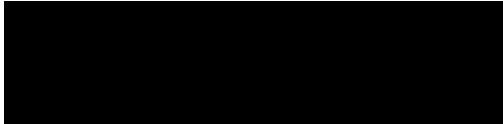


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22 October 2019



Policy and Advice Division
Australian Prudential Regulation Authority

By email: PolicyDevelopment@apra.gov.au

Dear Ms Richards,

QBE submission: APRA Discussion Paper – Strengthening prudential requirements for remuneration

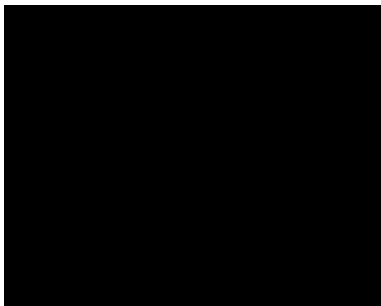
QBE welcomes the opportunity to comment on the proposals outlined in APRA's Discussion Paper released on 23 July 2019 and on the draft *Prudential Standard CPS 511 Remuneration*. We would also like to thank APRA for meeting with QBE during the consultation period.

This submission is on behalf of the QBE Insurance Group Limited and the Level 1 insurers comprising QBE Australia Pacific (collectively "QBE").

QBE supports APRA's objectives to improve accountability and achieve greater balance in assessing performance so that remuneration arrangements promote effective management of both financial and non-financial risks, sustainable performance and long-term soundness. Our feedback on the proposals in the Discussion Paper and draft Prudential Standard seek to build on these objectives in a way that can be implemented effectively, is applicable across the industry and minimises impact on efficiency and competition in the market.

We would be pleased to provide any further information that assists APRA's consideration of the feedback provided in our submission.

Yours sincerely





QBE Submission:

APRA Discussion Paper
Strengthening prudential
requirements for remuneration

OCTOBER 2019



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1 Executive summary

On 23 July 2019, APRA released draft Prudential Standard CPS 511 Remuneration (CPS 511), with the proposals aiming to ensure that an entity's remuneration arrangements produce appropriate incentives and outcomes. In doing so, APRA has considered its primary objective to improve financial safety and promote financial system stability. In addition, APRA is seeking through CPS 511 to strengthen remuneration frameworks with the long-term interests of entities and their stakeholders, including customers and shareholders.

The proposed CPS 511 reforms address recommendations 5.1 to 5.3 from the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Royal Commission or RC), which were endorsed by the Government and APRA in February 2019.

QBE believes remuneration-related regulation is most effective when it is principles-based, underpinned by ongoing and effective supervision and where appropriate, subject to intervention by the regulator.

While QBE fully supports the recommendations of the Royal Commission and APRA's objectives for CPS 511, we believe the prescriptive elements of CPS 511 will lead to unintended consequences that are counter to APRA's primary objective of financial system stability.

In its current form, CPS 511 will provide QBE and other APRA-regulated entities with a significant disadvantage in attracting and retaining talent. For QBE, with more than three quarters of our workforce and business written outside of Australia, this challenge is magnified by the application of the standard across the Group creating an uneven playing field with our industry competitors in our key markets outside of Australia.

The impact of such unintended consequences could result in a gradual talent drain from Financial Services to industries and jurisdictions where less onerous or no regulatory remuneration requirements exist, and/or drive up the cost of fixed remuneration. In our view, neither of these outcomes support APRA's primary objective of promoting financial system stability.

In preparing this submission, QBE has provided suggested alternative approaches that we believe address our key areas of challenge. We have sought to achieve this in a way that is applicable across the industry and meets or enhances the objectives of CPS 511.

The specific challenges of CPS 511 for QBE and suggested alternative approaches are summarised in **Table 1** below and expanded upon in more detail in this submission. These specifically respond to APRA's consultation questions under the headings of 'Remuneration Design' and 'Remuneration Outcomes'. While not a focus of this submission, Section 4 sets out QBE's response to APRA's specific consultation questions under the remaining headings of 'Remuneration Framework', 'Board Oversight' and 'Transparency'.

Table 1: Summary of key challenges for QBE and suggested alternative approaches

#	KEY AREA OF CHALLENGE	SUGGESTED ALTERNATIVE APPROACH
1	Entities such as QBE, with a large proportion of its operations outside of Australia, will be at a significant competitive disadvantage in attracting and retaining talent in local markets	1. Allow a proportionate approach to be adopted for persons subject to 'equally as effective' remuneration regulation.
2	CPS 511 does not apply the prescriptive remuneration requirements proportionately to allow for the material differences in the risk profiles of general insurers compared to banks	2. Apply a tiered approach to the deferral portion, recognising the differing size and complexities of Significant Financial Institutions (SFIs) in a similar way to the Banking Executive Accountability Regime (BEAR). 3. Tailor the deferral periods applying to SFIs, recognising the differences in risk profiles across the financial services sectors.
3	There are practical implications of the proposed limit on financial measures in variable remuneration arrangements which will result in conflicts with APRA's primary objectives	4. Limit the use of financial measures in long-term variable remuneration arrangements by introducing a prescriptive requirement to modify the long-term variable remuneration outcomes based on non-financial factors (rather than a cap on weighting).
4	There are practical implications of the proposed clawback provisions which will limit the effectiveness of its application	5. Align the clawback period to be the same length as the maximum deferral period whilst retaining the extended clawback period where an investigation is in progress. 6. Condense malus and clawback criteria into one remuneration consequence management requirement to provide full flexibility for boards to determine which tool to use as most appropriate in the circumstances. 7. (i) Amend wording for malus criteria to improve clarity on the circumstances under which malus should apply (paragraph 44); and (ii) Align the criteria for clawback application to that of malus.
5	The layering of multiple and inconsistent regulatory requirements in Australia and overseas will increase complexity and drive up the cost of compliance	8. Reduce complexity caused by the interaction between the BEAR and CPS 511 by: (i) amending the definition of 'special role category' in CPS 511 to include Accountable Persons identified under the BEAR legislation; and (ii) removing deferred remuneration obligations Division 4 under the BEAR legislation and introducing proposed deferral requirements into CPS 511 as per Suggestions 2 and 3. 9. Amend the definition of 'highly-paid material risk taker' to simplify the identification of impacted individuals (paragraph 16 (c)). 10. Raise the de minimis threshold for actual variable remuneration outcomes, below which no deferral applies (paragraph 55).

2 Areas of challenge for QBE

Key areas of challenge

While we acknowledge that further clarity on CPS 511 will be provided by APRA via a Prudential Practice Guide (PPG) in 2020, our analysis has identified five key areas of challenge for QBE for which we have provided suggested alternatives. These include:

1. Entities such as QBE, with a large proportion of its operations outside of Australia, will be at a significant competitive disadvantage in attracting and retaining talent in local markets;
2. CPS 511 does not apply the prescriptive remuneration requirements proportionately to allow for the material differences in the risk profiles of general insurers compared to banks;
3. There are practical implications of the proposed limit on financial measures in variable remuneration arrangements which will result in conflicts with APRA's primary objectives;
4. There are practical implications of the proposed clawback provisions which will limit its application; and
5. The layering of multiple and inconsistent regulatory requirements in Australia and overseas will increase complexity and drive up the cost of compliance.

A description of the key areas of challenge and summary of suggested alternatives follows in this Section 2. A more detailed description of suggested alternatives is provided in Section 3.



Key challenge 1

Entities such as QBE, with a large proportion of its operations outside of Australia, will be at a significant competitive disadvantage in attracting and retaining talent in local markets

The application of the standard to APRA-regulated entities is set out in paragraphs 2 to 9 of CPS 511. Our interpretation is that CPS 511 must be applied to QBE Insurance Group Limited as the non-operating holding company and throughout the Group, including entities that are not APRA-regulated. In this regard, the scope of CPS 511 aligns with the current standard governing remuneration, CPS 510 Governance. However, the scope of persons covered by CPS 511 has been expanded in two ways:

1. The new definition of Material Risk-takers (MRTs) will capture a broader population as a result of removing the test of variable remuneration significance and going beyond those who can materially impact the financial soundness, to the overall 'long-term soundness' (paragraph 16(f)); and
2. CPS 511 regulates remuneration arrangements for all employees and some service providers, going beyond the persons in specific categories covered by CPS 510. For QBE, CPS 511 will apply to many more employees than CPS 510 – this includes 60 to 70 employees in the special role categories, of which more than 50% are located outside of Australia.

This is particularly concerning to QBE.

The prescribed deferral periods in CPS 511 of four to seven years for the CEO and four to six years for the other senior managers and highly paid MRTs are significantly more onerous than in any other jurisdiction regulating insurance firms in which QBE operates. To provide context to this issue for QBE, the next most significant deferral requirements are observed in the UK where category 1 and 2 Insurance firms (there are five categories of insurance firms based on risk profile), are required to defer 40% of variable pay over a three-year vesting period.¹

The differences between CPS 511 and remuneration standards in insurance and banking in key markets for QBE is provided in the Appendix.

While QBE is domiciled in Australia, many of our competitors are based (and subject to regulation) overseas. We compete for talent in a global labour market and believe that global entities, such as QBE, will be at a significant competitive disadvantage both in Australia and overseas through the application of CPS 511 in its current form.

We are also concerned that the deferral arrangements will make it very difficult to attract senior executives in 'industry-agnostic' roles (such as functional roles or technology, digital and data science roles). These individuals may more easily move to industries or jurisdictions that are not subject to deferred remuneration requirements. In our view, these requirements will make Australia less attractive as a destination for senior global talent within Financial Services. The implication is that we may see a gradual talent drain from Financial Services as senior executives opt for other industries and we will struggle to attract individuals into roles which can truly drive and improve the experience of the customer.

In response to these competition issues, we expect Financial Services companies will seek to create a more compelling proposition for attracting talented individuals through higher remuneration quantum and/or changes to pay mix that places greater emphasis on fixed remuneration. Both strategies increase the cost base of the company and so would either need to be passed onto customers or weaken shareholder returns.

At its extreme, some companies may choose to re-domicile to a jurisdiction that allows them to compete for talent on a more even playing field.

This has the potential to weaken the Financial Services industry, counter to APRA's primary objective of promoting financial system stability.



Summary of alternatives for consideration:

1. Allow a proportionate approach to be adopted for persons subject to 'equally as effective' remuneration regulation

Summary of aspects requiring further guidance:

- Identification of Material Risk Takers (MRTs)

¹ PRA Supervisory Statement on Solvency II <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2018/ss1016update>.

2 Areas of challenge for QBE continued



Key challenge 2

CPS 511 does not apply the prescriptive remuneration requirements proportionately to allow for the material differences in the risk profiles of general insurers compared to banks

Regulators around the world have differentiated between the banking, insurance and asset management industries when implementing the FSB Principles for Sound Compensation Practices and their Implementation Standards (FSB P&S). In its most recent Progress Report¹, the FSB observed that banks that are 'significant' for the purposes of the FSB P&S have been the main area of focus of supervisory authorities globally.

Local supervisors who have determined general insurers to be 'significant' for the purposes of implementing the FSB P&S, have adopted less prescriptive standards for those insurers than for banks. Further, their regulatory and supervisory regimes do not have the same intensity as for banks².

In Australia, APRA has also taken a different approach to supervision across the banking and insurance industries.

In our view, the approach taken in other jurisdictions to regulate 'significant' insurers and asset managers differently to 'significant' banks is warranted. While all these firms are considered to be 'significant' (i.e. large and systemically important), their objectives, business models and risk profiles differ.

When we consider the requirements to defer variable remuneration, we observed significant differences across industries, which is likely explained by the differing risk profiles for both financial and non-financial risk. Within general insurance, both the UK and Hong Kong supervisors have set expectations for three-year deferral periods, whereas other supervisors have not prescribed deferral periods for 'significant' general insurance institutions. In contrast, deferral requirements in banking were much more onerous and typically require deferral periods of between three and five years via regulation or legislation. The longest deferral period requirements are observed for significant UK banks, and require deferral periods of up to seven years.

Furthermore, the prescriptive deferral requirements were observed to apply to the most senior employees only.

In general insurance, the time period for which a risk or conduct issue may present varies to some extent by the mix of short and long-tail business across the book of business. For example, at QBE the weighted average duration of our liabilities as at 31 December 2018 was 3.3 years – this would be significantly higher in banking and life insurance. It is difficult to foresee any risk or conduct issue emerging within general insurance over a period longer than five years.

In our opinion, the proposed deferral portions and periods in CPS 511 should be proportionate for general insurers. We believe a more nuanced approach is warranted considering not only the significance of firms by size, but also the risk profile of the industries and persons for which the prescriptive deferral requirements are applied.



Summary of alternatives for consideration:

2. Apply a tiered approach to the deferral portion, recognising the differing size and complexities of SFIs in a similar way to the Banking Executive Accountability Regime (BEAR)
3. Tailor the deferral periods applying to SFIs, recognising the differences in risk profiles across the financial services sectors

Summary of aspects requiring further guidance:

- Define the term 'inception' as it relates to the variable remuneration component trigger for the start of the deferral period (paragraphs 53 and 54)

1 FSB, Implementing the FSB Principles for Sound Compensation Practices and their Implementation Standards: Sixth progress report, 17 June 2019.

2 FSB, Implementing the FSB Principles for Sound Compensation Practices and their Implementation Standards: Fifth progress report, 4 July 2017.



Key challenge 3

There are practical implications of the proposed limit on financial measures in variable remuneration arrangements which will result in conflicts with APRA's primary objectives

As shown by the Royal Commission and recent reviews by APRA, executive remuneration outcomes have had a tendency to over-emphasise financial performance to the benefit of the shareholder, rather than a more balanced focus which also considers outcomes for customers and communities. These findings on executive pay have focused on the long-term variable remuneration. By contrast, the use of non-financial performance measures has been found to be well-embedded in executive short-term variable remuneration (APRA, Royal Commission).

QBE supports APRA's key principle for remuneration design to achieve a balance of outcomes relating to effective risk management, sustainable performance and long-term soundness. However, we believe that APRA's proposal to limit the weight on financial performance measures for any variable remuneration arrangement (paragraph 38) goes beyond both APRA's intent and the Royal Commission recommendation. We consider that the prescribed limit should be applied to long-term variable remuneration only, and not all forms of variable remuneration.

We acknowledge that QBE and others in the industry need to continue to work with shareholders and their advisers to demonstrate how non-financial performance measures are an integral measure of organisational and executive performance. This includes how selected measures in long-term incentive arrangements can impact future financial and share price performance.

However, we are concerned with the practical implications of the proposed limit on financial measures for any variable remuneration arrangement. This is for several reasons.

Firstly, the limit unintentionally forces a simple scorecard approach to performance measurement for all variable remuneration plans by prescribing a specific weighting percentage on the financial measures. This fails to recognise the large variance in incentive models across the industry and precludes alternative designs, such as the use of a modifier to adjust financial outcomes for non-financial performance (for example risk, reputation, customer and culture). Such alternative designs may better align to APRA's key principles.

Secondly, as recent regulatory reviews have found, there is a low degree of maturity in the setting and calibrating of non-financial risk performance measures. This is supported by the ASIC Corporate Governance Task Force's recent report, which states that, *"In general, we also observed that companies' risk appetite and metrics were less mature for non-financial risks than for financial risks, where metrics were more granular and comprehensive"*¹. Employees will likely focus on measures that are considered 'easily quantifiable' and 'controllable', (i.e. financial measures), and in extreme cases ignore those with less clear targets and subject to greater discretion. This diminishes the effectiveness of balanced scorecard approaches for long-term performance measures.

Thirdly, we have concerns regarding the exclusion of risk-adjusted financial measures in the calculation of the financial measures weighting (and in turn the 50% weighting cap). This may result in situations where, instead of introducing additional non-financial measures, companies will simply shift to using risk-adjusted measures as 'non-financial' measures for the purpose of complying with the limit. This does not, in our view, meet APRA's intention to "promote a broader suite of measures of performance, including non-financial and risk-based measures."²



Summary of alternatives for consideration:

4. Limit the use of financial measures in long-term variable remuneration arrangements by introducing a prescriptive requirement to modify the long-term variable remuneration outcomes based on non-financial factors (rather than a cap on weighting)

Summary of aspects requiring further guidance:

- Provide greater clarity of what APRA considers to be a financial performance measure (paragraph 38)

1 ASIC, Information Report: Director and Officer oversight of non-financial risks, October 2019.
2 APRA, Discussion Paper: Strengthening prudential requirements for remuneration, 23 July 2019.

2 Areas of challenge for QBE continued



Key challenge 4

There are practical implications of the proposed clawback provisions which will limit the effectiveness of its application

QBE is supportive of the inclusion of a range of remuneration adjustment tools, including clawback, to promote effective risk management and sustainable performance. As clawback provides for the recouping of cash amounts already paid or equity awards already vested, QBE views this adjustment tool to only be appropriate in the most severe or extreme circumstances and where other tools to adjust remuneration have been exhausted.

CPS 511 provides for a number of other mechanisms to adjust remuneration as a form of consequence including:

- appropriate tools to adjust variable remuneration when and if required (paragraph 37a);
- the need for payout and vesting schedules to be commensurate with the possible range of risk and performance outcomes (paragraph 37c);
- the determination of variable remuneration outcomes that are commensurate with performance and risk outcomes (paragraph 41a);
- adjustments of variable remuneration outcomes, to zero if appropriate, through tools that are triggered in specified circumstances. These tools include but are not limited to in-period adjustments, malus, clawback and overriding discretion and judgement (paragraph 41b);
- specific criteria for the application of malus (paragraph 44);
- for senior managers and highly paid MRTs of SFIs, extended deferral requirements whereby 40–60% of variable remuneration must be deferred for at least six to seven years (paragraphs 53–54); and
- APRA's stated intention to intensify their supervision of remuneration practices (CPS 511 Discussion Paper, page 8).

In our view, the range of adjustment mechanisms or tools provided in the CPS 511 are substantive and complex. QBE agrees with APRA that *"while clawback provisions are one mitigant to risks and poor outcomes that emerge after remuneration amounts have been paid out, in APRA's view there are sufficient uncertainties about the practical use of clawback, such that it is yet to be proven as a reliable means to adjust remuneration outcomes on a routine basis."*¹

Therefore, it is important that the benefits of requiring variable remuneration to be subjected to clawback is balanced with the practical challenges of implementation. We believe there are a number of practical implications of the proposed clawback provisions which will limit the effectiveness of its application.

Firstly, the extended deferral periods provide a sufficiently long timeframe by which to identify and address risk and conduct issues, sustainability of performance or long-term soundness. It is difficult to foresee any matter occurring within the general insurance industry that would not emerge within the maximum deferral period. By deferring the variable remuneration over this extended period, there is already much greater access to other forms of remuneration adjustments (such as malus) therefore negating the need for a clawback period that extends beyond the maximum deferral period. The proposed clawback period in CPS 511, being up to 11 years from the inception of the award for a CEO, goes well beyond typical statutes of limitations (e.g. for tortious claims) or generally accepted industry liability periods (e.g. D&O liability run-off periods), and is materially more onerous than any other remuneration standard for insurers globally.

Secondly, the amount of variable remuneration which is available for clawback may not be proportionate to the failing or issue. This is because the deferred variable remuneration may vest in a staggered way (i.e. 'no faster than on a pro-rata basis' paragraphs 53–54) and so the amount of remuneration which may be clawed back at any particular time is also staggered and much less than the initial deferred amount.

¹ APRA Discussion Paper: Strengthening prudential requirements for remuneration (page 35).

Thirdly, while having a prescribed set of criteria for the application of adjustments, malus and clawback (in paragraphs 41(b), 44 and 58) is helpful and will ensure alignment across APRA-regulated entities, the wording of the criteria is broad and ambiguous. This will result in ongoing uncertainty for both participants and Boards. For example, 'a significant downturn in financial performance' (paragraph 44a), may be caused by factors beyond the control of management (e.g. macro-economic events or natural catastrophes such as earthquakes) and may not compromise the entity's overall soundness where its balance sheet remains strong.

Fourthly, the use of separate criteria for the application of malus and clawback in CPS 511 means that in certain cases, the Board must use clawback as the risk adjustment mechanism instead of potentially more suitable alternatives such as malus or in-period adjustments.

This will limit the flexibility for entities who wish to use an overarching consequence management policy to determine the most appropriate adjustment mechanisms when such events occur. Although it is legally possible to apply clawback in Australia, this will likely involve significant legal and administrative cost as evident from historic clawback cases globally. It's worth noting that in those cases, where the executives still held unvested variable remuneration, clawback was applied in addition to in-period adjustments and/or malus – not instead of.

In our view, the Board should retain the flexibility to utilise the adjustment mechanisms it considers in the circumstances to be the most appropriate. Notably in the UK, malus and clawback criteria specified in the regulatory text (the PRA Rulebook¹) overlaps, allowing for malus and/or clawback to be applied where such event occurs.



Summary of alternatives for consideration:

5. Align the clawback period to be the same length as the maximum deferral period whilst retaining the extended clawback period where an investigation is in progress
6. Condense malus and clawback criteria into one remuneration consequence management requirement to provide full flexibility for boards to determine which tool to use as most appropriate in the circumstances
7. (i) Amend wording for malus criteria to improve clarity on the circumstances under which malus should apply (paragraph 44); and
(ii) Align the criteria for clawback application to that of malus.

1 PRA Rulebook, paragraphs 15.22 and 15.23 <http://www.prarulebook.co.uk/rulebook/Content/Part/292166/20-09-2019>.

2 Areas of challenge for QBE continued



Key challenge 5

The layering of multiple and inconsistent regulatory requirements in Australia and overseas will increase complexity and drive up the cost of compliance

The BEAR became effective in Australia on 1 July 2018 for ADIs. The BEAR will be extended to apply to insurers, with legislation to be introduced into Parliament by the end of 2020.

Under the BEAR and specific to remuneration, ADIs are required to defer a prescribed minimum proportion of an Accountable Person's variable remuneration for a minimum of four years and an ADI's remuneration policy must require a reduction in an Accountable Person's variable remuneration proportionate to any failure to comply with accountability obligations.

While it is not yet clear what the implementation and transitional arrangements of the BEAR will be for insurers, there is likely to be a material overlap with CPS 511 on deferral and malus requirements. In the CPS 511 Discussion paper, APRA also recognises that the interaction of CPS 511 and the BEAR could cause some difficulty (page 36).

This layering of regulation extends beyond the BEAR and CPS 511 to additional remuneration standards in other countries in which QBE operates. For example, for some employees, we will likely need to comply with four different remuneration standards – each with their own nuances.

QBE recognises that the remuneration standards of local regulators is important as it is set in the context of that local market. However, where regulation overlaps unnecessarily, it risks creating compliance costs for no additional benefit. There is an opportunity to significantly simplify the compliance effort by harmonising the remuneration aspects of the respective regulation. This includes our Suggestion 1 to allow a proportionate approach to be adopted for persons subject to 'equally as effective' remuneration regulation.

Additionally, we have identified certain provisions of CPS 511 that, as drafted, create practical challenges for companies to implement.

Firstly, a 'highly-paid material risk taker' is captured based on their total potential remuneration (i.e. fixed remuneration plus maximum potential variable remuneration). The inclusion of 'total fixed remuneration' to this definition adds considerable and unnecessary complexity to the identification of this group.

The complexity comes in how benefits, allowances and superannuation are valued. In many cases, the value may not be known until after the conclusion of the financial year, meaning that some individuals will not know for certain that they will be subject to the deferral and clawback requirements of CPS 511 until after the performance year has been completed. Additionally, certain benefits may require an actuarial calculation such as the value of defined benefit superannuation arrangements. In other cases, the threshold of A\$1 million may or may not be exceeded depending on foreign exchange rates.

Secondly, the A\$50,000 variable remuneration de minimis threshold is well-below the level applied in many companies' incentive plans and will result in an immaterial deferral amount. This raises questions as to whether the benefit of such requirement (i.e. to promote an individual's focus on long-term performance and providing a mechanism for consequence management) really outweighs the cost for the company to administer the policy.

These provisions, however, could be easily simplified without losing any intent of the provision.



Summary of alternatives for consideration:

8. Reduce complexity caused by the interaction between the BEAR and CPS 511 by:
 - (i) amending the definition of 'special role category' in CPS 511 to include Accountable Persons identified under the BEAR legislation; and
 - (ii) removing the deferred remuneration obligations Division 4 under the BEAR legislation and introducing proposed deferral requirements into CPS 511 as per Suggestions 2 and 3.
9. Amend the definition of 'high-paid material risk taker' to simplify the identification of impacted individuals (paragraph 16 (c))
10. Raise the de minimis threshold for actual variable remuneration outcomes, below which no deferral applies (paragraph 55)

3 Suggested alternative approaches

In this section we have set out suggested alternative approaches to address the key challenges described in Section 2.

In outlining an alternative approach, we have sought to ensure it not only addresses the challenges identified but meets key criteria, including:

- Alignment to APRA's objectives of improving financial safety and promoting financial system stability, and the Royal Commission remuneration recommendations;
- Promoting a customer-centric culture; and
- Minimising impact on efficiency and competition in the market.



Key challenge 1

Entities such as QBE, with a large proportion of its operations outside of Australia, will be at a significant competitive disadvantage in attracting and retaining talent in local markets

Relevant requirements in CPS 511:

- Application of the standard to APRA-regulated entities (paragraph 2-9); and
- Deferral and clawback for significant financial institutions (paragraph 53-59).

Suggestion 1 - Allow a proportionate approach to be adopted for persons subject to 'equally as effective' remuneration regulation

Proposed amendment to CPS 511

Introduce an additional requirement (as a standalone paragraph) under the Remuneration Framework section:

Where application of the standard extends to those employed by, or a contractor of an overseas related body corporate or connected entity of the APRA-regulated entity, the entity may consider a proportionate application of the requirements under this Prudential Standard to the extent that such body corporate or connected entity is subject to regulatory requirements on remuneration that are equally as effective as those applicable under this Prudential Standard.

Additional guidance to be included in the Prudential Practice Guide

What does a proportionate approach to applying CPS 511 standard mean?

Where a jurisdiction is identified as having satisfactory or equally as effective remuneration regulation:

- MRTs would still be identified for CPS 511 purposes
- For the MRTs outside of Australia
 - The APRA-regulated entity must ensure that remuneration outcomes are commensurate with performance and risk outcomes of the Group (paragraph 41(a)); and
 - Reward structures and governance procedures may otherwise align with local regulations.
- An assessment of the effectiveness of the remuneration arrangements in the relevant jurisdiction would be included in the triennial review

How is 'satisfactory' or 'equally effective' determined?

- The APRA-regulated entity must undertake and document an assessment of the local regulations with consideration given to:
 - A comparison of the objectives of those regulatory requirements (and not a required equivalence in terms of the specific requirements);
 - A comparison of the supervisory approach (i.e. alignment of the local regulator's approach to supervision to APRA's approach); and
 - An assessment of the maturity of local market practice.

Alternatively, APRA in its Guidance can provide a list of jurisdictions it considers satisfactory/equally effective.

3 Suggested alternative approaches continued

How does the proposed approach address the issue highlighted?

This approach enables APRA-regulated entities that are subject to 'equally as effective' remuneration requirements to be deemed to have met the APRA CPS 511 requirements for the relevant populations. This removes the duplication of applying Australian regulation in overseas jurisdictions, meaning that usual competitive pressures apply in 'equally as effective' jurisdictions.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">• This approach ensures that the remuneration policy applicable to overseas MRTs is designed to meet the same or similar objectives as those set out by APRA;• Risk adjustments are considered at both a local jurisdiction and a Group level;• Reduces complexity of complying with multiple layers of remuneration regulations;• Reduces the cost of compliance; and• Builds on APRA's supervision of remuneration practices.
Promotes a customer-centric culture	<ul style="list-style-type: none">• Alignment with customer outcomes are considered at both a local jurisdiction and Group level.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none">• Improved competitiveness in local markets;• Applicable across industry; and• Reduced cost of compliance improves efficiency and productivity.



Key challenge 2

CPS 511 does not apply the prescriptive remuneration requirements proportionately to allow for the material differences in the risk profiles of general insurers compared to banks

Relevant requirements in CPS 511:

- Deferral for SFIs (paragraphs 53, 54).

Relevant requirements in APRA's supervision of CPS 511:

- Approach to Identifying SFIs (CPS 511 Discussion Paper table 4).

Suggestion 2 - Apply a tiered approach to the deferral portion, recognising the differing size and complexities of SFIs in a similar way to the BEAR

Proposed amendment to CPS 511

CATEGORY	EXAMPLE ENTITIES	ROLE	DEFERRAL AMOUNT
Level 1 SFIs	Large ADIs ¹	CEO	60% of variable rem
		Other Accountable Persons, Senior Managers and Highly Paid MRTs	40% of variable rem
Level 2 SFIs	Medium ADIs ¹ Significant Insurers Significant RSE Licensees	Accountable Persons, Senior Managers and Highly Paid MRTs	40% of variable rem
All other APRA-regulated entities	Small ADIs ¹ Other Insurers Other RSE Licensees	Accountable Persons	40% of variable rem
		All other persons	Principle-based only (per para 37(c))

¹ As defined under the BEAR.

How does the proposed approach address the issue highlighted?

In a similar approach to the BEAR, this suggestion takes a proportionate approach to applying remuneration deferral requirements with consideration of the size and therefore complexity of the APRA-regulated entity.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none"> • Maintain that higher standards must be met for key roles and certain large, complex entities; and • More closely aligns remuneration with risk taking, particularly at the most significant entities.
Promotes a customer-centric culture	<ul style="list-style-type: none"> • More closely aligns remuneration with the period of time over which customer outcomes may be measured.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none"> • Reduces cost of compliance by aligning with overlapping requirements (i.e. the BEAR).

3 Suggested alternative approaches continued

Suggestion 3 - Tailor the deferral periods applying to SFIs, recognising the differences in risk profiles across the financial services sectors

Proposed amendment to CPS 511

CATEGORY	EXAMPLE ENTITIES	ROLES	DEFERRAL PERIOD ¹
Level 1 SFIs	Large ADIs ²	CEO	Seven years
		Other Accountable Persons, Senior Managers and Highly Paid MRTs	Six years
Level 2 SFIs	Medium ADIs ² Significant Insurers Significant RSE Licensees	Accountable Persons, Senior Managers and Highly Paid MRTs	Five years
All other APRA-regulated entities	Small ADIs ² Other Insurers Other RSE Licensees	Accountable Persons	Four years
		All other persons	Principle-based only (per para 37(c))

1 Vesting may occur after four years from the time of inception and no faster than on a pro-rata basis.
2 As defined under the BEAR.

How does the proposed approach address the issue highlighted?

In a similar approach to the BEAR, this suggestion takes a proportionate approach to applying remuneration deferral requirements with consideration of the size and complexity of the APRA-regulated entity.

The five-year deferral periods suggested for Medium ADIs, Significant Insurers and Significant RSE Licensees extends the deferral periods beyond prescribed levels under the BEAR, while recognising the differences in risk profile for the most significant firms.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Align to APRA objectives	<ul style="list-style-type: none">Maintain that higher standards must be met for key roles and certain large complex entities; andMore closely aligns remuneration with risk-taking, particularly at the most significant entities.
Promotes a customer-centric culture	<ul style="list-style-type: none">More closely aligns remuneration with the period of time over which customer outcomes may be measured.
Minimise impact on efficiency and competition in the market	<ul style="list-style-type: none">Not expected to disadvantage smaller entities.



Key challenge 3

There are practical implications of the proposed limit on financial measures in variable remuneration arrangements which will result in conflicts with APRA's primary objectives

Relevant requirements in CPS 511:

- Remuneration design (paragraph 38).

Suggestion 4 - Limit the use of financial measures in long-term variable remuneration arrangements by introducing a prescriptive requirement to modify the long-term variable remuneration outcomes based on non-financial factors (rather than a cap on weighting)

Proposed amendment to CPS 511

Alternative wording for paragraph 38:

For any long-term variable remuneration arrangement (i.e. variable remuneration element that is linked to the long-term performance of the entity) of an APRA-regulated entity, non-financial performance and risk measures should have an overriding impact on the overall performance measures used to determine the size of the incentive pool and allocate the remuneration outcome, such as a modifier to a formulaic outcome.

Non-financial measures should include risk management and conduct.

APRA practice guide (expected in 2020)

Introduce an additional qualitative disclosure requirement:

Companies must include, as part of their remuneration disclosure, a description of the ways in which non-financial performance and risk measures are taken into account in the remuneration process. Disclosure must include:

- an overview of the non-financial performance and risk measures an APRA-regulated entity takes into account in the long-term variable remuneration arrangements;
- an overview of the nature and type of measures used to take account of these non-financial performance and risk measures; and
- a discussion on the ways in which these measures affect remuneration.

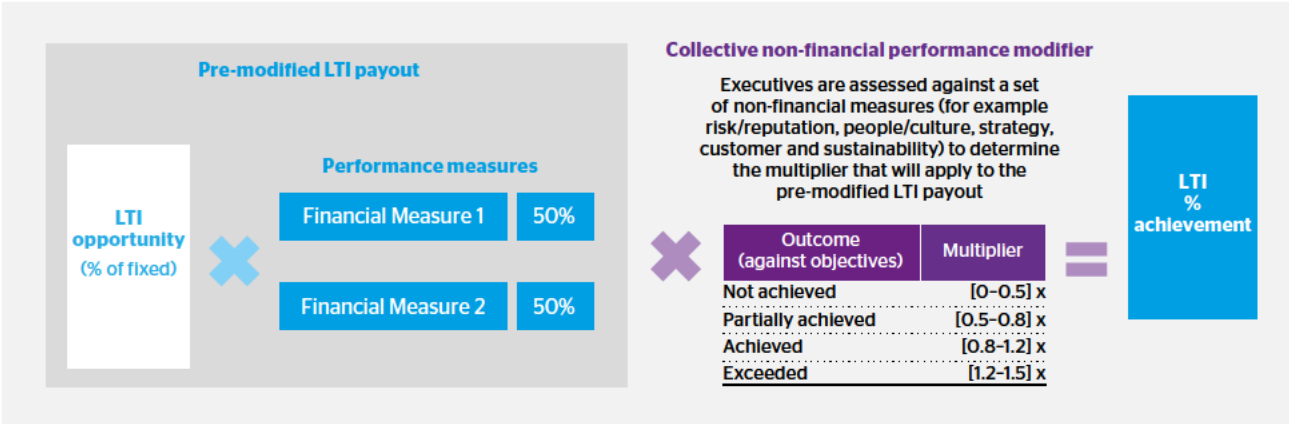
3 Suggested alternative approaches continued

How does the proposed approach address the issue highlighted?

This approach places a limit on financial performance measures in a manner which provides for non-financial factors to override the outcome, satisfying the Royal Commission remuneration recommendation 5.3 to “set limits on the use of financial metrics in connection with long-term variable remuneration.”

The override may be achieved, for example, by modifying the incentive pool and/or outcome – which may be upwards or downwards (including to zero) – with consideration of non-financial performance. This approach does not preclude entities from incorporating non-financial measures as a balanced scorecard of discrete weighted measures. An example of how the override may work in practice is provided in **Figure 1** below.

Figure 1: Illustrative example of an LTI modifier in practice



In our opinion, a structured override mechanism, such as a modifier, provides for a simpler plan design than a scorecard approach. Where the impact of the modifier is certain and defined (such as defining the minimum and maximum impact it may have), it may have a greater motivational value for participants, as compared to the approach stated under paragraph 38 of CPS 511.

There is a precedent for a more discretionary approach in Australia. Stephen Sedgwick’s recommendations on retail banking remuneration required a limit on the weight of financial measures where a scorecard is utilised. However, where a discretionary decision-making approach is used, banks should be able to “demonstrate credibly that performance against financial measures did not play a significant part in determining the variable remuneration amount”.¹

QBE believes that applying non-financial performance measures as an override strengthens the alignment of non-financial risk with incentive outcomes. This is because, the management of non-financial risks is ultimately demonstrated through financial outcomes and in the case of long-term incentive arrangements will already be incorporated to some extent in the financial performance measures prior to applying the non-financial modifier. While boards were criticised during the Royal Commission for being too lenient in applying discretionary adjustments to remuneration outcomes for non-financial performance (such as risk and reputational issues), the suggested modifier approach described above creates a level of transparency which in turn will drive board accountability with its stakeholders.

Finally, this alternative modifier approach removes the loop hole in the current drafting of paragraph 38 whereby entities may utilise only risk-adjusted financial metrics to meet the requirements. The override requires consideration of non-financial performance and risk, risk-adjusted financial measures are not a substitute for the override.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Align to APRA objectives	<ul style="list-style-type: none">By strengthening the impact of non-financial outcomes (including risk) through the modifier-mechanism; andAddresses RC recommendation 5.1 and 5.3.
Promotes a customer-centric culture	<ul style="list-style-type: none">Allow a more holistic assessment of customer outcome to be incorporated through Board’s assessment.
Minimise impact on efficiency and competition in the market	<ul style="list-style-type: none">Applicable across industry; andApplicable to any remuneration arrangements.

¹ Stephen Sedgwick AO, Retail Banking Remuneration Review Report, 19 April 2017.



Key challenge 4

There are practical implications of the proposed clawback provisions which will limit the effectiveness of its application

Relevant requirements in CPS 511: The differing trigger criteria set out for:

- Variable remuneration adjustments (paragraph 41(b));
- Malus (paragraph 44); and
- Clawback for Significant Financial Institutions (paragraph 57, 58).

Suggestion 5 - Align the clawback period to be the same length as the maximum deferral period whilst retaining the extended clawback period where an investigation is in progress

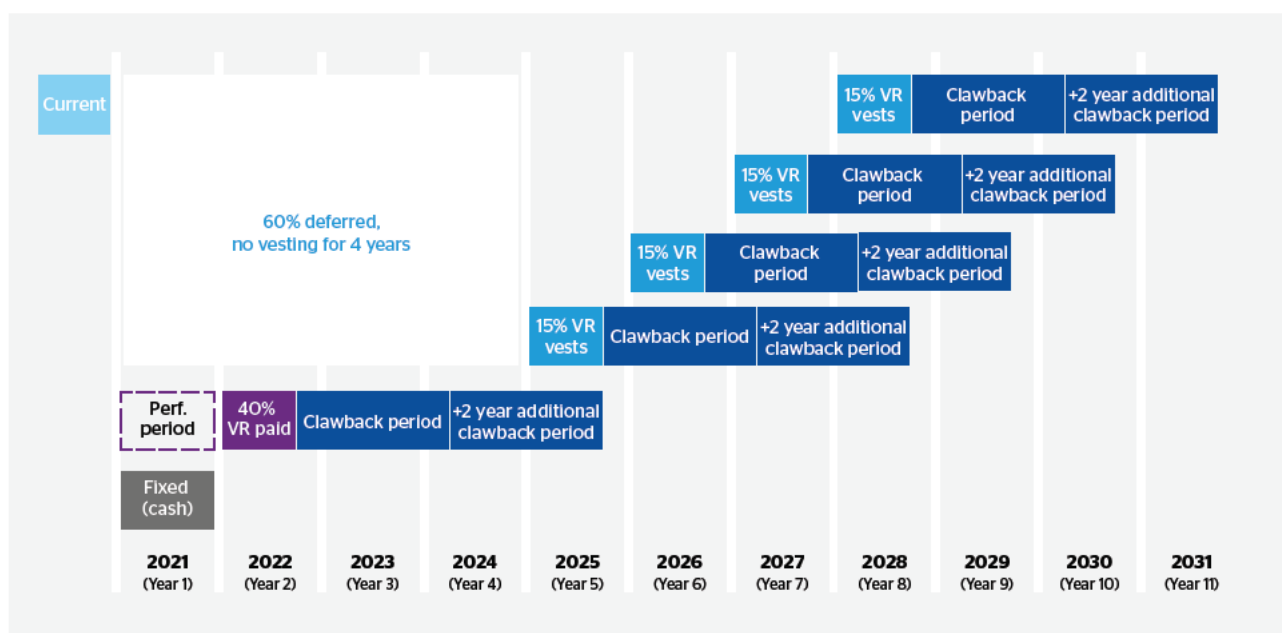
Proposed amendment to CPS 511

Alternative wording for paragraph 57

A **Level 2** SFI must subject the variable remuneration of a senior manager or highly-paid MRT to malus and clawback. Variable remuneration must be subject to clawback for a period of:

- five years from the date of inception of the variable remuneration; or
- In circumstances involving a person under investigation at the end of five years from the date of inception, seven years from the date of inception of the variable remuneration.

Figure 2: Illustration of **current** clawback requirement's interpretation (for a CEO of an SFI)



3 Suggested alternative approaches continued

Figure 3: Illustrative example of proposed clawback alternative (for a CEO of a banking SFI)

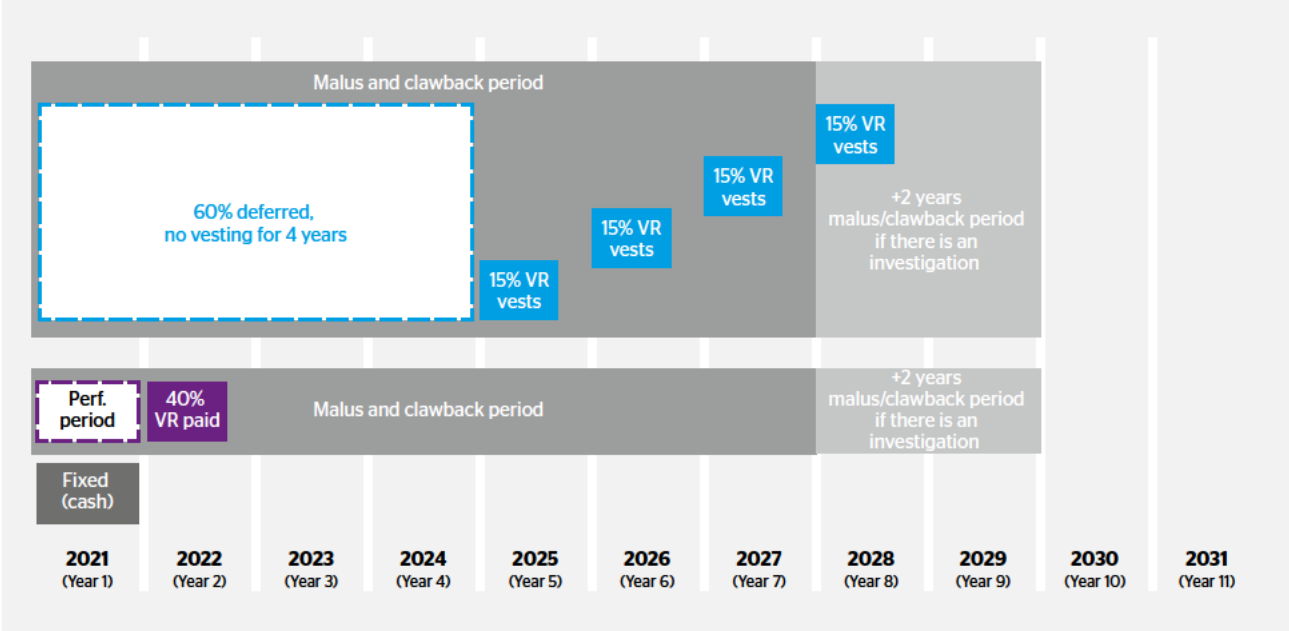
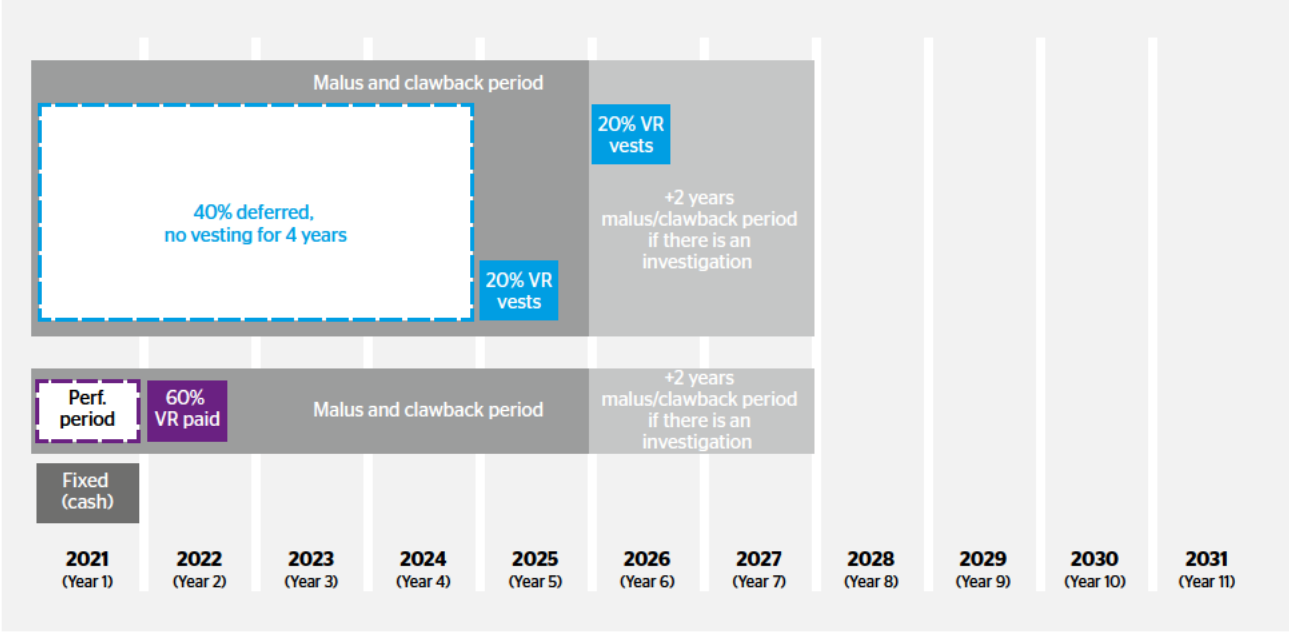


Figure 4: Illustrative example of proposed clawback alternative (for a CEO of a Level 2 SFI)



How does the proposed approach address the issue highlighted?

This simplified approach recognises that issues will likely have arisen during the maximum deferral period and have been addressed with adjustments occurring via in-period and/or malus adjustments. This approach also provides the means to claw back the whole amount of variable remuneration if and when an issue presents (rather than a portion only, due to the phasing of deferred remuneration after four years).

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">• Strengthens the entity's ability to adjust remuneration by introducing the ability to claw back the entire variable remuneration, if necessary, to appropriately reflect the risk and performance outcomes, and long-term soundness; and• Addresses RC remuneration recommendation 5.1.
Promotes a customer-centric culture	<ul style="list-style-type: none">• Strengthens the entity's ability to adjust remuneration by clawing back the entire variable remuneration, if necessary, to appropriately reflect customer outcomes.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none">• Applicable across industry; and• Simpler to administer by reducing the number of 'clawback periods'.

Suggestion 6 – Condense malus and clawback criteria into one remuneration consequence management requirement to provide full flexibility for boards to determine which tool to use as most appropriate in the circumstances

Proposed amendment to CPS 511

Introduce an additional requirement (as a standalone paragraph) under Special Role Categories section:

An APRA-regulated entity must have a formal consequence management framework that includes, at a minimum, the specific criteria for the application of a variable remuneration adjustment (in-period, malus or clawback), including:

- (a) a significant downturn in financial performance due to circumstances or events reasonably in the control of management and where the entity faces adversity that has a material impact on its long-term soundness;
- (b) material misstatement of financial results or other criteria on which the variable remuneration determination was based;
- (c) circumstances where there is direct evidence of an individual's misconduct, misconduct through the individual's action or failure to take action, or negligence resulting in losses;
- (d) a significant failure of financial or non-financial risk management;
- (e) a material or wilful breach of the entity's code of conduct or compliance obligations;
- (f) significant adverse outcomes for customers, beneficiaries or counterparties; and
- (g) breach of accountability obligations or fitness and propriety.

3 Suggested alternative approaches continued

How does the proposed approach address the issue highlighted?

This alternative ensures that all APRA-regulated entities have an appropriate policy and process in place to enable adjustments to be determined and applied for negative risk and customer outcomes. In the absence of a prescribed mechanism to apply remuneration consequence, companies and their Board will have the flexibility to determine the most appropriate risk adjustment mechanisms (i.e. in-period adjustment, malus or clawback). These will subsequently be used in the circumstances identified and in consideration of the commercial interests of the entity in order to ensure that the required amount is recovered from the individual.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">• Strengthens the current requirement on specific criteria to consider malus and clawback, putting emphasis on the implementation of the policy;• Ensures there is a process in place to determine the appropriate adjustments to reflect negative risk outcomes; and• Addresses RC recommendation 5.1.
Promotes a customer-centric culture	<ul style="list-style-type: none">• Ensures there is a process in place to determine the appropriate adjustments to reflect negative customer outcomes.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none">• Applicable across industry.

Suggestion 7(i) - Amend wording for the malus criteria to improve clarity on the circumstances under which malus should apply (paragraph 44)**Proposed amendment to CPS 511****Alternative wording for paragraph 44 (amendments noted in blue text)**

An APRA-regulated entity must set specific criteria for the **application of malus** for variable remuneration, including:

- (a) a significant downturn in financial performance **due to circumstances or events reasonably within the control of management and where the entity faces adversity that has a material impact on its long-term soundness;**
- (b) **material misstatement of financial results or other criteria on which the variable remuneration determination was based;**
- (c) **circumstances where there is direct** evidence of **an individual's** misconduct, **misconduct through the individual's action or failure to take action,** or negligence resulting in losses;
- (d) a significant failure of financial or non-financial risk management;
- (e) a **material or wilful breach of failure to meet** the entity's code of conduct **or compliance obligations including in relation to misconduct risk; and**
- (f) significant adverse outcomes for customers, beneficiaries or counterparties; **and**
(g) breach of accountability obligations or fitness and propriety.

How does the proposed approach address the issue highlighted?

The proposed amendments to the draft standard address the issue of the malus criteria being broad and ambiguous. The proposed amendments clarify that malus may only be applied where the criteria (or trigger event) is caused by an internal act or failure to act (e.g. misconduct, fraud or negligence), as opposed to one that is outside an individual's control (e.g. a macro-economic event).

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">Introduce additional criteria around accountability and fitness and propriety (currently under paragraph 58(d)) as such event should trigger the consideration of malus and/or clawback adjustment(s);Additional wording aims to clarify the circumstances under which malus applies – there is no change to the nature of the circumstances as set out in the draft standard;
Promotes a customer-centric culture	<ul style="list-style-type: none">Maintain that higher standards must be met for key roles and certain large, complex entities; andAddresses RC recommendation 5.1 and 5.3.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none">Ensure consistent interpretation of the standard across the industry by providing more clarity around each criteria.

3 Suggested alternative approaches continued

Suggestion 7(ii) - Align the criteria for clawback application to that of malus

Proposed amendment to CPS 511

Alternative wording for paragraph 58 (amendments noted in **blue text**)

Subject to conditions set in the remuneration policy, a significant financial institution must set specific criteria for the **application of clawback where appropriate in addition to in-period adjustment and malus** including:

- (a) responsibility for material financial losses;**
- (a) material misstatement of financial statements or other criteria on which the variable remuneration determination was based;
- (b) a material or wilful breach of the entity’s code of conduct or compliance obligations including in relation to misconduct risk; and**
- (c) **breach failure** of accountability **obligations** or fitness and propriety;
- (d) a significant failure of financial or non-financial risk management; and**
- (e) significant adverse outcomes for customers, beneficiaries or counterparties.**

How does the proposed approach address the issue highlighted?

The proposed amendments to CPS 511 address the issue of the clawback criteria being broad and ambiguous. The proposed amendments provide companies with the flexibility to determine the appropriate adjustment mechanism. To support this, we have aligned the criteria for malus and clawback without materially changing the nature of the circumstances where clawback must apply as set out in CPS 511.

Duplication across the clawback criteria (i.e. inclusive statements and separate points covering accountabilities and responsibilities) have been removed.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">Introduce two additional criteria where we believe they cover issues that materialise over a longer period of time;Additional wording aims to clarify the circumstances which clawback applies – there is no change to the nature of the circumstances as set out in the draft standard;
Promotes a customer-centric culture	<ul style="list-style-type: none">Maintain that higher standards must be met for key roles and certain large, complex entities; andAddresses RC recommendation 5.1 and 5.3.
Minimises impact on efficiency and competition in the market	<ul style="list-style-type: none">Provide flexibility for companies to determine the most appropriate remuneration adjustment mechanisms; andEnsure consistent interpretation of the standard across the industry by providing more clarity around each criteria.



Key challenge 5

The layering of multiple and inconsistent regulatory requirements in Australia and overseas will increase complexity and drive up the cost of compliance

Relevant requirements in CPS 511:

- Definitions including that of 'highly-paid material risk taker' (paragraph 16 (c)); and
- Deferral and clawback for significant financial institutions (paragraphs 53–59).

Suggestion 8 – Reduce complexity caused by the interaction between the BEAR and CPS 511 by:

- amending the definition of 'special role category' in CPS 511 to include Accountable Persons identified under the BEAR legislation; and
- removing deferred remuneration obligations Division 4 under the BEAR legislation and introducing proposed deferral requirements into CPS 511 as per Suggestions 2 and 3

8(i) Proposed amendment to CPS 511

Alternative wording (amendments noted in **blue text**)

New 16(a) accountable person – means an accountable person under the Banking Executive Accountability Regime

- 16(m) special role category – means a person in the category of **accountable person**, senior manager, material risk-taker (including highly-paid material risk-takers) and risk and financial control personnel.
- 48 The Board Remuneration Committee must assess and make recommendations to the Board annually on the remuneration arrangements and variable outcomes for persons in special role categories as follows:
 - (a) individually for **accountable persons**, senior managers and highly-paid material risk-takers.
- 54 A significant financial institution must for **an accountable person** or a senior manager other than its CEO and for a highly-paid material risk-taker, defer 40 per cent of their total variable remuneration for at least six years from the inception of the variable remuneration component. Vesting of this 40 per cent may only occur after four years from the time of inception and no faster than on a pro-rata basis.
- 56 A significant financial institution must subject the variable remuneration of **an accountable person or** a senior manager or a highly-paid material risk-taker to clawback. Variable remuneration must only be awarded if an amount corresponding to it can be recovered from the person if recovery is justified on the basis of the criteria specified in paragraph 58.

8(ii) Proposed amendment to the Banking Act 1959

Remove the Division 4—Deferred remuneration obligations section from Schedule 1—The Banking Executive Accountability Regime.

No deferred remuneration obligations included for equivalent BEAR regulation for insurance and registrable superannuation entity licensees.

Proposed amendment to CPS511

As per Suggestions 2 and 3.

3 Suggested alternative approaches continued

How does the proposed approach address the issue highlighted?

The complexity caused by the interaction between the BEAR and CPS 511 can be significantly reduced by adding Accountable Persons as defined under the BEAR to the ‘special role category’ and other relevant sections of CPS 511. The purpose of this suggestion is that Accountable Persons are then subject to one set of deferred remuneration requirements (CPS 511 rather than the BEAR).

Please also refer to Suggestions 2 and 3 for the proposed changes to the deferral provisions, including specific requirements for accountable persons.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Alignment to APRA objectives	<ul style="list-style-type: none">Maintain that higher standards must be met for key roles.
Promotes a customer-centric culture	
Minimises impact on efficiency and competition in the market	
	<ul style="list-style-type: none">Align the references across regulations; andReduces cost of compliance by aligning with overlapping requirements (i.e. the BEAR).

Suggestion 9 – Amend the definition of ‘high-paid material risk taker’ to simplify the identification of impacted individuals (paragraph 16 (c))

Proposed amendment to CPS 511 – alternative wording for paragraph 16 (c)

highly paid material risk taker – means a material risk-taker whose maximum potential variable remuneration is equal to or greater than A\$750,000 in a financial year.

How does the proposed approach address the issue highlighted?

This approach ensures highly-paid material risk takers roles are defined solely on the basis of their maximum potential variable remuneration. This group will be easily identified and communicated with at the beginning of the financial year, significantly reducing the time and cost of administration.

Assessment against defined criteria:

CRITERIA	ASSESSMENT
Align to APRA objectives	<ul style="list-style-type: none">Focus on those with a substantial amount of variable remuneration.
Promotes a customer-centric culture	<ul style="list-style-type: none">Policy change does not impact the customer.
Minimise impact on efficiency and competition in the market	<ul style="list-style-type: none">Applicable across industry;Focus the implementation effort on those with higher amount of pay at risk; andAgnostic to the different pay mix that exists across the financial services sectors and roles within the same organisation (e.g. front line versus control function).

Suggestion 10 – Raise the de minimis threshold for actual variable remuneration outcomes, below which no deferral applies (paragraph 55)

Proposed amendment to CPS 511

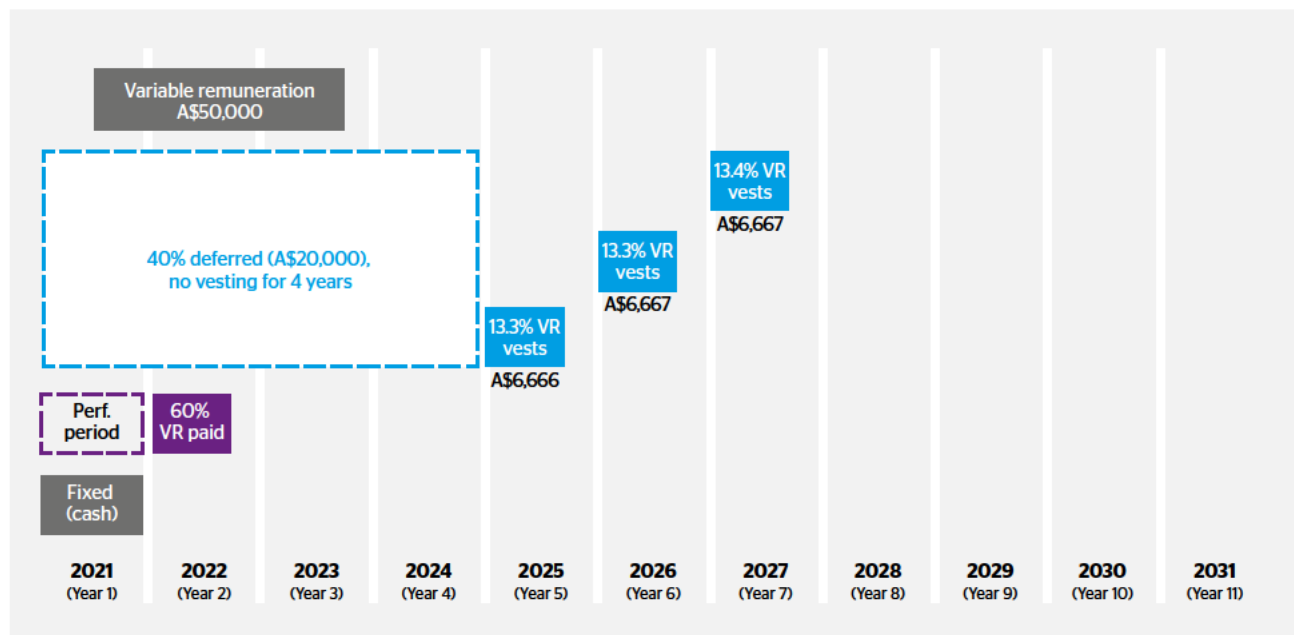
Alternative wording for paragraph 55

- Paragraphs 53 and 54 do not apply in respect of any person with actual variable remuneration of less than A\$250,000.

How does the proposed approach address the issue highlighted?

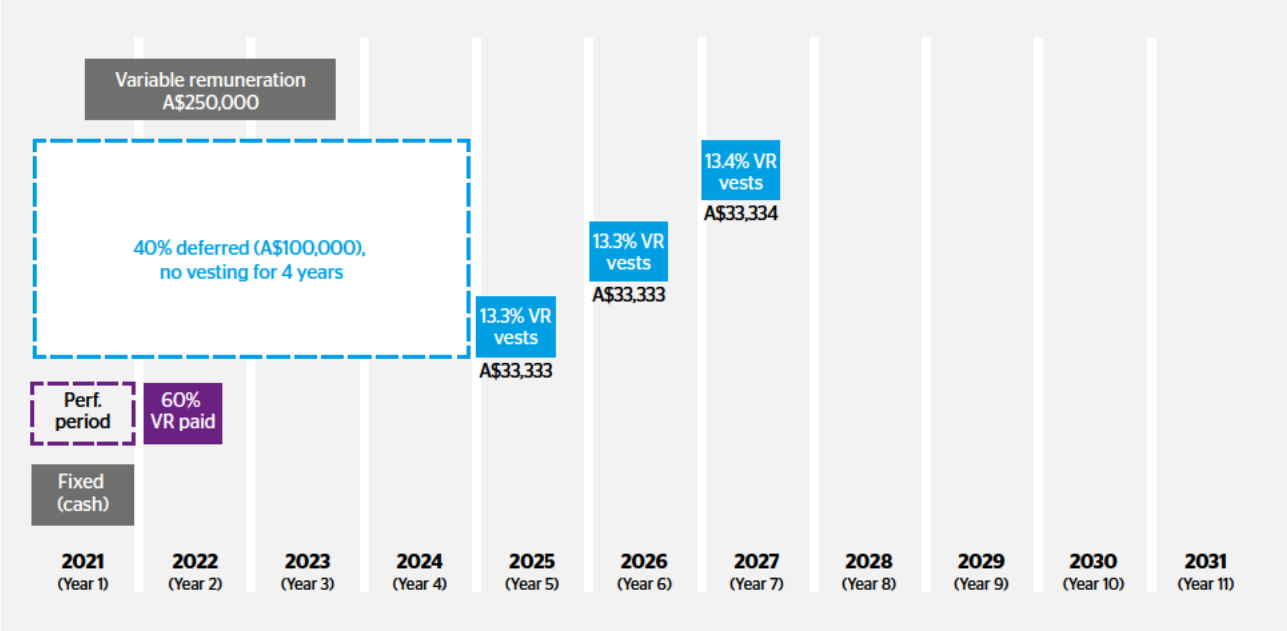
An increase in the de minimis threshold to A\$250,000 will mitigate the concern associated with deferring immaterial amounts over an extended period of time and also support the principle of proportionality.

Figure 5: Illustration of **current** variable remuneration de minimis threshold for non-CEO (A\$50,000)



3 Suggested alternative approaches continued

Figure 6: Illustration of **proposed** variable remuneration de minimis threshold for non-CEO (A\$250,000)



Assessment against defined criteria:

CRITERIA	ASSESSMENT
Align to APRA objectives	<ul style="list-style-type: none">The entire variable remuneration amount remains subject to adjustments for negative risk and customer outcomes (via in-period adjustments, malus and clawback).
Promotes a customer-centric culture	
Minimise impact on efficiency and competition in the market	<ul style="list-style-type: none">Applicable across industry; andFocus the implementation effort on those with higher amount of pay at risk.

4 Responses to APRA's consultation questions

In addition to the information provided above, we have responded to the direct consultation questions referenced in the APRA Discussion Paper (page 43).

	CONSULTATION QUESTION	QBE RESPONSE
Remuneration framework	Is triennially an appropriate frequency for conducting independent reviews of the remuneration framework?	We agree that a triennial review is appropriate.
	What areas of the proposed requirements most require further guidance?	<ul style="list-style-type: none"> How the commencement date of 1 July 2021 should be interpreted for entities with non-30 June balance dates (paragraph 9); The identification of 'material risk-taker' (paragraph 16 (f)); The calculation of total fixed remuneration as it applies to the identification of 'highly paid material risk-taker' (paragraph 16 (c)); Provide greater clarity in relation to the intent and application of the requirements to third parties (paragraph 19(d)(ii)). General insurers engage a broad range of service providers and the potential application of an insurer's remuneration framework to these third parties would present significant challenges. We suggest that the existing approach of CPS 510 Governance that provides for the risk management framework to address the structure of payments under service contracts remains appropriate to address risks associated with third party remuneration arrangements; Provide greater clarity of what APRA considers to be a financial performance measure (paragraph 38); Define the term 'inception' as it relates to the deferral of variable remuneration (paragraphs 53 and 54); and A number of items in the current drafting of malus/clawback are vague or broad brush and require further clarification (paragraphs 44, 45, 58 (a), 58 (b), 58 (d), 59).
Board oversight	Are the proposed duties of the Board appropriate?	APRA's intention to strengthen Board requirements with respect to accountability and oversight of remuneration is supported by QBE.
	Are the proposed duties of the Board Remuneration Committee appropriate?	<p>However, the significant increase in both the breadth and depth of remuneration arrangements that Boards are now expected to oversee will provide challenges for Boards seeking to optimise their time and focus on the most important strategic issues rather than taking on the role of management in presiding over the remuneration outcomes of dozens of individuals.</p> <p>The scope of individuals captured under paragraph 48(a), together with the fact that the definition of 'material risk-taker' is open to wide interpretation, means that Boards and Remuneration Committees approvals for individual remuneration arrangements and outcomes will multiply by 5 to 10 times. QBE does not consider this the most effective use of Boards' time.</p>

4 Responses to APRA's consultation questions continued

	CONSULTATION QUESTION	QBE RESPONSE
Remuneration design	APRA is proposing that financial performance measures make up at least 50 per cent of variable remuneration measurement and individual financial performance measures are limited to 25 per cent. Is this an appropriate limit, if not what other options should APRA consider to ensure non-financial outcomes are reflected in remuneration?	Refer Key Challenge 3 (page 7) and Suggestion 4 (page 15).
	What would be the impacts of the proposed deferral and vesting requirements for SFIs? For ADIs, what would be the impact of implementing these requirements in addition to the BEAR requirements?	Refer Key Challenge 2 (page 6) and Suggestions 2 and 3 (pages 13 and 14).
	Would the proposals impact the industry's capacity to attract skilled executives and staff?	Refer Key Challenge 1 (page 5) and Suggestion 1 (page 11).
Remuneration outcomes	What practical hurdles are there to the effective use of clawback provisions and how could these be overcome? Would requirements for longer vesting where clawback is not preferred address these hurdles?	Refer Key Challenge 4 (page 8) and Suggestions 5, 6 and 7 (page 17 to 22).
	What transitional provisions may be necessary for particular components of the new standard or for particular types of regulated entities?	
Transparency	What disclosures would encourage a market discipline in relation to remuneration practices?	<p>We consider the existing remuneration disclosure requirements of the Corporations Act as being overly prescriptive and inhibitive to providing information on remuneration practices that is clear and easily understood by all stakeholders.</p> <p>Providing further prescription to remuneration disclosures, specifically for APRA-regulated entities, will:</p> <ul style="list-style-type: none"> • add further complexity to remuneration disclosures making remuneration reports longer and more difficult for readers to digest; and • create different standards of remuneration disclosures for APRA-regulated entities vs non-regulated entities. <p>QBE therefore supports a principles-based approach to remuneration disclosures and would welcome any initiative that improves transparency and accountability.</p>

5 Appendix

Appendix - Summary of deferral requirements of CPS 511 vs insurance and banking in QBE's key markets

COUNTRY	APRA CPS 511	LOCAL REGULATION - INSURANCE	LOCAL REGULATION - BANKING
AUS	60% deferral (for CEO) for at least seven years, vesting commences after four years 40% deferrals (not CEO) for at least six years, vesting commences after four years		Banking - BEAR <ul style="list-style-type: none"> Applies only to Accountable Persons of ADIs; A proportionate approach to the percentage deferred is applied (40% or 60% of variable pay or a lesser amount if based on total remuneration) based on size of entity and role; and A proportion of an accountable person's variable remuneration must be deferred for a minimum period of four years.
GBR		Insurance - Solvency II¹: <ul style="list-style-type: none"> Applies to category 1 and 2 insurers only 40% deferral of variable pay, minimum three-year vesting period 	Banking - CRD IV²: <ul style="list-style-type: none"> Applies only to MRTs of Level 1 and Level 2 firms; At the individual level, the requirement does not apply to the MRTs who meet both of the following conditions: <ul style="list-style-type: none"> his/her variable remuneration is no more than 33% of total remuneration; and his/her total remuneration is no more than £500,000. At least 40% of variable remuneration deferred over a period which is not less than: <ul style="list-style-type: none"> for MRTs who perform a PRA senior management function, seven years, with no vesting to take place until three years after award and vesting no faster than on a pro-rata basis thereafter; for MRTs who do not perform a PRA senior management function, but whose professional activities meet certain qualitative criteria (as set out under Material Risk Takers regulations)³, five years, vesting no faster than on a pro-rata basis; for all other MRTs, three years, vesting no faster than on a pro-rata basis. At least 60% of variable remuneration deferred if variable remuneration is: <ul style="list-style-type: none"> £500,000 or more; or payable to a director.

1 Article 275 of the Commission Delegated Regulation (EU) 2015/35 ('the Solvency II Regulation') <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015R0035&from=EN>, PRA Supervisory Statement on Solvency II <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2018/ssi016update>.

2 PRA Rulebook for CRD IV firms <http://www.prarulebook.co.uk/rulebook/Content/Part/292166/18-09-2019>.

3 Qualitative criteria as set out under Article 3(1) to 3(9), 3(10) of the Commission Delegated Regulation (EU) No 604/2014 of 4 March 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution's risk profile <https://op.europa.eu/en/publication-detail/-/publication/4c81143c-d376-4d1d-a9dc-67a7e02a22c1/language-en>.

4 Responses to APRA's consultation questions continued

COUNTRY	APRA CPS 511	LOCAL REGULATION - INSURANCE	LOCAL REGULATION - BANKING
HKG		<p>Insurance – Guideline on the corporate governance of authorised insurers¹</p> <ul style="list-style-type: none"> Major part of any variable remuneration should be deferred for an appropriate period². The deferral period usually varies on the level of seniority, responsibility of the individual, and the nature and time horizon of the risks undertaken by the individual. Where variable remuneration comprises share-based elements (such as shares and share options), safeguards should be implemented: <ul style="list-style-type: none"> (i) Vesting restrictions – include vesting conditions and vesting schedules where shares should be vested over a period of at least three years after their award; (ii) Holding restrictions – share options should be exercisable for a minimum period of at least three years after their award; and (iii) Retention restrictions – an appropriate proportion of the shares should be retained after vesting or exercise. Retention portion and period set should take account of factors including seniority level, nature and time horizon of risks undertaken, and the relevant vesting period or holding period of shares. 	<p>Banking – HKMA Guideline on a sound remuneration system³</p> <p>– the Guideline (dated 12 Mar 2015) appears to be principles-based and does not include prescriptive requirements around deferral. However, the draft revised Guideline (currently in consultation) does provide some more prescriptive requirements – summary of requirements as set out below:</p> <ul style="list-style-type: none"> – For roles where the risks taken by them are harder to measure or will be realised over a longer timeframe, deferral will be appropriate. Generally, the proportion of variable remuneration made subject to deferment would be expected to increase in line with the seniority and responsibility of the employee in question. – The minimum vesting period should be appropriately aligned with the nature of the business, its risks, the activities undertaken by the employee in question and the timeframe during which the risks from these activities are likely to be realised. – The deferred remuneration should generally vest gradually over a period of years and no faster than on a pro rata basis, subject to fulfilment and validation of the pre-defined performance conditions. – (In consultation) For significant financial institutions, it is expected that 40 to 60% of the variable remuneration of senior executives, and other employees whose actions have a material impact on the risk exposures of the firm, should be subject to deferral. • (In consultation) In principle, the deferral period (at least for senior management and individual employees whose duties or activities involve the assumption of material risk or the taking on of material exposures on behalf of the bank (e.g. proprietary traders and dealers who are in a position to take on material exposures)) should not be less than three years.

1 Insurance Authority Guideline on the corporate governance of authorised insurers https://www.ia.org.hk/en/legislative_framework/files/GL10.pdf.

2 Reference was made to the Implementation Standards (No. 6 and 7) for the Financial Stability Board Principles for Sound Compensation Practices where a minimum deferral period of three years was suggested and the proportion of variable remuneration subject to deferral be set at 40%-60% for senior executives and other employees whose actions have a material impact on the risk exposure of the company; and over 60% for most senior management and most highly paid employees.

3 Hong Kong Monetary Authority (HKMA)'s Guideline on a Sound Remuneration System <https://www.hkma.gov.hk/eng/regulatory-resources/regulatory-guides/supervisory-policy-manual/>.

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USA		<p>No specific deferral provisions in the regulations¹, however the guidance notes state that deferral is useful in aligning risk and remuneration and should be considered. The length of the deferral period should be sufficiently long to allow for crystallised risks to be reflected in remuneration outcomes.</p> <p>Tax rules² restrict the ability to award deferred compensation to employees and service providers, such that it can only be awarded where:</p> <ul style="list-style-type: none"> • An election to defer the compensation is made in the year prior to the award; and • It vests in line with a pre-defined vesting schedule (which cannot be changed at a later time). 	

1 There are mandatory requirements for banks regulated by the Federal Reserve Board and the Interagency Arrangement, including: (1) Guidance on Sound Incentive Compensation Principles (2010); (2) Dodd-Frank Wall Street Reform and Consumer Protection Act (2010); (3) Enhanced Prudential Standards (2016); and (4) Incentive Compensation Practices: A Report on the Horizontal Review (2011). The regulation applies to 'Covered Employees', which includes: Senior Executives, Individuals responsible for firm wide activities, and individual and collective Material Risk Takers.

2 The Internal Revenue Service's (IRS's) Internal Revenue Code.

The background of the entire page is a deep blue gradient. Overlaid on this are several dynamic, glowing trails of light blue and white particles. These particles are concentrated in the lower half of the image, forming a large, sweeping arc that curves from the left towards the right. The particles vary in size and brightness, creating a sense of depth and movement, similar to a nebula or a high-speed data stream.

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