

Prudential Inquiry into the Commonwealth Bank of Australia

Progress Report

1. Background to the Prudential Inquiry

In recent years, a number of issues have raised concerns about the Commonwealth Bank of Australia's (CBA) governance, culture and accountability frameworks and practices, and have damaged the bank's reputation and public standing.

In response to these issues, on 28 August 2017 APRA announced that it would establish a Prudential Inquiry, to be conducted by an independent Panel, into governance, culture and accountability within CBA. The goal is to identify any shortcomings in these areas and make recommendations as to how such shortcomings should be promptly and adequately addressed.

However, the Panel is not tasked with making specific determinations regarding matters that are currently the subject of legal proceedings, regulatory actions by other regulators, or customers' individual cases.

The Terms of Reference for the Inquiry are attached.

This Progress Report provides an update on the status of the Inquiry and outlines the methodology that the Panel has adopted to address the Terms of Reference. The work undertaken to date, on a range of fronts, is helping to provide the Panel with a comprehensive understanding of CBA's frameworks and practices. That said, issues of governance, culture and accountability in a large financial institution are complex and interwoven, and the Panel does not consider it appropriate to draw conclusions, even preliminary ones, before this work is completed and all relevant evidence collected and carefully evaluated.

Accordingly, the Panel will reserve its substantive findings and recommendations for inclusion in the Final Report, which will be provided to APRA by 30 April 2018.

2. The Panel's approach to the Inquiry

The Panel is focused on identifying the key organisational and behavioural factors, or combination of factors, that can explain the public "fall from grace" of an otherwise iconic and financially very successful Australian financial institution. The Panel is seeking to understand any dynamic between CBA's financial success and any shortcomings in its responsiveness to and management of risk. To this end, the Panel has adopted a methodology structured around three core themes that are aligned with the Terms of Reference:

- **Governance** - the way in which decisions at CBA are made, including how financial objectives, values and strategic priorities impact on the decision-making process, and how decisions, once made, are implemented.
- **Culture** – the norms of behaviour for individuals and groups within CBA that determine the collective ability to identify, understand, openly discuss, escalate and act on the organisation's current and future challenges and risks.

- **Accountability** - the way in which CBA staff, both individually and collectively, fulfil their responsibilities and the consequences of not fulfilling these responsibilities.

Within each of these three core themes, there are a number of more detailed focus areas or “work streams”. These cover whether CBA’s organisational structure and governance, its risk management and compliance framework, its remuneration and accountability frameworks, its financial objectives, and its framework for identification, escalation and addressing matters of concern, are conflicting with sound risk management and compliance outcomes.

Each work stream is undertaking a detailed assessment of CBA’s current practices and any initiatives CBA may already have underway, using a combination of:

- **Evidence-based analysis** of quantitative and qualitative information about CBA’s governance, accountability and culture frameworks and practices. This information is being obtained through a range of activities, each of which is described below.
- **Case study analysis.** The Panel is reviewing more recent incidents that have occurred at CBA that are considered relevant to the Inquiry. This review provides additional insights into how CBA’s decision-making processes and behaviours have operated in practice.

The results of the evidence-based and case study analyses are also being assessed in the context of global industry norms and practices. This is assisting the Panel to form a holistic understanding of CBA and gain a broad perspective on governance, culture and accountability issues.

3. Activities undertaken by the Inquiry

The Panel acknowledges the strong support it has received from a project team of APRA staff. This team incorporates a Secretariat function, along with relevant subject matter experts from APRA’s supervision and specialist areas.

The Panel is also supported by Oliver Wyman, a global management consultancy, which is providing specialist input and additional advice about international practices and lessons learnt from recent governance, culture and accountability incidents in various financial centres.

Each of the work streams is managed by a dedicated group drawn from the project team and Oliver Wyman. The range of activities being undertaken, particularly to build-up a comprehensive evidence base, include:

Staff interviews

Approximately 80 interviews with current and former CBA staff are expected to be conducted as part of the Inquiry, covering a broad range of staff levels and functions. To date around 60 interviews have been completed, and the remainder are scheduled for coming weeks.

Interviewees include:

- Board directors;
- the CEO, CFO and CRO and other relevant CBA Group Executives;

- senior management, including Executive General Managers and General Managers; and
- former CBA Board directors and executive staff.

Interviews have been structured as general “fact finding” interviews, as well as deep structured interviews to understand the organisational and cultural drivers of Board and management actions within CBA and whether particular factors are conflicting with sound risk management and compliance outcomes. The Panel has conducted a number of these interviews, and intends to meet with all Directors and key decision-makers during the course of the Inquiry. Other interviews are being run by the project team, which then briefs the Panel.

Staff focus groups

Eleven focus groups have been held, involving in excess of 100 CBA staff at management level. These groups have been moderated by the project team and are conducted on a confidential basis. They are structured as workshops designed as a means of identifying behavioural norms that either support or detract from the effective management of risk.

Staff survey

An online staff survey has been developed and made available to nearly ten thousand CBA staff across a range of levels. The survey captures Australian-based staff and select overseas staff.

The survey, which draws on similar surveys overseas, contains a range of questions designed to understand CBA’s culture and its approach to risk management. The results are not yet to hand, but are expected to provide another useful source of data to analyse and supplement other evidence.

Meetings with other regulators

The Panel has met with the Australian Securities and Investments Commission (ASIC), and has plans to meet with other relevant agencies, to gain further insights into CBA’s framework and practices, as well as additional background on particular incidents where necessary.

Document review

Over 10,000 documents requested of and voluntarily produced by CBA are being reviewed as part of the Inquiry. Documents include framework documents such as policies and procedures, Board and Board committee papers, executive committee papers, project documentation, internal staff communications, Human Resources data, and emails and correspondence.

4. Remaining steps in the Inquiry

There is further work to be done. Interviews with current and former CBA directors and staff are continuing, the CBA staff survey needs to be completed and analysed, and the review of the extensive documentation provided by CBA is ongoing. Further benchmarking of CBA’s frameworks and practices against global industry norms and practices will be carried out.

As the fact-finding process nears completion, the Panel is directing its attention to some particular issues that have emerged from the work to date. These issues include:

- Board (including Board Audit and Risk Committees) and senior executive responsiveness to emerging risk issues and diligence in overseeing the resolution of these issues;
- the influence on CBA's culture of the Board and senior executives;
- the complexity of policies and decision-making processes within CBA;
- the prioritisation and execution of investment in risk systems;
- capabilities and accountabilities for risk management in the organisation, particularly for operational, compliance and reputational risk;
- the stature, maturity and resourcing of the compliance function; and
- the responsiveness of remuneration to risk outcomes, adverse or positive.

The Panel wishes to acknowledge CBA's cooperation with the work of the Inquiry. The Panel also notes that CBA is undertaking a number of significant remediation initiatives in the risk management and compliance areas, which the Final Report will take into account.

31 January, 2018

APRA Prudential Inquiry into CBA: Terms of Reference

The purpose of the Prudential Inquiry is to examine the frameworks and practices in relation to governance, culture and accountability within the CBA group, so as:

1. to identify, in light of a number of incidents in recent years that have damaged the reputation and public standing of the CBA group, any core organisational and cultural drivers within CBA that have contributed to these incidents.
2. to assess, at a minimum, whether any of the following areas, or their implementation, are conflicting with sound risk management and compliance outcomes:
 - a. the group's organisational structure, governance framework, and culture;
 - b. the group's framework for delegating risk management and compliance responsibilities;
 - c. the group's financial objectives;
 - d. the group's remuneration frameworks;
 - e. the group's accountability framework; and
 - f. the group's framework for identification, escalation and addressing matters of concern raised by CBA staff, regulators or customers.
3. to consider, where CBA has initiatives underway to enhance the areas reviewed under (1) and (2) above, whether these initiatives will be sufficient to respond to any shortcomings identified and, if not, to recommend what other initiatives or remedial actions need to be undertaken.
4. to recommend, to the extent that there are other shortcomings or deficiencies identified under (1) and (2) above that are not already being addressed by CBA, how such issues should be rectified.

The Prudential Inquiry should not make specific determinations regarding matters currently the subject of legal proceedings, other regulatory reviews or investigations by regulators other than APRA, or customers' individual cases.

The Inquiry Panel appointed to conduct the Inquiry will submit a progress report to APRA by 31 January 2018, and a final report by 30 April 2018.