10 February 2017

Mr. Stephen Sedgwick AO
Independent Reviewer
ABA Retail Banking Remuneration Review

Dear Mr Sedgwick,

The Finance Sector Union of Australian welcomes the opportunity to provide comment of your Retail Remuneration Review Issues Paper dated 17 January 2017.

The structure of the union's response to your report is:

1. General comments regarding the contents of the report
2. Specific responses to the questions you have sought feedback on
3. The union's position regarding the finalisation of the report
4. Attachment A
5. Attachment B

Should you wish to discuss the union's response or require any further information please contact National Assistant Secretary Geoff Derrick on (02) 9320 0005.

Yours sincerely

Julia Angrisano
National Secretary

Section One ~ General Comments

The Industry Doesn't Accept That Change Is Necessary

The union challenges the weight to be given to the assertion that, "key figures within the banking industry are openly acknowledging that a significant trust deficit has emerged because practices have developed that have not been, or have been seen not to be, in the interests of customers. They are calling for this deficit to be addressed." We remain sceptical about the extent that this acknowledgement will lead to any meaningful and lasting improvement in the culture or practices of the industry, without industry wide mandatory regulatory reform.

Without regulatory reform, Australians are left with a mixture of market forces and self-regulation to bring about the necessary change. The cultural aspects of the industry that caused this "trust deficit" emerged and became entrenched under a system of market forces and self regulation. The decision makers in the industry have proven, in large part, to have a "tin ear" and are unable to hear the cries of foul play from their own customers and staff.

The FSU believes that while 'key figures' acknowledge the existence of a 'significant trust deficit' this comes as a part of a well-worn strategy where the banks acknowledge a small number of minor problems, usually characterized as individual and isolated, which they then assert have all been resolved, whilst organising a resistance against any proposed change that would force them to alter their business models.

This approach is evident whenever a bank is asked a question about whether their remuneration or work systems are responsible for the ever growing number of cases where a customer has been disadvantaged as a result of an interaction with their bank. Their standard response is to state that if a customer was disadvantaged then it was due to the behaviour of a rogue employee.

The FSU attended the 2016 annual general meetings of the big four banks and asked each Board Chairman the following question, *'… in light of the Australian Banking Association's review into front line retail bank staff pay and incentives how has the board ensured that the executive remuneration structures and outcomes drive a better culture from the top down and deliver on rebuilding trust and confidence in the bank and financial system.'*

Whilst the words used in each answer varied, the sentiment across the four banks was the same. Each Chairman stated that they had full faith in their culture, processes and systems and that all examples of a poor customer outcome occurred due to the behaviour of a rogue employee who was punished for their transgression.

A full transcript of each question and answer is detailed in Attachment A.

Of further concern is the fact that none of the answers contained a commitment to implement the recommendations of your report. In fact the response from the CBA Chairman implied that the CBA is more of a spectator than a participant in your review.

Your report states that, "a number have told the Review that they have scaled back over time the significance of product-related payments and strengthened the checks in place. Some have announced an intention to go further in this direction in the year ahead. Others, on the other hand, argue that their culture has been historically strongly service oriented and significant change is not required".

Remuneration And Work Systems Are Designed To Drive Behaviours

The major banks invest millions of dollars into the design and implementation of their remuneration and work systems. These systems are designed to motivate and drive specific human behaviours and reward the behaviours that the organisation values.

Australian banks in particular the big four, are judged to be successful when they maximize their return on equity, reduce costs, maximize profitability and increase their share price. It is inconceivable that banks would design and implement remuneration and work systems that do not drive the human behaviours that enable the bank to be judged as successful against these measures, particularly by the investment community.

There is a truism that, 'You measure what you value'. Nothing is measured more by banks than sales.

The union rejects that poor customer outcomes only occur when a rogue employee acts out.

The union also rejects that bland statements of good intentions from chairpersons and CEOs are capable of trumping the remuneration and work systems that staff are managed by every day.

Skills, Attributes and Motivation of Bank Staff

Whilst the union believes that the banks' remuneration and work systems are designed to drive any employee to see every customer interaction as a sales opportunity, the banks' employment strategies over the past decade with regard to front line staff have exacerbated the problem, as banks have focused on identifying and employing individuals with retail sales experience.

Many of these employees have come from industries that pay commissions based on the volume of sales and are subject to little or no regulation in relation to the processes used to secure sales.

These employees understand and accept that the work and remuneration systems they work under expect them to exploit every sales opportunity and that their ongoing employment and advancement are determined by their ability to achieve and surpass their sales targets.

The remuneration models in place encourage this behaviour because they do not value a responsible decision not to sell an inappropriate product. Rather, the banker who makes this decision risks losing out financially every time they forgo a sales opportunity. If they do it enough times they even risk their job security because of the threat of being sacked for failing to meet targets.

New management claims of moderated remuneration models do not fundamentally change the culture or direction of this sales focus. What they do is transfer the blame for the inappropriate sale onto the individual banker if the customer complains.

The FSU does not believe that it is a coincidence that the increase in the number and frequency of poor customer outcomes has coincided with the introduction of remuneration systems that are driven by volume based sales outcomes.

Customer Best Interest

Much of the report is spent discussing what defines a 'poor customer outcome' and to what extent remuneration and work systems can drive behaviours that can contribute to 'poor customer outcomes'.

Whilst organisations and individuals can argue the two elements above, the union continues to assert that the customer's best interest requirement contained within the FOFA laws should be extended to cover all interactions between a bank and its customers.

The definition of customer's best interest must include the notion of a customer's genuine banking needs, rather than the approach used by Australian banks where each customer interaction is seen as an opportunity to sell, refer and/or cross sell – rather than meet the banking needs of the customer.

FSU members have explained to you the techniques that they are trained in that are designed to identify and exploit sales opportunities. The notion of a, 'do you want fries with that' approach is annoying at a fast food outlet but contains real risks when the fries are substituted by a credit card, a loan or insurance product that has the potential to create real financial disadvantage for the individual.

The FSU believes that only a legislated customer best interest requirement coupled with a ban on conflicted remuneration is capable of trumping the existing remuneration and work systems within the industry.

Australian banks have used their submissions to your review, their ongoing public comments, and their advertising, to assert that treating the customer ethically is what drives their business.

Surely if the industry means what it says then they can have no objection to a legislated customer best interest requirement.

Without a legislative response, customers will be left to rely on market forces and the goodwill of banks - trusting that their rhetoric about caring for customers will win out against their need to increase their return on equity.

In this battle the customer will not win. The banks will continue to design remuneration systems that encourage and prioritise volume based sales over customer needs.

Your report states:-

> "A strong and deeply embedded sales culture, for example, is difficult to change quickly. Attempts to do so need to be sustained, credible and possibly dramatic to have an ongoing effect".

Why should the community have to rely on the sustained efforts of their bank, particularly when there is little evidence that they are either capable or willing of sustaining such an effort?

A bank that practices ethical behaviour should not be at a competitive disadvantage. The only way to ensure that remuneration and work systems or the needs of the bank are not achieved at the expense of customer interests is to enact an industry wide legislative requirement for this to be the case. Anything less is piecemeal.

This solution will also ensure industry wide consistency in relation to consumer protections and rights, and whilst each bank would remain free to establish their own compliant remuneration and work systems, each system would have to ensure it incentivises employees to behave ethically and provide the appropriate product or service to meet the needs of the customer.

Evidence

The union is concerned by the statement in the report that, 'few submissions to date have provided clear evidence that the risks in banks' current arrangements lead to such significant systemic risks of poor outcomes for retail banking customers as would warrant the outright banning of product-based payments'.

It should not take the discovery of a 'smoking gun' that definitively proves a certain element of a remuneration system and/or work system is the direct link to a specific employee behaving in a way that specifically disadvantaged a particular customer.

There is material before the inquiry that demonstrates a casual link between the design and implementation of existing remuneration and work systems and the emergence of a culture and management practice that meet the definition of a poor customer outcome.

This material includes the oral evidence of workers in the industry about management prioritising sales over service. It includes evidence of the design of remuneration systems that balloon payments for product cross selling and higher volume sales over definite timeframes, and it includes the acknowledgement of a number of banks that they have already seen the need to move away from strict volume based measures as the sole determinant of employee performance.

Scorecards

The union agrees that the balanced scorecard concept is often intended to mitigate the concentration on selling at any cost but agrees with the assertion in the report that most of the existing scorecards reinforce the emphasis on volume based sales outcomes.

The union has also noted that the banks that have adopted scorecards use them as a defense against claims that their remuneration systems drive unethical behaviours. These statements are predominantly made to a public audience by Executives and Chairpersons and demonstrate a lack of knowledge of the application (and sometimes the content) of their scorecards and what elements of the scorecard are performance managed most aggressively by their managers.

The union will revise its position on the ability of any 'balanced scorecard' to mitigate the push to achieve a sale with every customer interaction when we see evidence of genuine balance between the score attributed to ethical behaviour that leads to a decision not to sell, as much as decision to sell.

The Risk Is Known?

The report asserts that:-

> "Senior managers whom we consulted are very aware of the risk that rewards will encourage approaches or activities that exceed, underachieve or are contrary to the effect that they seek to achieve. This occurs because humans are themselves complex and may interpret incentives differently from those who created them. Moreover, messages may be lost or modified in transmission in a large workplace, including as Managers seek to interpret potentially complex messages for their staff. All banks therefore have arrangements intended to mitigate such risks, which include the risks of miss selling, potentially leading to poor outcomes for customers."

The term "Senior Manager" unfortunately is vague when referring to corporations with over 30,000 employees and many layers of management. The FSU would be interested to know how senior the 'senior managers' referred to in the report were, and how they would explain the daily and weekly meetings run by regional and state managers who only focus on performance against volume based sales targets, and who routinely threaten staff who have not met their targets with dismissal.

Is it possible that these ‘Senior managers’ are the same managers who issue the daily digital scorecards and leader boards that detail regional, state and national sales results against target? Are they the same senior managers who routinely speak with a rhetoric that eulogises those who achieve the highest sales results, and vilifies those who have not achieved their sales targets (despite meeting all of their other measures).

The union sees the responses received from ‘senior managers’ as yet another example of the industry trotting out the tested line that conveys the message “if one employee misunderstands what we mean then our systems will catch them and we will step in and fix the problem”.

This approach repeats the mythology of the “bad apples” being the source of the problem, despite ASIC Chairman Greg Medcraft has more accurately describing the problem as emanating from a poisoned tree (ASIC Annual Forum Sydney March 2016).

Does The Size Of The Incentive Matter?

Whilst most reviews and investigations into the effect of financial incentives conclude that the larger the incentive the greater the risk of unethical behaviour, the union is concerned that such a premise could lead to a debate designed to find the mythical incentive amount that drives sales but does not encourage unethical behaviour.

The reason for our concern is that the existing systems, for most front line staff, do not rely on large amounts to drive behaviour, rather they rely on aggressive management systems with the larger rewards only being available to senior managers.

This suggests that if the theory of larger incentives driving greater risks is true, then it is the larger incentives for senior managers who drive behaviour through command and control structures that should be the focus of this inquiry, not the relatively small payments on offer to front line bankers.

The other factor that should be considered when assessing whether the amount of an incentive is a determinative factor in driving behaviour is that for many FSU members their jobs are threatened when they do not achieve their sales targets.

When assessing this issue the report should consider the threat of losing 100% of a salary and ongoing employment as a more insidious tool designed to drive behaviour, than trying to determine the appropriate percentage of remuneration that should be at risk.

Complexity

The report identifies that the complexity of some schemes and the subsequent ability of managers to oversee these complex schemes could be a cause for some poor behaviours.

Whilst some schemes are overly complicated and the levels of complexity make it more difficult for managers to ensure that the right behaviours are rewarded, the feedback from members indicates that in many cases it is the brutal simplicity of the existing priorities that create problems.

For example, when an employee is told they must achieve 10 referrals a week, or sell mortgages to the value of $500,000 in a week, or open 9 new accounts in a week – complexity isn't the issue. The issue for the employee is how do I convince a customer to open an account or be referred on in relation to a product or service they don't want? Or, how do I write a $500,000 mortgage when none of my customer leads want a mortgage that large?

The system complexity is overcome by managers when they simply look at the results and determine whether the employee has met their target.

It is also not complex when a manager abuses an employee for not achieving their target and won't accept any excuse for failure. There is no complexity when a manager refuses to excuse a banker for not achieving a volume based sales target when the customers the bank dealt with didn't want to be referred on, or to open a new account, or didn't want a mortgage.

The legislated customer best interest test coupled with a ban on conflicted remuneration would also drive simplified management systems and product disclosure statements.

Cross Selling

The report states:-

> "I have tentatively concluded that cross-sales targets, especially those that are used as a gateway to access rewards otherwise available to a Seller (or a modifier to increase the reward otherwise available), significantly increase the risk of mis-selling."

The union welcomes this conclusion but does not understand how you have only reached this position regarding cross selling. Many elements of the system that the report describes relating to cross selling also exist in the systems that don't require a cross sell trigger.

Any finding in relation to cross selling must equally apply to selling because it has the same fundamental flaw that it is potentially driven by something other than the customers' best interests.

Customer Satisfaction

The union agrees with the assertion in the report regarding customer satisfaction being a limited tool in assessing a customer interaction, namely:-

> "Many banks are moving to increase the emphasis placed on customer satisfaction in their performance metrics and in the service offer they propound to customers. However, the metrics to support such an orientation appear rudimentary. Typically, data is collected about whether or not a customer would recommend the bank to a friend (sometimes called the Net Promoter Score) or the level of satisfaction a customer expresses against a numerical scale. Often the customer is approached just after an interaction with a bank staff member, well before the effectiveness will be apparent to the customer of the product they may just have been sold."

In the experience of many FSU members, customer satisfaction depends on how long the customer had to wait in a queue or on the phone and whether they liked the answer that was provided to them.

Customer satisfaction should be measured by whether the institution meets the genuine needs of the customer and such a measure begins with legislating the customer best interest test.

Culture

Attachment B to the union's response contains an article written by Michael Bennett from The Australian.

The article reinforces the effect that culture has on what employees believe their employer values most. Existing bank cultures do not stop unethical behaviour, rather they drive work and remuneration systems that predominantly focus on sales.

The suggestion of more open reporting around defined 'cultural and non financial hurdles' would be worth exploring.

Section Two ~ Specific Responses To Questions

The FSU's response has grouped together questions that the union believes relate to similar topics. Should you require further information in relation to a specific question, contact FSU and we will provide a more detailed response.

Questions

1. Is there a realistic alternative to setting targets as an aid to the management of a large organisation?
2. What is the appropriate role of targets in managing performance and assessing rewards payable to an individual?
3. What is the nature of the risk attached to setting targets that are sales or product-related compared to others such as service metrics? (See also section 6.2 below.)
4. Is such a risk lowered if targets are set and eligibility for rewards is assessed less frequently (e.g. annually compared to monthly)?
10. Alternatively, should banks limit the weight applied in total to financial measures to, say, 35% in these assessments?
26. What approaches to performance management and rewards and incentives are most conducive to achieving it?
27. What weight should be attached to sales targets in the assessment of the performance of a bank's most senior executives?
28. What are the key principles that banks should apply in designing the incentives that apply to their most senior executives?
33. Is there evidence that the risks of mis-selling are currently significant, not sufficiently mitigated by existing strategies, and systemically important?

The union does not accept that a performance management system with a target regime at its core is required to manage or drive the performance of employees.

Those who suggest that such systems are essential tools make two erroneous assumptions;

- Firstly performance based pay with volume based targets driving financial reward is an effective or necessary motivation tool to get employees to perform their duties satisfactorily; and
- Secondly, that conflicted pay can be accommodated within a best interests duty environment.

There is now a substantial body of international evidence demonstrating that performance based pay does not deliver the desired or assumed results from a productivity or motivational perspective. If the Inquiry is not aware of this evidence please contact the FSU and we will provide references.

A best interests duty is irreconcilable with a conflicted pay model, regardless of the proportion of remuneration at risk.

The union believes that an alternative system would be a skills based accreditation system underpinned by professional ethical standards that recognise and reward the skills required to assess the needs of a customer, provide advice regarding the appropriate product or service, and the provision of the relevant service or product. This system would also reward regulatory and professional standards compliance.

Volume based sales, cross selling or referral target regime have no place within the Australian finance industry. The risks associated with such systems include:

- Pushing products and services onto customers regardless of their needs;
- The implementation of work and management systems that drive and reward unethical behaviours;
- The use of bullying and humiliation as management tools;
- Focusing overwhelmingly on sales results when assessing an employee's performance;
- The sale of inappropriate products and services to customers;
- Reduction in the professional standing and reputation of the finance industry; and
- Reduced focus of regulatory and professional standards compliance.

The union believes that a debate about the percentage value of a target, eligibility for rewards or what are acceptable incentives is a red herring. Any target driven sales regime (regardless of the remuneration amounts contained within) must see the customer as a sales opportunity to be exploited during every interaction, and require employees to ignore the genuine needs of the customer in their attempts to secure the sale.

When coupled with a command and control regime that has management driving, intentionally or otherwise, poor behaviours, any target driven pay regime is fundamentally compromised.

The union will continue to advocate for the introduction of a legislated customer's best interest test and the abolition of conflicted pay similar to that contained within the FOFA laws. The introduction of such a standard would necessitate the complete redesign of all performance management systems and that that would be the appropriate time to debate the weightings contained within the system. This debate is rightly an industrial issue to be dealt with in the appropriate industrial forums once the legislative framework is set.

Question

5. How best can we address the trade-off between simplicity, on the one hand and, on the other, elements to guard against the risk of incentivising poor outcomes for customers?

Whilst the FSU agrees that the documents detailing the various performance management systems can be complex, confusing and contradictory, the feedback we consistently receive from FSU members is that there is no complexity or confusion regarding how they are applied within workplaces.

There can be little doubt regarding the measure that is most valued by managers and little doubt about what measure their employer will use to assess whether they are a successful employee. The remaining elements of complex remuneration designs tend to be used after the fact by managers when something goes wrong.

As has been pointed out here and in workers round tables held during the first phase of the inquiry, sales results are the only issue that is the subject of daily, weekly and in some case hourly meetings.

Every employee is aware of their bank's assessment of their ability to sell, cross sell or refer as an individual and as compared to their peers.

There is no complexity in this assessment (you are either on or above target or you are failing), and there is no complexity when it comes to understanding the consequences of the assessment (you either have to maintain your target or above rating or you will lose your job).

Questions
6. Should banks discontinue the practice of using accelerator-type50 payments?
7. If yes, what other devices are suitable to reward high performers?
8. Should banks discontinue the practice of applying gateways to incentives payments based on the achievement of financial measures?
9. Should banks discontinue the practice of assessing performance and eligibility for rewards on the basis of product-based payment? If yes, on what basis?
11. Should banks discontinue the practice of applying cross-sales gateways or modifiers?
12. If yes, what other approaches are available to encourage and reward staff that assist customers to identify and meet their needs?
13. Are cross-sales incentives more likely to lead to poor outcomes for customers than general sales targets?
17. Should banks adopt the principle that sales incentives should be 'product neutral'?
18. If yes, how is that neutrality best established?
19. Should banks discontinue the practice of applying accelerator-like arrangements?

The union's position in relation to above questions is the same as its position in relation to the other elements of the existing sales based remuneration systems.

Whilst it is possible to argue that some incentive tools are more likely to drive unethical behaviour than others, it is a fallacy to think that there is a magic number when an incentive scheme suddenly creates an unacceptable risk compared to one dollar below that figure. All of these systems drive the same behaviours and form part of remuneration and work systems that reward volume based sales (regardless of customer need), and punishes the employee whose only failure is to meet a 'stretch' sales target. More importantly, the remuneration system for the middle and senior management drives both behaviour and culture. These managers do not sell directly to customers, rather they manage the sales force that does. Having a scaled back conflicted pay model at the front line misses the point entirely.

Question

15. Is there a case for banks to adopt scorecard-based approaches in order to minimise the risks of mis-selling? If so, why?

The FSU supports the concept of a balanced approach to assessing the performance of an employee but rejects the notion that that is what currently applies in the industry.

An examination of most scorecards used within the industry clearly illustrate that sales, cross selling and referrals (revenue measures generally), are what is most valued by the bank. In some cases the weight attached to sales related activities are higher than the weight attached to all of the other activities on the scorecard. In other cases revenue based measures are disguised as skills or teamwork or even service.

Where a scorecard places an aggregate value on non sales activities that is higher than the sales based activities, that bank will use leader boards and meetings that only emphasise the sales related activities leaving the employee in no doubt as what activity is of most value to their employer.

Question

20. What conditions need to be met to ensure that Manager discretion is exercised in ways that minimise the risk of poor outcomes for customers?

There are literally thousands of line managers, middle managers and senior managers in the industry. As long as the debate is about relying on individual managers to exercise discretion to moderate conflicted pay related behaviours the risk of poor customer outcomes will continue to be unacceptable. Scandals will continue and public trust will be eroded. Pursuing an approach based on individual discretion panders to the bad apple myth. The problems are systemic. The solutions must be systemic.

Questions

21. Should the regulatory framework for retail banking be strengthened? If so, then how?
22. Are further changes required to the regulatory environment to reduce the information gap between a seller and the retail purchaser?
23. Is the legal distinction between the 'provision of information ', 'general advice' and 'personal advice' useful or effective in the retail banking context?
24. Having regard also to the mitigation strategies available to banks, is there excessive risk of mis-selling attached to the practices outlined in Chapters 3 and 4 regarding incentives to retail banking staff and third parties that act on behalf of banks?

The Commonwealth Parliament should legislate a customer best interest test coupled with a ban on conflicted remuneration (similar to the FOFA laws, that applies to all interactions between the industry and the customer).

Question
25. What constitutes a 'service' culture in the retail banking context?

A 'service culture' within the Australian finance industry should be defined by at least the following:

- Management systems and management driven behaviours that put a high value on service; and
- Meeting the genuine financial needs of a customer (not seeing the interaction as a sales opportunity to be exploited); and
- Agreed qualifications and professional standards that all employees must obtain and maintain; and
- The provision of quality service and advice; and
- Products and services that are designed to meet the genuine needs of the customer; and
- Acceptance of fault when a product or service does not match the assertions made by the PDS or the individual who sold it.

Question
32. What do you think of the adequacy of adopting the FSA's approach for the purpose of defining a poor customer outcome?

The FSU supports the elements identified by the FSA.

Section Three ~ What Next?

The FSU has previously expressed its concerns about the narrow terms of reference of this inquiry and the fact that a complete review of all remuneration systems in banking from the front line to the CEO is required if the problems are to be fixed.

Whilst the FSU does not presume to dictate the final structure, content and findings of the inquiry, it believes the following issues need to be confronted and addressed:

Remuneration Systems Do Contribute To Poor Customer Outcomes

There is sufficient evidence for the inquiry to find that remuneration systems do contribute to poor customer outcomes and this finding should not be qualified.

The FSU notes that the quote within the report from the head of the RBA who accepts that there is a link;

> *"In terms of behavioural issues...I think it comes down to incentives within the organisations, and that is largely remuneration structures...If there was one thing I could focus on...is making sure that the remuneration structures within financial institutions promote behaviour that benefits not just the institution but its clients."*[9]

What Will It Take To Change?

The lack of consistent, across the board commitment from the industry to fully implement the recommendations of the final report, and the continued positioning of some banks as spectators (rather than participants) to the review, demonstrate the industry's unwillingness and indeed, inability, to implement any industry wide change that the community can rely upon.

When this is combined with the ongoing statements from banks that their existing culture, practices and policies are sufficient to prevent and/or address the small number of poor outcomes, an "In-house", industry led inquiry, where the industry determines both terms of reference and the implementation and compliance regimes, the only conclusion is that this is insufficient to ensure the introduction of necessary change.

The union has valued its interactions with the inquiry and believes that the inquirer continues to approach this task with integrity and a real desire to address the issues that are the subject of the review. However this is not enough. Rebuilding public trust and confidence requires a judicial review with independent terms of reference followed by legislative action to introduce industry wide reforms.

The most recent example of this situation were the FOFA laws. The banks were aware of the problems in the advice industry, and were responsible for a number of the scandals that bankrupted many Australians. Despite this knowledge, they aggressively campaigned against the need for any change to the advice laws and when the Parliamentary Inquiry into the FOFA laws recommended legislative change they campaigned against those changes, and when the government of the day changed they again campaigned to have the effect of those laws reduced.

With this knowledge, the FSU believes that this inquiry's report must acknowledge the industry's reluctance to change and the need for the recommended changes to be enacted into law.

Will Banks Implement The Findings Of The Report?

Probably not. An independent review conducted one year after the findings are published will be required to assess the degree to which the banks actually implement the recommendations.

Attachment A

The following are the transcripts from questions the union asked at the 2016 annual general meetings of Westpac, ANZ, National Australia Bank and the Commonwealth Bank.

WESTPAC GROUP LTD AGM QUESTION AND ANSWER TRANSCRIPT

The WBC AGM was held in Adelaide on 9 December 2016

Question asked by FSU National Secretary Julia Angrisano

"Thank you Mr. Chairman. On behalf of the Finance Sector Union, the question relates to statements made by yourself on the 13th May 2016, when you were reported by the Australian Financial Review has holding the following views regarding the way conflicts can play out.

'These comments include; I can remember times when as the CEO and the pressure is on in the last quarter, so you are saying things to staff like its really important that you meet your targets this month do this and this, and that this can be misrepresented.

Perhaps Lindsay is telling me whatever it takes, and finally in setting those KPIs for employees they have to understand customer first has to be in there and then you have to back it up, do what you really mean, and then when the pressure comes on earnings you don't revert to type and say make sure you get your sales targets this month or next month.

That's what makes it really hard and complex and quite annoying when people come in from the outside and say this is really bad culture, these are really big complex organisations to run and people can get mixed messages.'

So given these comments and in light of the Australian Banking Association's review into front line retail bank staff pay and incentives how has the board ensured that the executive remuneration structures and outcomes drive a better culture from the top down and deliver on rebuilding trust and confidence in the bank and financial system."

Response from WBC Chairperson Lindsay Maxsted

"Thank you and it's a good question and it's something we think about a lot and I suppose I would answer it in a couple of ways.

One I think it all goes right back to the beginning in terms of what the vision is for the bank and the strategy, and you heard that adequately set out by Brian during his speech earlier that if we are to be one of the great service organisations we have to put the customer first and we have to deliver on the promise to the customers.

So with that in mind then and to the extent that the 40,000 employees embrace that as a proposition as to why they wish to work at Westpac that is our starting point.

And then specifically in relation to the remuneration for the CEO and for the broader group executive then they have, each of them have certain key performance indicators KPIs as to what has to got to be achieved during the year to earn the bonus, the short term incentive for the year and whilst absolutely part of that is financial performance so what are the cash earnings and what is the cash earnings and what is the growth in returns and so on, a large part of that assessment that we make as a board is around the issues that will drive the behaviours.

Some of its around risk management, around the sustainability pieces, its around employee treatments pieces so if we observe, if I observe, if the board observes, less than satisfactory behaviour like that in relation to the CEO (which I add for completeness that we do not) but were we ever to then notwithstanding what the financial results were then the short term incentive payment would be much less lower than it would otherwise be and that applies right across the entire organisation."

ANZ AGM QUESTION AND ANSWER TRANSCRIPT

The ANZ AGM was held in Melbourne on 16 December 2016

Question asked by National Secretary Julia Angrisano

"Thank you Mr. Chairman. Mr. Chairman on the 13th of May 2016 you were reported by the Australian Financial Review as holding the following views:

'It is imperative that the person working in a branch should be proud of who their chairman is, should be keen on who the board members are because they are emblematic of the culture of that organisation, and in your view remuneration should encourage longer term thinking for the benefit of the bank, all of the bank stakeholders which includes the customer, the society and the staff.'

Given these comments and in light of the Australian Bankers Association's Sedgwick review into frontline retail bank staff pay and incentives how will the board ensure that executive remuneration structures and outcomes drive a culture from the top down and deliver on rebuilding trust and confidence in the bank and our financial system?"

Response from ANZ Chairperson David Gonski

"Thank you for that question, I think it is a very good question and one is always nervous when you say what you said on a particular day but I agree with what I said on that date.

And I want to assure you and the other shareholders that we know that the way we pay people does instigate particular ways of dealing with things and we are absolutely aware of that.

This why as Shane mentioned in his speech we've moved to this balanced scorecard which gives at least an equal weighting to customer satisfaction, because we see that as incredibly important before anybody gets we have what we call a gateway and the gateway is that our staff adhere to our code of conduct, and let me tell you, and I know you are from the union, our staff are excellent and indeed would adhere to the code but we make that a principle, that is has got to get through the gateway we want to make sure that in bringing things together that the stakeholder importance together with the staff motivation together with the abilities of the staff are all weighed together so that they are not pushed to do things which would be improper and that they are not paid when they do something wrong.

So I can assure you that from the top we are aware, we have spoken to our CEO, our people committee is aware of this, that we have this balance scorecard which is being intensified and I think working pretty well.

We should say, I have been reminded, measure customer satisfaction over time not just at a point in time so for those who are cynical you just can't improve your customer satisfaction in one moment and then expect that that will get you a bonuses or pay or whatever."

And that's the culture that we want and we have in many many parts of the bank and you know we live here in Australia, we want to do the right thing in those communities so its really important as a final note on that we don't reward on branch staff purely based on revenue and selling things, we don't, we have a very balanced approach to that and one the most important metrics that we reward is actually customer feedback so we do this, real time customer feedback and so if you go into a branch we survey a lot of those people and so that's what the customer satisfied."

CBA AGM QUESTION AND ANSWER TRANSCRIPT

The CBA AGM was held in Perth on 9 November 2016

Question asked by National Assistant Secretary Geoff Derrick

"Good morning Chairman. Mr. Chairman on the 13th of May 2016 you were reported by the Australian Financial Review as holding the following views and I quote:

'Turner accepts there can be conflicts between customer and employee interests, there could be conflict, you can structure remuneration in a number of ways so that it doesn't conflict, you can have counter veiling measures that will put it right, we are looking at how remuneration is structured, its too early in the day to tell you what we are going to do because I don't know but it is part of how you incentivise people and Turner argues that the board has a significant role to play in building culture especially amongst senior employees.'

Mr. Chairman given this report and in light of the Australian Bankers Association's Sedgwick review into frontline retail bank staff pay and incentives, how has the board ensured that executive remuneration and structure together with outcomes will drive a better culture from the top down and deliver on rebuilding trust and confidence in the bank and our financial system?"

Response from CBA Chairperson David Turner

"Well thank you it's a very good question and touches on some of the points I made when I was talking earlier.

We are very aware, this year in particular, that we do need to talk to our shareholders about how we are remunerating our top people, the structure of the remuneration, how variable it might be, how success dependent it is and a raft of other issues and we are going to be talking to the shareholders over the next 9 to 12 months.

Before we come back to the next annual general meeting that will be absolutely active, we are listening to what people say and as for the executives at the very top level, in so far as the banker's association is concerned we are tracking what they're doing with very great interest and look forward to the outcome of their deliberations."

NAB AGM QUESTION AND ANSWER TRANSCRIPT

The NAB AGM was held in Adelaide on 16 December 2016

Question asked by National Assistant Secretary Geoff Derrick

"Dr. Henry, I'm Geoff Derrick I'm here as a proxy for the Finance Sector Union. Dr. Henry on the 13th of May 2016 you were reported in the Australian Financial Review as holding the following views and I quote:

'If you were to ask the Chief Executives of all the Australian banks right now they would say they are customer centric organisations, the question is yep well they are.

We should think about the possibility that the particular financial incentives we provide do actually encourage behaviour which is not really in the interest of customers. The article went on to also quote you as saying the leaders of the banks and the ABA considered that the banks needed to ask themselves a question, are we really doing everything we possibly can to ensure our organisation is appropriately focused on the customer, really asking are we sufficiently focused on the interests of the customer' end of quote.

Given this media report and in light of the Australian Bankers Association's Sedgwick review into frontline retail bank staff pay and incentives how has the board ensured that executive remuneration and structure and outcomes will drive a better culture from the top down and deliver on rebuilding trust and confidence in this bank and our financial system?"

Response from NAB Chairperson Ken Henry

"Thank you Mr. Derrick that's a very good question and those comments you were quoted, I don't know if they were perfectly accurate, but I'm prepared to accept them, they actually sound pretty good to me and not just because I said them.

But thank you, look I want to assure you that as I've said previously this is something that we take very seriously and we do accept, we understand that the structure of remuneration, at all levels of business actually not just executive remuneration, the structure of remuneration the way in which people at all levels get rewarded for the things they do in their day to day jobs that can have an impact on conduct.

Of course the other thing that has an impact on conduct is culture but the two can fed into one another, the structure of remuneration can effect the culture of the organisation we are very well aware of this.

There are two things that in particular that we focus on as a board, the remuneration committee focuses on it and I know that Andrew and his executive leadership team focus on it when they are assessing the remuneration and performance of the people below them.

The first is whether the person in the job is demonstrating the right values, behaviours which are consistent with the values of the organisation none of which is more important than the value that all people in the NAB sign up to, which is to do the right thing and the values and the code of conduct that surrounds the values these are things that people have to hold themselves accountable for and they are held accountable for delivering for performing in a way that is consistent with the values of the organisation and with the code of conduct so that’s the first thing.

And that assessment is made about everybody at every level of the organisation, when I have a conversation with Andrew about his performance we have a conversation about whether he and to what extent he has demonstrated the values of the organisation in his performance in his behaviours.

The second thing is consequence, that if the right behaviours have not been demonstrated, if there has not been a demonstrated commitment in performance to the values of the organisation, then there are consequences and those consequences can include a discount on a short term incentive payment that discount can be a 100%, we don’t report on this publicly but very senior people in the organisation in recent years have received absolutely no short term incentive payment because of poor performance, not poor financial performance but because they have not demonstrated the values of the organisation appropriately in the way they have behaved throughout the year.

Another consequence is dismissal, we do every year dismiss people in NAB not because they have not delivered financially for the organisation even delivered they can say but I have delivered for shareholders, my actions have improved the profitability of the company this is in shareholders interests – no it is not in shareholders interests if it does not demonstrate a commitment to the values of the organisation, it might be in the short term interests of shareholders you might be able to argue that but it can’t possibly be in the long term interests of shareholders.

So it’s through those two things, an assessment at every level in the organisation that people have been demonstrating the values of the organisation and then secondly consequences if they have not that we seek to influence conduct and the culture of the organisation.”

Attachment B

Article from The Australian newspaper.

Executive hurdles must be defined

MICHAEL BENNET

Commonwealth Bank chief executive Ian Narev is believed by ma...

The bruising "strike" suffered by Commonwealth Bank's board against its executive pay policies should serve as a reminder to companies that they must improve the transparency of non-financial hurdles or face a similar backlash, says a leading governance analyst.

Using CBA as a "case study" in a report looking at the use of non-financial hurdles such as culture and diversity, Credit Suisse environmental, social and governance analyst Sandra McCullagh said banks should look at how the mining industry did a good job of defining its high-risk areas.

"CBA's culture hurdles are a good example of the need to improve the measurement of non-financial hurdles, rather than exclude them altogether," Ms McCullagh told clients.

Ms McCullagh — one of the few sell-side ESG broking analysts in the market — said the mining sector in the past decade had formed "clear" non-financial measures for health, safety and the environment that made up a "sensible component" of short-term bonuses.

"There are often lagging (lost time injury rates) and leading indicators (number of near misses, number of observable incidents) and gateway measures such as no fatalities or major environmental incidents," she said. "We believe the banks should consider defining cultural measures in a similar way — leading indicators, lagging indicators and gateways.

"For many investors, some of the recent issues in banking, such as the alleged rates rigging and issues within CommInsure, could be regarded as gateway issues that would result in no payment under that component of the long term incentives."

She added that many investors believed Ian Narev had presided over several of the CBA's reputational issues, such as the CommInsure life insurance scandal, since becoming chief executive in »

Continued

2011, and thus should not be rewarded for improving cultural issues "that he may have had ultimate responsibility for in past transgressions".

Marking a historic first strike for one of the big four banks, 50.9 per cent of CBA shareholders voted against the bank's remuneration report at its annual meeting in November following criticism of changes to the bank's pay structure, including greater use of alleged "soft targets".

Such was the tension, on the morning of the AGM the bank pulled the motion to award Mr Narev up to 55,443 fresh reward rights based on the new performance measure of "people and the community", weighted at 25 per cent of long-term bonuses.

Previously, long-term incentives were measured across four years of performance based on a total shareholder return hurdle weighted at 75 per cent, while customer satisfaction was 25 per cent.

CBA has vowed to engage with shareholders before future changes but still backed the use of a "balanced set of measures between financial, customer, people and community" to determine senior executives' bonuses.

Ms McCullagh said CBA's disclosure prior to the AGM was light on transparency. She added that measures such as the proportion of women and culturally diverse staff were part of the CEO's "normal role", and the bank should improve its disclosure and definition of culture, singling out rival National Australia Bank as the leading lender in the sector.

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