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APRA's BEAR Implementation Review
Does it change your BEAR framework (or FAR plans)?

What is the BEAR Implementation Review?

The Banking Executive Accountability Regime (**BEAR**) is viewed by many as a major regulatory step-up, imposing additional personal accountability requirements across the Australian banking sector. The BEAR – and its industry-wide expansion through the Financial Accountability Regime (**FAR**) – is a weighty lever, intended to transform corporate culture.

The release of the BEAR Implementation Review in December 2020 (**Review**) marks "the end of the beginning" of this push. The Review looked at the arrangements of Australia and New Zealand Banking Group Limited (**ANZ**), Commonwealth Bank of Australia (**CBA**) and National Australia Bank Limited (**NAB**) 18 months in.

Westpac Banking Corporation remained side-lined, thanks to ongoing APRA investigations. The Review found all three major banks had "adequate" frameworks in place, though there was room for improvement across the board.

APRA expects these organisations to take its key observations into account. This expectation was borne out by ANZ, CBA and NAB's commitments following the Review to address APRA's feedback.

The same expectation, by implication, now extends across the industry.

So, what does this mean for you?

"When a regulator proactively shares best practice, it comes with expectations attached."

What action do you need to take?

The right approach to implementing BEAR or FAR continues to depend on your organisation's relative size and complexity.

Consequence management

What the Review found

APRA reiterated its focus on ensuring each organisation has "robust" consequence management arrangements, with demonstrable remuneration impacts for Accountable Persons where appropriate.

Getting this right has proved challenging – where NAB's approach was criticised for a lack of detail, ANZ's approach was considered "overly complex".

What it means for you

The key to designing a consequence management framework is to treat the different breach and consequence management activities as a single process, and map the potential conflicts of interest end to end.

A conflicts-based analysis may have helped ANZ recognise and avoid the situation where potential breaches were reviewed at divisional consequence management forums, chaired by the same executive Accountable Person who may eventually be found accountable for misconduct identified.

In most cases, a conflicts-based analysis will result in a need for:

- qualitative and quantitative criteria to define breaches;
- a clear escalation process, including arrangements for referring breaches for further investigation which vary according to who is involved in the breach; and
- robust and impartial investigation processes, which also vary according to who is involved in the breach. These should deal with the possibility of the most senior executive Accountable Persons being implicated (eg in relation to funding decisions) with clear procedures for non-executive directors to assume control.

Finally, while it would be a provocative mistake to try and cloak the entire consequence management process in legal professional privilege, you still need to ensure legal professional privilege is appropriately maintained throughout, and that Accountable Persons have access to legal counsel where necessary.

Insight

What the Review found

APRA expects board members and executive management to be able to demonstrate their understanding and implementation of the BEAR obligations through ongoing prudential engagements.

In this context, CBA, ANZ and NAB have all initiated various forms of post-implementation assurance over their BEAR implementation.

What it means for you

When designing your board and executive briefings, keep in mind the need to both:

- explain the key program design choices and their rationale, as well as any material assurance findings; and
- arm each director and executive with clear, meaningful speaking points to demonstrate their understanding of these.

Newer directors and executives can find mock interviews helpful.

Reasonable Steps

What the Review found

When it comes to creating records evidencing the “reasonable steps” taken by Accountable Persons, the large banks have struggled to find an operating rhythm.

– **Practices and tools**: The large banks were found to be using a mix of principles-based frameworks, delegations and “demonstrated practices reflecting individuals’ executive style”. There was significant variety within these “demonstrated practices”. CBA and NAB experimented with principles-based guidance and sharing examples of different practices internally in an effort to increase standardisation.

– **Monitoring and assurance**: The large banks came to different conclusions on the monitoring and reporting required, as indicated by the different levels of resourcing for their centralised BEAR functions. APRA found room for improvement across the board, including the development of periodic reporting to assess BEAR compliance.

What it means for you

It is understandable that Accountable Persons and their delegates want a simple way to know whether their reasonable steps record-keeping practices are sufficient.

The short answer is that APRA has not identified better practice when it comes to “reasonable steps” record-keeping. The longer answer is that the clearest guidance continues to be found in the BEAR itself, which sets a baseline by defining the taking of “reasonable steps” as including – in relation to the matter in question – having:

– appropriate governance control and risk management;

– safeguards against inappropriate delegations; and

– procedures for identifying and remediating problems that arise or may arise.

APRA’s reticence when it comes to identifying better practice in this area is understandable for the following reasons:

– It doesn’t take much imagination to see the likelihood of this issue being central to high profile enforcement cases in years to come. With inclusive statutory draft, and without case law on point, APRA risks providing false comfort, as well as setting itself up for a costly fall.

– The proximity of the reasonable steps requirements to existing legal obligations provides additional disincentive. It is common practice for directors and officers to rely on an ad hoc mix of company and personal records to satisfy the Business Judgment Rule in section 180(2) of the Corporations Act 2001(Cth) to create a presumption they have satisfied their duty of care and diligence.

For APRA to anoint certain records over others, without any apparent statutory basis for doing so, would be strolling in a minefield of unintended consequences.

In the circumstances, APRA appears open to the incremental development of market practice and, to some extent, to be banking on the development of monitoring programs to drive innovation and consistency. In practice this means that centralised BEAR functions are expected to become the invisible hand within organisations, using a mix of policy, monitoring and communication tools to cultivate a culture of personal accountability. This may be a thankless task – the fact that APRA focused on the number of bodies in each team says something about how difficult it is to measure their impact otherwise.

Scenario testing

What the Review found

Although all the large banks used interviews, workshops, challenge sessions and scenario testing as part of their implementation, only NAB had an ongoing scenario testing program to proactively identify accountability gaps and overlaps.

Following the Review, both CBA and ANZ committed to building out their scenario testing program.

What it means for you

Scenario testing is a core feature of any BEAR or FAR program.

– There is now some clarity that an annual board scenario exercise is likely to be sufficient, with additional workshops for executives and their direct reports.

– At a minimum, your program should test the interaction between business, operations and technology executives, including the ownership of data assets. It also makes sense to cross-check your scenario testing program against your organisation's Risk Appetite Statement to ensure it is realistic. This means cybersecurity-related scenarios will be essential for most organisations.

– Your scenario testing program should also recognise the likelihood of changes in Accountable Persons (or their direct reports) and/or organisational changes which shift accountabilities, and show you have planned accordingly.

Accountability Statements and delegations

What the Review found

The large banks have taken conflicting approaches to how they document Accountable Persons' delegations to their direct reports.

– CBA and NAB created individual delegations, with an indirect link into performance management.

– ANZ created generic delegations with a direct link into performance management.

APRA did not back either approach, concluding instead that better practice "could involve the more rigorous aspects of both." That said, following the Review, ANZ committed to developing tailored delegations, and CBA committed to cascading responsibilities two layers down, suggesting that tailored delegations are the way forward.

In this way, APRA appears more open to the value of incremental improvements in this area – as opposed to, say, the more immediate need for an effective consequence management framework. Given the purpose of scenario testing is to identify improvements, this makes sense.

What it means for you

If you haven't already, you should put thought into Accountability Statement management. You will need to ensure:

– "robust" governance and version control to deal with shifting personnel and responsibilities on an ongoing basis, e.g. handover checklists for on-boarding new Accountable Persons or delegates; and

– the right access arrangements to give Accountable Persons and their delegates easy access to the latest arrangements, while maintaining appropriate confidentiality. That said, an APRA spokesperson was recently quoted saying it would be an "excellent idea" for banks to make BEAR accountability statements available to all staff to increase transparency.

Many organisations will be able to leverage existing workflow tools (e.g. Trello, JIRA, Sharepoint) – though they may need to live the challenge of managing Accountability Statements manually to realise the need to do so.

Lessons from London

What practical cues can you take from the UK Senior Managers and Certification Regime (SMCR)?

Key BEAR/FAR concepts – such as reasonable steps – have their roots in the UK SMCR requirements. This means the UK experience gives you leading indicators of how BEAR/FAR may operate locally. Our London-based colleagues share two:

1. Don't expect regulatory guidance on reasonable steps.

In the early days of SMCR, the lack of clarity on what constitutes reasonable steps meant many Senior Managers were uncomfortable relying on frameworks, and tempted to:

- make contemporaneous notes of every last interaction relating to their responsibilities; and/or
- request written attestations from their delegates at every turn.

Some executives were so anxious about protecting themselves that they covertly used private dictation services to create their own records, creating a range of confidentiality issues. These reactions alarmed the UK regulators, who feared the emergence of a blame culture.

Instead of offering further guidance, the regulators opted for a soft but deliberate messaging campaign to the effect of "if you are operating a sound risk business with good controls you have nothing to worry about – our expectations haven't changed, we are just articulating them more clearly". This targeted reassurance was reinforced over time by the very measured way the regulators exercised their supervisory and enforcement powers for breaches of these requirements.

The UK regulators' approach is generally regarded as successful, with Senior Managers taking appropriate comfort while the quality of governance has perceptibly improved.

2. There's teething pain to come

Many UK firms mistakenly thought the work was done once their Statements of Responsibility and Responsibility Maps were submitted and approved – failing to recognise the heavy lifting required to manage ordinary levels of Senior Manager turnover, as well as the routine annual training and attestation requirements.

While the large Australian banks have clearly put thought and investment into managing their ongoing operational burden, smaller organisations may be tempted to manage these arrangements manually using existing resources, at least initially. The UK experience suggests this approach may be painful, and short-lived.

How can A&O Consulting help?

We are experts in governance, regulatory strategy, risk management and corporate culture. With specialist teams in Australia, the UK and the U.S., we have a hands-on understanding of global best practice. Importantly, as former regulators and industry experts, we understand the need for practical, cost-effective and sustainable solutions.

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