ("**Review**") of the Australian Prudential Regulation Authority ("**APRA**"), by a panel led by the Chair Graeme Samuel AC, Diane Smith-Gander and Grant Spencer ("**Panel**"). It was noted that the Review will provide a forward-looking assessment of APRA's ability to respond to an environment of growing complexity and emerging risks for APRA's regulated sectors.

The Panel released the final Terms of Reference for the Review and invited all interested parties to make a submission regarding APRA's capability per the final Terms of Reference by 10 April 2019.

In summary, we note that the objectives of the Review are to:

1. Assess APRA's capability to deliver upon its statutory mandate under the APRA Act and relevant industry acts.
2. Undertake a forward-looking assessment of APRA's ability to respond to an environment of growing complexity and emerging risks for APRA's regulated sectors.
3. Identify recommendations to enhance APRA's future capability, having regard to the changing operating environment and any relevant organisational initiatives which are already underway.

Also, as part of its work, the Panel will be evaluating the extent to which nine factors identified by the Panel support APRA to deliver its statutory mandate.

### **FSC submission to the Panel**

We thank you for the opportunity for the FSC to make a submission to the Panel in relation to the Review. This document includes FSC's feedback and high-level recommendations in relation to three of these factors that could have significant impact to APRA's future capability with regard to changing operating environment globally and in Australia:

1. Culture that supports supervisory and enforcement actions in support of strategic objectives;
2. Robust internal governance arrangements, supported by fit-for-purpose internal reporting, performance monitoring and audit and assurance activities; and
3. Appropriate engagement with Australian financial sector regulators, including suitable information sharing arrangements

We would welcome the opportunity to discuss further any queries the Panel may have in connection with FSC's submissions.

**Dated:** 10 April 2019



David McGlynn

Senior Legal Counsel

## Recommendations to consider:

### 1. Culture that supports supervisory and enforcement actions in support of strategic objectives;

We understand a number of regulators in the well - developed countries have undertaken their own internal risk culture assessments as part of the OECD Regulatory Review and G20 Governance and Culture initiatives. (Samples being: DNB Bank have engaged external consultants twice in the period of the last three years. *Ref: Speech/presentation by Melanie De Waal, DNB, at the Culture & Governance in Financial services Conference 13-15 November 2018.* Ms De Waal also mentioned that other banks that she worked with including the Irish Central Bank are also considering to undertake their own culture assessments.) Perhaps, in light of the findings of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (“**Royal Commission**”) and APRA’s internal audit report undertaken by ANAO (<https://www.anao.gov.au/work/performance-audit/prudential-regulation-superannuation-entities>), APRA would also consider to bring an external expert/consultant to undertake its own culture review?

### 2. Robust internal governance arrangements, supported by fit-for-purpose internal reporting, performance monitoring and audit and assurance activities;

In November 2016, ANAO have published the summary of APRA’s audit report the purpose of which was to assess the effectiveness of APRA's processes for the prudential regulation of superannuation entities (<https://www.anao.gov.au/work/performance-audit/prudential-regulation-superannuation-entities>).

There are two recommendations made by ANAO that we believe APRA might already be in the process of addressing:

Recommendation 1: To promote proportionate, risk-based supervision of superannuation entities, APRA implements measures to provide greater consistency in the supervision of entities with similar risk profiles; and

Recommendation 3: APRA implements a quality assurance framework that includes independent reviews of the work undertaken by supervisors.

We understand the design of such quality assurance framework (Ref: Royal Commission Interim Report and Mr W Byres' speech – Nov 2018) only started in late Sep – Oct 2018. We also believe given recent APRA's internal restructuring and creation of the new Risk and Data Analytics (**RDA**) division as an internal centre of expertise for APRA's supervisors, the internal quality assurance process should reinforce the following:

1. RDA specialist knowledge/information is continuously available and consistent to all APRA supervisors within defined timeframes. [This would ensure that all entities have some consistency around similar risks and information/advice provided to them.]
2. APRA Supervisors are adequately trained by RDA risk teams (or external providers) to ensure they are operating at arms - length and not too attached or too close to their supervised entities. [This would ensure there are no personal opinions or views that might impact certain risks' overview of the entity or impact the quality of the supervision provided.]

We understand that some APRA's Supervisors do choose to engage RDA Risk Teams occasionally and on ad-hoc basis, while others – do not engage RDA Teams at all. Hence the framework ensuring some consistencies or even similar internal suit of products and services offered by RDA teams to Supervisors would make current processes are more efficient and transparent. This would also support internal knowledge transfer for APRA staff.

### **3. Appropriate engagement with Australian financial sector regulators, including suitable information sharing arrangements.**

While one of APRA's strategic goals introduced in FY18 (Corporate Plan 2017-2021) was to explore a partnership approach with various government agencies and financial services industry representatives, the engagement and information sharing processes utilised by APRA might need to improve further in order to reflect continuously changing operating environment. Perhaps samples of regulatory innovation in other well-developed countries can be used to slightly re-focus APRA's approach to working with industry.

For example, in light of Royal Commission report and Round 7 hearing (November 2018), the following might need to be looked into:

- 3.1. Similarly to DNB Bank's Expert Centre on Governance, Behaviour & Culture (<https://www.dnb.nl/en/about-dnb/organisation/legal-and-organisational-form/organogram/index.jsp>), APRA's RDA division has its own Governance, Culture and

Remuneration (“**GCR**”) Risk Team that acts as an internal knowledge centre of expertise covering risks associated with BEAR, Risk Governance Self Assessments, Fit & Proper requirements and others. We understand that DNB’s Expert Centre on Governance, Behaviour & Culture engages with DNB’s regulated entities in a way that is more focused on sharing the information, assisting entities to understand on how they are measured against their peers and more importantly, - explains DNB’s principals of supervisory approach and what it means in practice. The DNB’s Centre of Expertise also advises on the relevant remediation actions that might need to be adopted in order to improve entity’ specific frameworks and processes. We also understand that DNB’s Centre of Expertise is not using the information disclosed by their regulated entities during such meetings to their (DNB) direct supervisory division. This helps banks and financial institution to have open and transparent conversations, and to discuss real time challenges without being issued a contravention notice. Perhaps APRA should look into adopting similar practices between their supervised entities and GCR Team?

3.2. Any frameworks that APRA would use in order to assess, let’s say, Risk Governance Self Assessments or Operational Risks, should be also disclosed at high level/shared with the entities to achieve full transparency of the supervisory approaches or methodologies used. For example, PAIRS approach/logic/metric was disclosed to the entities/public previously, however the methodologies used behind assessing non-financial risks of APRA regulated entities – still remain the mystery.