

Independent governance expert report

Australian banking industry: Package of initiatives

Report 5

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This Report has been prepared for the Australian Bankers' Association in accordance with the engagement letter dated 19 May 2016 and available at <http://www.bankers.asn.au/media/media-releases/media-release-2016/letter-of-engagement>.

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Executive summary

In response to industry concerns about a growing gap between performance delivered by banks and that expected by customers, the banking industry committed in April 2016 to a package of six initiatives to better protect consumer interests, increase transparency and accountability, and build trust and confidence in banks.

The implementation of these initiatives continues against the background of close political and public scrutiny about the role of banks in Australia. Although this is a challenging time for the industry, it is in the best interests of both banks and their customers that the banks deliver on the objectives of the six initiatives to which they have committed.

In my previous report, I noted that with the completion of the significant independent reviews commissioned by the ABA relating to the Code of Banking Practice, and to product sales commissions and product based payments, the implementation status of the industry initiatives had improved considerably. At that time, overall progress to date was largely consistent with that timeframe for those measures where the industry has control over design and implementation; however, longer implementation periods were required for measures where there is reliance on statutory underpinnings.

In this last quarter, the industry has continued to build on earlier steps taken to lift its performance, with many initiatives having moved from design to implementation stage. While individual banks are progressing with the development of their own principles on remuneration and incentives, there are a range of views held by the banks on the merits of the industry proceeding with the development of industry-level guiding principles. It is clearly desirable for the industry to settle its position in relation to this matter and reflect it as appropriate in the ABA's implementation plan.

Overall though, good progress has been made by the industry to date in advancing its reform program. While we still need to see more rubber on the road, it is evident that there are early signs of the reforms starting to gain traction. The focus going forward will increasingly be on the efforts of individual banks to embed the reform measures to deliver on the goals of the six industry initiatives. This is a long-term endeavour, but done well, consumers and other stakeholders can be expected to benefit from this significant investment in reform which continues to have strong support from the banks I have consulted.

One of the focus areas of particular interest to me has been the development of performance indicators that can be used to inform the banking industry and the wider community about the extent of progress being made in building trust and confidence over time. This builds on the industry's previously announced commitments to report on Customer Advocates (Initiative 2) and Whistleblowing (Initiative 3). Positively, the ABA has appointed Edelman Intelligence to measure the outcomes of the reform program at an industry level with the expectation that the first wave of consumer research will be published shortly after the release of this report. A second wave of research, incorporating the perspectives of both consumers and bank employees, is expected to be published early in 2018. The industry is to be commended for directly seeking to measure its performance in terms of the high-level objectives for its reform program, and its willingness to publish this information.

To date, the industry has focused on putting in place the industry-level reporting framework and has not been explicit about its intentions around public reporting by individual banks against the performance indicators developed to measure trust and confidence over time. It would be desirable for the industry to be clear on its position going forward, and even better if the major banks were to show the way in reporting their results, with other banks considering such reporting where relevant and reliable information is attainable in a cost-effective manner. This would be consistent with the industry's goal of increasing transparency, which was a key objective in the ABA's original announcement of 21 April 2016. Importantly, better public reporting during the period that the industry reforms are being bedded down is likely to lead to better outcomes for customers given the competitive nature of the industry and the evident desire on the part of all participating banks to raise the standards of customer service. Most expect the results to show room for improvement early on but the industry has to continue to back itself on the initiatives, move forward with confidence, and in this way regain public trust and confidence.

Reflecting the overall intention of the reform program, the focus of my reports to date has been on the actions by the banks to build confidence in the manner they deliver services and respond to community expectations that their behaviour meets appropriately high standards. While understandably the reform program has a focus on the responsibilities of banks in articulating and delivering on service expectations for customers, my discussions about these issues with consumers and those in business, including in the banking industry, have also emphasised the nature of the bank-customer relationship being two-way, with both banks and customers each having separate responsibilities. The proposed amendments to the Code of Banking Practice will provide a higher degree of protection for consumers; the full benefits of this will only accrue if consumers recognise their responsibility to be diligent in informing themselves of, and protecting, their interests. A wider understanding of the bank-customer relationship is essential to many of the outcomes the industry is pursuing, particularly in making engagement by consumers easier and through the measures being taken by the banks to improve transparency and confidence.

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1 Introduction

1.1 Industry initiatives to strengthen community trust

The banking industry's package of six initiatives to protect consumer interests, increase transparency and accountability, and build trust and confidence in banks was announced in April 2016.¹ The initiatives, and their associated objectives, are:

Initiative 1: Reviewing product sales commissions and product based payments.

Objective – Strengthen the alignment of remuneration and incentives and customer outcomes.

Initiative 2: Making it easier for customers when things go wrong.

Objective – Ensure retail and small business customers have a voice and problems are resolved more efficiently. Ensure complaints are escalated and responded to within specified timeframes.

Initiative 3: Reaffirming support for employees who 'blow the whistle' on inappropriate conduct.

Objective: Promote highest standards of whistleblower protections and ensure a robust and trusted framework for whistleblowing.

Initiative 4: Removing individuals from the industry for poor conduct.

Objective: Demonstrate banks' commitment to improve practice and implement an industry register or other mechanism to identify poor conduct across all bank employees, including customer facing and non-customer facing roles, and promote good conduct and ethical behaviour.

Initiative 5: Strengthening the commitment to customers in the Code of Banking Practice.

Objective: Ensure the Code of Banking Practice adequately covers expected standards for banks and the relationship with customers, including standards for engagement between both parties.

Initiative 6: Supporting ASIC as a strong regulator.

Objective: Demonstrate banks' commitment to a well-regulated banking and financial services industry.

The ABA has advised that the overall program objectives specifically acknowledge there is a 'trust gap' in consumer expectations of banks. Moreover, the ABA has advised that the industry must, and wants to, close the gap between performance delivered by banks and expected by customers.

Under each of the industry's initiatives a number of more detailed measures have been developed, together with milestones for completion. The implementation plan is included in Appendix A.

Twenty-one of the ABA member banks have confirmed their active involvement in the package of initiatives, and are listed in Appendix B.

¹ Announced in the ABA media release on 21 April 2016 and available at <http://www.bankers.asn.au/media/media-releases/media-release-2016/banks-act-to-strengthen-community-trust>

In a reform program of this kind, sound governance arrangements are key to ensure that appropriate progress is made in implementing the initiatives, and in particular, to ensure that the industry's stated objectives of protecting consumer interests, increasing transparency and accountability, and building trust and confidence in banks remain clearly in focus. The governance structure and framework that has been put in place to oversight the implementation of the package of initiatives is outlined in my previous reports.² With completion of a number of measures, the associated Customer Advocate, Client Remediation and Whistleblower Working Groups identified in the governance structure, have been wound up.

1.2 Background to the independent review and summary of the previous reports

The ABA appointed me as an independent governance expert to report quarterly on the progress of the industry in implementing its announced package of initiatives, while at the same time maintaining a focus on the industry objectives of protecting consumer interests, increasing transparency and accountability, and building trust and confidence in banks.

The terms of my engagement are available on the ABA website.³ PwC Australia is supporting me in the execution of my responsibilities, including in the provision of secretariat functions, assistance in report preparation and with stakeholder consultation, and in the provision of senior banking industry expertise and advice in relation to industry practices and trends.

The independent governance expert review is not an audit. While I will be able to assess progress in development of the various measures, progress being made by banks will be advised by the banks or other stakeholders. Feedback provided to assist my preparation of the quarterly reports by the banks is made through the Chief Executive Officer of each bank.

My last report (Report 4) was issued on 21 April 2017⁴ and noted that with the completion of the significant independent reviews commissioned by the ABA, the implementation status of the industry initiatives has improved considerably. While there were some notable revisions to the industry's implementation plan, overall progress was largely consistent with that timeframe for those measures where the industry has control over design and implementation; however longer implementation periods were required for measures where there is reliance on statutory underpinnings. Report 4 also recognised that the industry had retained a significant commitment to achieving the program objectives, with a structured and pragmatic approach to delivery of individual initiatives. Finally, Report 4 noted that progress on developing the performance indicators had not advanced as quickly as might have been expected but it was the ABA's intention to confirm the approach for monitoring and measuring performance during this current quarter.

The next report of this review, Report 6, is scheduled to be issued by no later than 21 October 2017.

² Available at www.betterbanking.net.au

³ Available at <http://www.bankers.asn.au/media/media-releases/media-release-2016/letter-of-engagement>

⁴ Available at http://www.betterbanking.net.au/wp-content/uploads/2017/04/ABA-Report-4_Final_21-4-17-.pdf

2 Industry implementation progress

2.1 Introduction

The package of initiatives is based on measures that involve the development of industry positions or otherwise require an industry-level response. These industry-level measures are required to develop the principles, policies and/or frameworks to guide the industry and individual banks in tailoring approaches to the achievement of the industry objectives. This chapter summarises industry-level progress in this regard since the announcement of the initiatives by the ABA on 21 April 2016.

In addition to reporting on the status of the various initiatives, this chapter also summarises progress made by the industry in developing performance indicators against which the success of the initiatives can be evaluated by the industry, individual banks and stakeholders.

2.2 Revisions to the implementation plan

As mentioned in Report 4, following completion of the independent review of the Code of Banking Practice, the ABA advised that it had commenced consultations with key stakeholders, and that these would be the basis for further updates to the timetable for measures associated with Initiative 5 (Review of the Code of Banking Practice).

The ABA has now advised that the revised agreement-of-principles date for redrafting the Code will be December 2017, recognising the extensive work required to complete the redrafting and associated stakeholder consultation.

Initiative 5: Strengthening our commitment to customers in the Code of Banking Practice

Measure 5.2: Work with banks to implement changes to improve the operation of the Code of Banking Practice within their individual organisations

<i>Original agreement-of-principles date</i>	<i>Revised date for Code redraft</i>
Unspecified	December 2017
<i>Original completion date</i>	<i>Revised completion date</i>
Unspecified	Unspecified

Initiative 5 will extend beyond the original life-time of the implementation plan, which was anticipated to be December 2017. A completion date for the adoption of the new Code of Banking Practice has yet to be specified. This is understandable given specific clauses are still being settled in consultation with key stakeholders, and it will be necessary to ensure adequate transitional arrangements are in place. The ABA has also identified that it is revisiting certain issues to further strengthen commitments to customers and achieve better outcomes for customers. The ABA has advised that the completion date for the new Code of Banking Practice should be determined in time for inclusion in Report 6.

No further changes have been made to the implementation plan during this quarter.

2.3 Update on progress of initiatives

The achievement of the objectives of the industry's initiatives relies on the effective completion of a range of measures designed to enhance the industry's performance in key areas affecting customer service and stakeholder engagement. Once the industry positions have been settled, it is expected that participating banks will give effect to them by adjusting their own approaches and governance arrangements, where this is required.

The ABA published its first annual report on the package of initiatives on 2 May 2017.⁵ The annual report aimed to raise community awareness about the industry's actions to lift its performance on the path to addressing customer concerns and building trust and confidence in banks. It included background about the construction of the package of initiatives and outlined a number of themes which have gained public attention, notably in respect of the 'trust gap' that has emerged between customers and their banks. Importantly, the annual report also responded to calls for further information about the package of initiatives and greater transparency from the industry about progress and implementation of the measures.

In relation to the current quarter, set out below is an update on the status of the key measures committed to by the industry, together with commentary on any remaining steps to be taken to deliver on the various commitments.

Initiative 1: Reviewing product sales commissions and product based payments

The independent review of product sales commissions and product based payments by Mr Stephen Sedgwick AO (the 'Sedgwick Review'), was initiated to inform the development of industry policies that strengthen the alignment of remuneration and incentives with customer outcomes. The findings of the Sedgwick Review⁶ provided the industry with direction on how to improve some current remuneration practices to address the way bank staff and third party channels are paid, and to better align remuneration and incentives with customer outcomes.

This Review was also intended to inform the industry and individual banks in their development of, or refinement to, overarching principles on remuneration and incentives to support good customer outcomes and sound banking practices.⁷ This work is planned for completion by December 2017.

An initial step towards implementation of the Sedgwick Review was the convening of the Mortgage Industry Forum on 9 June 2017 to discuss the potential impacts of both the Review and ASIC's review of mortgage broker remuneration.⁸ This was attended by the ABA, along with representatives of Consumer Owned Banking Association (COBA), Finance Brokers Association of Australia (FBAA), the Mortgage and Finance Association of Australia (MFAA), and representatives from mortgage brokers, aggregators and banks. A second meeting of the Forum was held

⁵ Available at <http://www.bankers.asn.au/media/media-releases/media-release-2017/one-year-on-banks-building-a-better-banking-industry>

⁶ The Sedgwick Review was released on 19 April 2017 and is available at http://retailbankingremreview.com.au/wp-content/uploads/2017/04/FINAL_Rem-Review-Report.pdf

⁷ Development of overarching principles, informed by the industry-level guiding principles, is specified in Milestone (d) of Measure 1.2 of the implementation plan at Appendix A.

⁸ Available at <http://asic.gov.au/regulatory-resources/find-a-document/reports/rep-516-review-of-mortgage-broker-remuneration/>

on 18 July 2017, which allowed the mortgage industry to continue to identify appropriate strategies for progressing changes to payments and governance arrangements. The ABA has advised it believes this Forum will be an important vehicle for the mortgage industry to work together on these reforms and in consultation with regulators.

The ABA has noted that both representatives from mortgage brokers and the Finance Sector Union have an expectation that any reforms will happen on an aligned basis across the industry, suggesting that further consultation will be required before positions can be settled.

The ABA lodged its submission in response to ASIC's review of mortgage broker remuneration on 30 June 2017. The ABA believes there is a significant opportunity for the mortgage industry, in consultation with government and subject to any necessary regulatory approvals, to develop a self-regulatory response to change payments and governance arrangements in mortgage broking that will manage risks to consumers and promote better consumer outcomes.

The Australian Prudential Regulation Authority (APRA) is also continuing its review into risk culture and risk governance within the banking industry. The ABA understands that this review will continue through to the end of the year, with APRA considering amendments to its prudential guidance as a result of this review. Additionally, the Federal Government has announced a new Banking Executive Accountability Regime.⁹ It is expected that APRA will introduce revised prudential standards as a result of these reforms. On this basis, the ABA has advised that the industry is monitoring these government processes in relation to the development of guiding principles on remuneration and incentives. The industry notes that it will be important to make sure there is consistency across these various activities. Participant banks will continue to analyse and augment their remuneration structures based on the findings of the Sedgwick Review as well as implement changes to performance management systems and remuneration and governance arrangements across the individual banks.

Based on advice from participant banks, there are a range of views on the merits of the industry proceeding with the development of guiding principles on remuneration, given the recommendations of the Sedgwick Review, the work by individual banks to develop their own remuneration principles and the review being undertaken by APRA which is expected to give consideration to remuneration principles applying to the industry. Given the significance of this issue and the profile which remuneration has for the industry, it is clearly desirable for the industry to settle its position in relation to this matter and reflect it as appropriate in the ABA's implementation plan. Should the industry decide not proceed with the guiding principles then a clear basis for the decision should be articulated, consistent with the approach for previous variations to the implementation plan.

Initiative 2: Making it easier for customers when things go wrong

Initiative 2 comprises the following measures: establishing a customer advocate in each bank; supporting the broadening of external dispute resolution (EDR) schemes; working with ASIC to expand customer remediation programs; and evaluating the establishment of an industry-wide mandatory last resort compensation scheme. With the immediate work on expansion of customer remediation programs complete, the status of the remaining measures is as follows.

⁹ Refer to http://budget.gov.au/2017-18/content/glossies/factsheets/html/FS_Banking.htm

a) *Establishing a customer advocate in each bank*

The ABA released its *Guiding Principles – Customer Advocate* on 30 September 2016, and all but one participant bank¹⁰ have advised they now have a customer advocate in place. The Better Banking website includes a list of the customer advocates in each bank.¹¹

The ABA has continued to work with the participating banks to provide informal implementation guidance, primarily related to the requirement of achieving sufficient separation of the customer advocate from business units within the bank, and how this can practically be done in the smaller participating banks to ensure the underlying intent is achieved and the needs of customers and the business are met.

The ABA has worked with the participating banks, in particular the non-major banks, to determine the nature of revision required to the Guiding Principles, in order to reflect these practical considerations. Revised Guiding Principles were issued by the ABA on 18 July 2017¹² making it clear that smaller banks may identify better options for introducing a dedicated customer advocate which recognises the low numbers of customer complaints and/or the nature, size, or business structure of the bank. For example, a bank may decide that an existing resource with dedicated time but not available on a full-time basis or alternatively a part-time resource or a resource also responsible for external dispute resolution assistance would provide the best service for their customers. If banks choose to implement this way, the role should continue to have separation from business units within the bank so as not to undermine the intent of the Guiding Principles.

A new Customer Advocate Forum has been established for the bank-appointed customer advocates in order to discuss implementation issues relating to the Guiding Principles and the role of the customer advocates. One matter that has been raised at the Forum was in relation to performance indicators. The Guiding Principles included provision for the development of mechanisms to measure the effectiveness of the customer advocate, as well as external public reporting on the outcomes of the customer advocate function.¹³

The ABA has advised that the customer advocates are considering how best to fulfil this reporting requirement, including the question of whether a standardised measure could be developed, noting the differences in the way the customer advocate function has been implemented.

b) *Supporting the broadening of external dispute resolution schemes*

The original implementation plan had anticipated adoption of the new EDR scheme by June 2017. This forecast was made when the Treasury's review of the financial system external dispute resolution framework ('Ramsay Review') was expected to be completed by December 2016.

¹⁰ Bank of Sydney – see footnote 26 in Chapter 3

¹¹ Refer to <http://www.betterbanking.net.au/better-service/getting-problems-fixed/>

¹² Refer to <http://www.bankers.asn.au/Small-business/Industry-Standards>

¹³ Refer to <http://www.betterbanking.net.au/wp-content/uploads/2017/01/ABA-Customer-Advocate-Guiding-Principles-FINAL-1.pdf>

The final report of the Ramsay Review was released on 9 May 2017.¹⁴ The key recommendations included:

- Establishment of a single EDR body for all financial disputes;
- Enhancing access to redress for consumers, including higher monetary limits and compensation caps;
- Enhancing access to redress for small business;
- Increased ASIC oversight of the single EDR body; and
- Transparency, through reporting to ASIC in a standardised form on banks internal dispute resolution activity.

As part of the 2017 Federal Budget,¹⁵ the Australian Government announced the establishment of the Australian Financial Complaints Authority (AFCA), adopting key recommendations of the Ramsay Review for a single complaints handling body. This organisation will commence from 1 July 2018. The Budget announcement also proposed the development of a standard definition of complaints to assist in reporting of internal dispute resolution data to ASIC.

The ABA lodged its submission on the Treasury consultation paper on the new external dispute resolution and complaints framework on 19 June 2017. The ABA supports the establishment of AFCA by adopting the existing infrastructure and systems to minimise disruption for consumers and financial service providers, but considers that the creation of the Ministerial authorisation process and ASIC directions power should not unduly inhibit or interfere with complaints determinations and proper decision making and administration. The ABA also supports the new requirements for financial services providers to report on their internal dispute resolution activity in a standardised form. In addition, the ABA considers that the design should avoid unnecessary duplication and compliance costs, and ensure identification of emerging risks and key issues that impact customer outcomes at an industry level.

c) Evaluating the establishment of an industry wide mandatory last resort compensation scheme

The Ramsay Review requested submissions on matters related both to a compensation scheme of last resort and to access to redress for past disputes, with a closing date of 28 June 2017. These submissions will assist the Ramsay Review in preparing a Supplementary Final Report to the Government during the second half of 2017.

The ABA has lodged a submission and continues to advocate for a mandatory, prospective last resort compensation scheme for financial advice, although is aware that other industry associations and stakeholders are taking a different view. The ABA has noted that this fragmentation risks further delaying progress on this measure. Accordingly, there will be considerable interest in the Ramsay Review's forthcoming position on this matter, as well as in the Government's response.

¹⁴ Available at <http://treasury.gov.au/ConsultationsandReviews/Reviews/2016/Review-into-Dispute-Resolution-and-Complaints-Framework/Final-Report>

¹⁵ Refer to http://budget.gov.au/2017-18/content/bp2/download/bp2_expense.pdf

Initiative 3: Reaffirming support for employees who 'blow the whistle' on inappropriate conduct

This initiative reflects the industry's commitment to establishing the highest standards of whistleblower protections by ensuring there is a robust and trusted framework for escalating concerns. Accordingly, protection of whistleblowers, including independent support and protection against financial disadvantage, is expected to be standardised across banks. The ABA published *Guiding Principles – Improving Protections for Whistleblowers* on 21 December 2016,¹⁶ which the participant banks have now adopted.

Similar to the Customer Advocate Forum, the ABA has advised that the participating banks have committed to establishing a Whistleblower Forum in order to “provide a network for banks to share implementation experiences” and discuss approaches to developing standardised measures to monitor the effectiveness of the program. The Guiding Principles included provision for the development of mechanisms to measure the effectiveness of whistleblower programs, as well as external public reporting on the outcomes of the whistleblower protections.

The report on the findings of the Parliamentary Joint Committee on Corporations and Financial Services into whistleblower protections in the corporate, public and not-for-profit sectors, originally due to be released on 30 June 2017, is now expected to be released in mid-August 2017. The ABA intends to review this report and revisit its Guiding Principles as appropriate.

Initiative 4: Removing individuals from the industry for poor conduct

The objective of this initiative was to demonstrate banks' commitment to improve practice and implement an industry register or other mechanism to identify poor conduct across all bank employees, including customer facing and non-customer facing roles, and promote good conduct and ethical behaviour. The development of an industry register, as a mechanism to improve recruitment practices and decisions in the banking industry, is one of the more difficult measures to implement given the legal issues involved and as such is contingent on some form of statutory underpinning. As an interim measure, the ABA and the banks have redirected resources into further advancing the development of a new *Conduct Background Check Protocol* for bank employees (the 'Protocol').

The ABA published the Protocol on 9 June 2017¹⁷ for adoption by participant banks. Major banks have adopted the Protocol as of 1 July 2017, with the majority of non-major banks committing to its adoption by 1 October 2017.¹⁸ In development of the Protocol, the ABA has consulted with key stakeholders, including ASIC, the Finance Sector Union and the Office of the Australian Information Commissioner.

The Protocol specifies fact-based questions about whether the prospective employee is subject to an ongoing misconduct investigation, or was dismissed or resigned in specific circumstances relating to misconduct.

¹⁶ Refer to http://www.betterbanking.net.au/wp-content/uploads/Final_Whistleblower_Guiding_Principles-Dec-2016.pdf

¹⁷ Available at <http://www.betterbanking.net.au/better-culture/stopping-poor-conduct/>

¹⁸ At the time of preparation of this report, the ABA advised that the following non-major banks have not yet committed to adoption by 1 October 2017: Bank of Sydney, Citigroup and Defence Bank. AMP has advised it will adopt the Protocol by January 2018.

The Protocol sets minimum standards for subscribing banks ('subscribers') regarding:

- A reciprocal obligation for subscribers to request the Conduct Background Check for prospective employees, and to respond to those requests for current employees and former employees who worked for the subscriber at any time within the request period;
- Standard format, process and timeframes for requesting and responding to Conduct Background Checks;
- Fact-based Conduct Background Check questions; and
- Related record keeping and confidentiality obligations.

These elements are intended to supplement existing recruitment processes. As stated by the Protocol, "it does not specify processes or outcomes relating to appointing prospective employees, other than the requirements for the Conduct Background Check, and subscribers acknowledge their legal obligation not to enter into any arrangement or understanding with each other about those matters."

The ABA has advised that the development of an industry register is still being investigated, however resources this quarter have been primarily directed to the delivery of the *Conduct Background Check Protocol*. A post-implementation review is to be conducted by 30 June 2018, including engagement with banks, regulators and other stakeholders to ensure the Protocol is operating as intended.

Initiative 5: Strengthening the commitment to customers in the Code of Banking Practice

The objective of this initiative is to ensure the Code of Banking Practice adequately covers expected standards for banks and the relationship with customers, including standards for engagement between both parties.

With completion of the independent review by Mr Philip Khoury (the 'Khoury Review'), the ABA has now appointed a team of external consultants to work with the ABA on redrafting the Code. External consultants' skills include project management, policy advice, consumer-friendly writing and editing, legal advice, consumer testing and design. The ABA has also advised that it has:

- Prepared an extensive project plan covering the various stages of the Code redraft process;
- Commenced engagement with key stakeholders on the industry's position in relation to recommendations of the Khoury Review, including liaising with ASIC on the process for its approval of the revised Code and the Code Compliance Monitoring Committee (CCMC) on its role and mandate; and
- Completed an intense series of workshops with banks on the industry's position, including revisiting more complex recommendations.

The ABA published a quarterly update on the Code redraft on 30 June 2017.¹⁹ In the industry response, the industry committed to making sure stakeholders and the public are updated on progress. The next quarterly update is due to be published by 30 September 2017.

The ABA has acknowledged that having a new Code of Banking Practice by 31 December 2017 is an ambitious target, particularly given the breadth of the

¹⁹ Refer to <http://www.bankers.asn.au/media/media-releases/media-release-2017/new-customer-focused-bank-code-on-the-way>

changes required and the level of stakeholder engagement to meet community expectations; and this needs to be balanced with the reputational risks to the industry in taking too long to make the required changes.

Initiative 6: Supporting ASIC as a strong regulator

To demonstrate banks' commitment to a well-regulated banking and financial services industry, the industry committed to supporting ASIC as a strong regulator. This comprises working with Government and ASIC to implement a 'user pays' industry funding model to enhance the ability of the regulator to investigate matters brought to its attention. In addition the industry also indicated its intention to work with ASIC to enhance the current breach reporting framework to provide more consistency in how its regulatory guidance is interpreted.

On 20 April 2016, the Government announced that it would introduce an industry funding model for ASIC, commencing in the second half of 2017. The Government released draft regulations for consultation in May seeking feedback on the mechanisms to be used to calculate the levies payable by each class of regulated entity in each financial year. The *ASIC Supervisory Cost Recovery Levy Regulations 2017* received Royal Assent on 19 June 2017.²⁰

The ABA lodged its submission on the ASIC Enforcement Review Taskforce's consultation paper on self-reporting of contraventions by financial services and credit licensees on 29 May 2017. The consultation paper proposes:²¹

- Clarifying when a reporting obligation is triggered - reducing compliance costs and delays in reporting, and removing uncertainty about when and whether a reporting obligation exists in the circumstances;
- Increasing accountability for financial services licensees, and their employees and representatives by expanding the class of reports that must be made to expressly include misconduct by individual advisers and employees;
- Introducing new and heightened penalties for non-reporting, giving ASIC greater flexibility to impose a range of penalties in response to a failure to report;
- Requiring ASIC to publish data on breach reports for major licensees; and
- Introducing an equivalent reporting regime for credit licensees (which are currently subject only to annual compliance reporting).

The ABA supports reforms to the breach reporting framework to ensure accountability and transparency, protect consumer protection, enable identification of emerging issues and risks, and support ASIC to meet its law enforcement objectives.

The ABA has advised it believes the review of the breach reporting framework is an opportunity to address concerns regarding potential under-reporting or delayed reporting of significant breaches and to clarify self-reporting obligations and improve and standardise breach reporting practices across the financial services industry. The ABA has also advised that it continues to monitor developments in this area.

²⁰ Available at <https://www.legislation.gov.au/Details/C2017A00043>

²¹ Refer to <http://www.treasury.gov.au/ConsultationsandReviews/Reviews/2016/ASIC-Enforcement-Review/Completed-Consultation>

Overall progress

The current status of measures supporting each initiative is summarised in Figure 1 below, with a comparison to the status reported in Report 4 (R4). An additional trackable measure for the agreement-of-principles phase²² has been added to the plan as outlined in Section 2.2. Further information is provided in the implementation plan at Appendix A.

Figure 1: Implementation status of the trackable measures²³

Milestone Status	Planning		Agreement of Principles		Complete Implementation	
	R5	R4	R5	R4	R5	R4
Complete	13	10	10	9	6	3
On track	-	3	-	1	1	3
On alert	-	-	3	2	2	2
Date not yet specified	-	-	-	1	1	1
Next phase reliant on government	-	-	-	-	3	4
Total	13	13	13	13	13	13

Aside from those measures where the next phases are reliant on government processes, the initiatives not yet finalised are:

- Initiative 1 (Reviewing product sales commissions and product based payments): Measure 1.2 (Each bank commits to ensure it has overarching principles on remuneration and incentives to support good customer outcomes and sound banking practices) and Measure 1.3 (Work with regulators to implement changes and, where necessary, seek regulatory approval and legislative reform) are still in the agreement-of-principles phase and continue to be on alert given the complexity of implementation for some banks. This initiative is scheduled for completion by December 2017;
- Initiative 4 (Removing individuals from the industry for poor conduct): With the publication of the *Conduct Background Check Protocol* and its implementation by the major banks, adoption by the non-major banks by 1 October 2017 is the only remaining activity outstanding for the industry to complete this initiative under the revised implementation plan (as explained in Report 4); and
- Initiative 5 (Review of the Code of Banking Practice): With the planning measures completed, work on redrafting the Code of Banking Practice is under way. This is the only remaining agreement-of-principles milestone remaining for this initiative. As noted in Section 2.2, this milestone step is due for completion by 31 December 2017, with the ABA yet to specify a target date for the complete-implementation phase.

²² As the ABA has now set a date for the agreement-of-principles phase for Measure 5.2 as specified in Section 2.2, an additional trackable measure has been added to Figure 1.

²³ Quantification and summary status of milestones is based on the information outlined in the implementation plan contained in Appendix A.

Longer implementation periods are required for the limited number of measures where there is reliance on statutory underpinnings.

2.4 Update on development of performance indicators

As mentioned in Report 3, senior leadership within the banks has acknowledged the need for performance indicators to assess the performance of the package of industry initiatives in driving behavioural change and in having a positive and sustained impact for customers. Against this background, the ABA has progressed the development of industry-level performance indicators to be able to measure and assess the impact that the initiatives have in meeting the industry's high-level objective of improving trust and confidence in banks. In addition, performance indicators are being developed to measure the effectiveness of the adoption of new or revised customer advocate and whistleblowing arrangements by all banks.

The primary method of assessment will be through consumer and employee surveys, supplemented with external complaint data from the Financial Ombudsman Service (FOS) and qualitative commentary collected from the participant banks.

Specifically, the survey tools will seek to:

- Evaluate the success of the banking reform program initiatives;
- Understand consumer interests and priorities;
- Understand consumer personal experience and perceptions of banks;
- Explore key factors driving consumers' experience, perceptions and knowledge;
- Measure perceptions of initiatives relevant to bank employees (including Whistleblower and changes to the use of product sales commissions); and
- Assess the correlation between consumers and bank employees' perceptions of the initiatives.

The ABA is seeking to survey 1,000 consumers and 1,000 employees across all participating banks. The first report on consumer sentiment is expected to be published by the end of July 2017. Incorporation of employee responses into the industry-level performance indicators is expected to take place by the end of December 2017, with publication in early 2018. Once the reporting framework is constructed, the ABA has advised that the industry will decide on ongoing research and reporting, including frequency.

In addition to providing an overall trust and confidence rating, regression modelling will be used to identify the specific factors contributing to overall satisfaction with banks and the industry's performance relating to trust, transparency and confidence. The ABA has advised this will minimise the likelihood of misleading correlations being made between any change (positive or negative) and the implementation of the initiatives. The research is also being set in the context of the Trust Barometer, which has been developed by Edelman and conducted annually since 2012.²⁴

As noted above, work is also being progressed by the participant banks in defining performance indicators associated with the customer advocate role, as well as

²⁴ Available at <http://www.edelman.com/trust2017/>

performance indicators to assess the effectiveness of revised whistleblower policies. In relation to the customer advocate function in particular, the banks are working through the challenge of developing a standardised measure across all banks, given differences in the way the customer advocate function has been implemented. The development of a common definition of complaints, announced by the Government as part of its recent budget measures, may go some way in addressing this matter.

To date, the industry has focused on putting in place the industry-level reporting framework and has not been explicit about its intentions around public reporting by individual banks against the performance indicators developed to measure trust and confidence over time. It would be desirable for the industry to be clear on its position going forward, and even better if the major banks²⁵ were to show the way in reporting their results, with other banks considering such reporting where relevant and reliable information is attainable in a cost-effective manner. This would be consistent with the industry's goal of increasing transparency, which was a key objective in the ABA's original announcement of 21 April 2016.

Importantly, better public reporting during the period that the industry reforms are being bedded down is likely to lead to better outcomes for customers given the competitive nature of the industry and the evident desire on the part of all banks consulted to raise the standards of customer service.

In their responses to this review, many banks are still considering their position, one of the banks has indicated it is awaiting guidance on individual bank reporting by the ABA, and at least one of the major banks is planning to report their bank's performance in relation to the industry indicators. There is a general recognition that increasing transparency is an important way to build trust but, given this is new territory, most banks are looking to gain a deeper understanding of the issues and costs before committing at this time. It is worth saying also that decisions to publish specific indicators should not be viewed as being in place forever and reasonably should be subject to periodic review.

2.5 Concluding remarks

Over this quarter the industry has continued to make good progress in completing a number of measures, against the backdrop of a rapidly evolving industry landscape. It is encouraging to see work progressing on the initiatives where the industry has control over design and implementation, including in relation to the review of product sales commissions and the redraft of the Code of Banking Practice. As a consequence, the reform program is well advanced with many initiatives having moved from design to implementation phases. While there is still work to be done to complete some of the measures, the focus going forward will increasingly be on the efforts of individual banks to embed the reform measures to the extent required to deliver on the goals of the six industry initiatives.

As the regulatory and broader landscape becomes clearer, it will be important for the ABA to continue to develop and/or refine industry guidance to individual banks in order to allow them to refine their approaches, where required, to achieve improvements in both outcomes and efficiency. This will be particularly helpful for the smaller banks, where for example, the *Guiding Principles – Customer Advocate* have been modified recently to cater for circumstances where the volume of complaints does not justify a dedicated customer advocate position as envisaged by the initial version of the *Guiding Principles*. While there is still a range of views from the banks on the merits of the industry proceeding with the development of

²⁵ Major banks account for greater than 80% of both total gross loans and advances, and total deposit based on APRA statistical collections (for 2017).

guiding principles on remuneration and incentives, in the months ahead it is clearly desirable for the industry to settle its position in relation to this matter and reflect it, as appropriate, in the ABA's implementation plan.

Being able to measure, assess and report progress being made by the industry and individual banks against the goals of the initiatives is important for both the industry and stakeholders. It will contribute to the building of trust by the industry and may highlight areas where there are opportunities for improvements to be made in pursuit of better outcomes. During the last quarter, it has been encouraging to see tangible work being progressed in the development of industry-level performance indicators. The ABA has appointed Edelman Intelligence to measure the outcomes of the reform program at an industry-level with the expectation that the first wave of consumer research will be published shortly after the release of this report. A second wave of research, incorporating the perspectives of both consumers and bank employees, is expected to be published early in 2018. The industry is to be commended for directly seeking to measure its performance in terms of its high-level objectives for its reform program, and its willingness to publish this information. That said, as indicated above, going forward it would be desirable for the industry to be clear in relation to its expectations about the public reporting expected by individual banks against the performance indicators developed.

In all, good progress has been made by the industry and there is sound reason to expect this to continue given the early benefits that are already showing, as explained further in the next chapter.

3 Implementation by the banks

3.1 Introduction

This chapter outlines the progress made by the 21 participating banks in implementing the various measures for which they are individually responsible.

Consistent with previous reports, feedback was requested from those participating banks on:

- The status of the measures (or actions) that will contribute to the nominated initiative;
- The work planned for the next three months; and
- The current judgement as to any significant risks in achieving the objectives of the initiative, and appropriate mitigants.

All participating banks responded to this request for information. In addition to their implementation status, banks were invited to submit case studies that demonstrated specific actions being taken to address the objectives of the initiatives or otherwise inform banks of implementation issues. Selected responses are included in this chapter.

3.2 Progress on initiatives

As the industry has completed, or progressed to an advanced stage, the various measures designed to provide the platform for the achievement of the goals of the various initiatives, the focus is increasingly turning to the steps being taken by individual banks to implement the revised industry approaches. This has required in many cases consideration of the best approaches to achieve the desired goals and additional resources to give effect to the required program of change, particularly in respect of changes proposed by the Sedgwick and Khoury Reviews.

Australia and New Zealand Banking Group (ANZ) has summarised the project governance measures it has put in place to effect change arising from the industry reforms and broader regulatory agenda. The approach adopted is outlined in Case Study A.

Case Study A: Governance frameworks to effect change

ANZ has introduced a program structure with governance and resources to oversee implementation of the large number of commitments banks have made under the industry reform program (e.g. Khoury Review and subsequent development of a new Code of Banking Practice, Sedgwick Review) and broader regulatory agenda, such as the House of Representatives Economics Committee review of the major banks and Budget announcements. These all require implementation over the next 12-24 months. The work program will report to the Group Executive, Australia Division and his leadership team.

Implementation ownership and reporting structures are in place to ensure heads of business units have assigned resources to assess impacts of the expected changes on current business processes, identify linkages with ongoing projects, and deliver the commitment on time.

Priority has been given to those changes that need to be completed first (e.g. changes to small business lending contracts arising from the Carnell Inquiry) and those requiring long lead times to implement.

A number of the banks have commented on the importance of focusing resources on program and governance structures in order to coordinate the implementation of the various initiatives, along with the significant demands of government and regulatory processes. The cost and resourcing demands on the smaller banks have been particularly emphasised, with one bank advising that this has been an extremely busy quarter requiring a significant investment in time and resources in these industry-led initiatives, as well as the Government's extensive regulatory reform agenda, but good progress has been made. This has been a consistent message from the smaller banks that have advised they are moving ahead in implementation of the various measures, with the major banks passing on their experience and providing guidance where this may assist. This level of engagement among the participating banks to achieve the industry objectives, despite the resource demands, is a positive sign of the level of commitment to the reform program.

Initiative 1: Reviewing product sales commissions and product based payments

There is a spectrum of responses across the participant banks in relation to the implementation of the Sedgwick Review which focused on reviewing product sales commissions and other product based payments. Some banks moved early in advance of the final report to adjust remuneration structures, while others have waited for the release of the review's findings to analyse the impact on their business prior to making any changes. All participant banks have confirmed they will be in a position to have fully addressed the recommendations of the Sedgwick Review by the performance year commencing 2020, the end-date for adoption of the revised approach recommended by Mr Sedgwick.

Many of the banks have either implemented, or are investigating the implementation of a balanced scorecard approach to performance evaluation. In this context many banks have increased the weighting of customer measures and reduced the weight of financial measures in the design of incentive arrangements, consistent with the recommendations of the Sedgwick Review. One bank saw the main risk arising from the changes as being the loss of high performing employees who may opt to leave the organisation, and indeed the industry, and indicated the mitigation here was engagement with their employees as part of the change program. A small number of banks have indicated that product sales commissions or product based payments in respect of retail banking products are not provided, and as a result no changes to policies are required.

The Commonwealth Bank has provided an example of how it has modified its remuneration arrangements to increase focus on the bank's customers. This is outlined in Case Study B.

Case Study B: Product sales commissions and product based payments

At Commonwealth Bank, we believe our employees are critical to securing and enhancing the financial wellbeing of communities and customers. It has been important, therefore, that the way we motivate, recognise and reward our employees supports them to deliver exceptional customer service and outcomes and reduces any potential or perceived conflicts of interest.

In recent years we have refined our people management practices, performance management, and remuneration to ensure we have a strong culture focused on delivering good outcomes for our customers. As an example in our Retail Banking Services division we have moved away from incentives linked to product sales and moved towards team based incentives for our frontline branch staff.

Our longer term focus on customer service and satisfaction has meant that we have been able to implement many of the recommendations made by Mr Stephen Sedgwick AO in his review of retail banking remuneration by 1 July this year. We will have all changes in place by the following financial year. One of the changes we are implementing from 1 July is a new variable remuneration scheme for all our lenders in the Retail Banking Services Division.

The new scheme has completely removed any financial targets as a prerequisite to receiving a variable incentive, with the best performing and recognised lenders being those who can demonstrate a focus on customer needs and satisfaction. Lenders who participated in the year-long pilot reported having greater role clarity and felt there was a strong emphasis on customer conversations and outcomes. The changes to our lender incentive scheme reinforces our commitment to adopting the Sedgwick Review recommendations in full and supports our focus on fostering a culture that recognises and rewards our people for meeting customer needs.

We are serious about doing the right thing by our customers and will continue to ensure our retail bank employees and leaders have the training and support to meet our customers' needs.

Some banks have mentioned that the changes being adopted in the light of the Sedgwick Review impact on a number of business units and, as such, programs of work are underway to ensure appropriate alignment and consistency is achieved. Plans are being socialised with responsible managers and staff; and training to enhance the understanding of broader incentive and management tools is being scheduled so the changes can be understood in the spirit of the reform. One participant bank has highlighted the awareness campaign it is conducting across its senior leadership team to enhance the understanding of the potential behavioural impacts of the use of targets, as highlighted by the Sedgwick Review. Extending further, another bank has flagged its intention to examine workplace culture in its retail operations. Positively, too, mention has been made of the implementation of improved governance and oversight arrangements of remuneration policies at Board level.

These actions show that many banks are taking a broad view of the changes that may beneficially be adopted in the light of the industry reforms, and leveraging from the insights and stimulus provided by the Sedgwick Review to lay the groundwork for the provision of better services to customers.

Initiative 2: Making it easier for customers when things go wrong

In accordance with the implementation plan, all but one of the participating banks have now confirmed that customer advocates are in place, and operating in accordance with the ABA's *Guiding Principles – Customer Advocate*.²⁶ As outlined in Section 2.3, the ABA has updated these Guiding Principles to make it clear that smaller banks may identify better options for introducing a dedicated customer advocate which recognises the low numbers of customer complaints and/or the nature, size, or business structure of the bank.

Westpac Banking Corporation (Westpac) has highlighted an example of the work being undertaken by their customer advocate in Case Study C.

Case Study C: Work of the customer advocate

A matter was referred to the customer advocate regarding FOS making a determination accepting some, but not all, of our customer's claims.

Our customer, for whom English was a second language and who was elderly, did not accept FOS' determination and in line with standard policy both FOS and the Bank closed their files. In hindsight it appears that the customer did not fully understand the FOS process and upon review by the Customer Advocate we decided that the matters the subject of the determination against the bank should be implemented where possible. This was the case even though the FOS file had been closed and, because of the customer's action, there was no FOS binding obligation on us to implement the findings.

As a result of this review Westpac's approach has been refreshed to ensure that customers are aware of FOS determinations in their favour and, when appropriate, we will act on FOS determinations, even if not accepted by the customer. This will be the case particularly where it involves a vulnerable customer.

Many of the banks commented on the positive impact which the customer advocates are having already. This seems to be particularly the case where the customer advocate is taking a proactive role in identifying thematic issues and then encouraging actions within the bank to prevent recurrence. This role is reinforcing a more customer-centric approach by the banks while seeking to gain down-stream efficiencies by adopting preventative measures. To illustrate, one bank has begun identifying trends and opportunities for continuous improvement in the complaints review process, and going forward plans to complete a review of 150 closed complaints relating to small business issues to identify themes and process improvement opportunities; another is planning to roll out a 'Customer Feedback Training' module to staff commencing this month; and another has arranged for the Customer Advocate to present to the bank's Board meeting along with a Q&A session with Directors on improving customer experience. An early observation conveyed by one bank on the customer experience, from customers that have chosen to go through the Customer Advocate review, is that customers have expressed appreciation for the involvement of the customer advocate.

As noted in Section 2.2, the banks' customer advocates have formed the Customer Advocate Forum as a mechanism to share experiences and to drive further the benefits of the customer advocates for better customer outcomes.

The adoption of customer advocates by 20 of the participating banks has been one of the standout changes that has assisted customers in navigating the complaints handling process and when appropriate helping customers with specific issues, and

²⁶ Bank of Sydney has stated that it supports the customer advocate initiative and already has elements of the guiding principles in place within existing functions; the bank is committed to formal adoption of the guiding principles and is incorporating this in the review of their entire complaints process, which is currently underway.

assisted the banks to improve their processes to reduce the incidence of poor outcomes. The sharing of experience and information within the banks and, as appropriate, within the industry is a good sign that the banks have begun to make it easier for customers when things go wrong.

In addition to their work in implementing the customer advocate function, the banks have also been contributing to the Ramsay Review, and its extended consultation period on a last resort compensation scheme. Contributions are also ongoing with respect to EDR, particularly in light of the announcement of the establishment of the AFCA, and this is expected to continue.

Initiative 3: Reaffirming support for employees who 'blow the whistle' on inappropriate conduct

The ABA's *Guiding Principles – Improving Protections for Whistleblowers* was scheduled to be adopted by all participant banks by 30 June 2017. All participating banks have confirmed that a policy consistent with the Guiding Principles, or requiring little amendment, is now in place.²⁷

A number of the banks observed that a critical success factor in the effective implementation of their whistleblower policies is that these policies are clear and accessible to all staff. In their submissions, a majority of the banks have reported a focus on communications and training in order to promote awareness and to encourage staff to 'speak up'.

National Australia Bank (NAB) has provided information on its pilot program to raise awareness of the whistleblower policy, and support employees in speaking up, in Case Study D.

Case Study D: Champions - Putting Heart and Soul into NAB's Whistleblower Program

NAB is currently piloting a Whistleblower Champion network in its retail division as part of the process of bringing the revised Whistleblower Protection Policy to life.

The Whistleblower Program worked with the retail division to identify the appropriate number and location of whistleblower champions, recognising the need to ensure appropriate coverage and staff accessibility. Whistleblower Champions were recently appointed on the basis they demonstrated an appropriate level of authority, are trusted in their business, are approachable, model NAB values, and demonstrated a genuine interest in promoting the Whistleblower Program.

Whistleblower Champions are already playing a critical role in demonstrating NAB's commitment to supporting whistleblower by:

- Acting as high profile advocates of the Whistleblower Program, promoting a culture of 'speaking up' amongst employees
- Increasing the visibility of the Whistleblower Program and helping employees to feel more comfortable and willing to raise concerns
- Educating employees on how they can make a whistleblower disclosure and the protections they will be afforded.

Importantly, it is not the role of Whistleblower Champions to receive disclosures or commence/run an investigation.

²⁷ Defence Bank has advised that the bank's whistleblower policy has not been amended as the existing policy was broadly in line with the Guiding Principles.

Case Study D: Champions - Putting Heart and Soul into NAB's Whistleblower Program (continued)

Our Whistleblower Champions are now fully trained and have undertaken a number of awareness raising initiatives, including:

- Running whistleblower awareness sessions at leaders days across the retail network
- Promoting the responsibility of leaders to ensure their staff know how to raise concerns in the workplace
- Promoting staff participation in independent whistleblower research led by Griffiths University
- Developing communication strategies tailored to staff and channels in the retail network
- Developing a poster to raise awareness of whistleblowing in the retail network.

The Whistleblowing Program will assess the success of the pilot (after 6 months) and determine any opportunities for improvement before rolling the concept out in other parts of the bank. In time, we anticipate a bank-wide network of Whistleblower Champions, each acting as high profile whistleblowing advocates and together promoting a culture of 'speaking up' amongst NAB employees.

One participating bank stated that, along with the accessibility of the policy, tone-at-the-top is critical, requiring frequent and high visibility senior executive communication as to the value and criticality of 'speaking up'.

In this regard, it was positive to note that a number of banks reported the active engagement of their Executive Committees and/or Boards on matters concerned with the implementation of the Guiding Principles.

As noted in Section 2.2, the establishment of the Whistleblower Forum among the participating banks is expected to progress the development of suitable performance indicators in order for the effectiveness of the whistleblowing policies to be assessed.

Initiative 4: Removing individuals from the industry for poor conduct

All major banks have adopted the *Conduct Background Check Protocol* as of 1 July 2017, with the majority²⁸ of non-major banks committing to its adoption by 1 October 2017. This timetable is ahead of the planned implementation deadline of December 2017.

One bank has advised that it cannot adopt the Protocol in its current form, citing concern over legal risks in the absence of legislative backing. That bank has nevertheless indicated it endorses and supports the broader intent of the Protocol.

A number of the participating banks have also raised a concern around the 'uneven application' of the Protocol. As stated in the Protocol:

"Subscribers who are part of a corporate group with significant parts of the corporate group not involved in retail banking business may choose to apply the protocol only to those Employees involved in the provision of banking services or the banking business of the group generally."

²⁸ At the time of preparation of this report, the ABA advised that the following non-major banks have not yet committed to adoption by 1 October 2017: Bank of Sydney, Citigroup and Defence Bank. AMP has advised it will adopt the Protocol by January 2018.

The ABA has acknowledged this operational risk, but has stressed the objective of this initiative needs to be contained to retail banking, particularly at this stage, in order to maximise the number of subscribers, noting the reform program was targeted at retail banks. A post-implementation review is scheduled to be conducted in relation to this measure before 30 June 2018.

Initiative 5: Strengthening the commitment to customers in the Code of Banking Practice

Fifteen of the participant banks have confirmed they are taking an active role in the ABA's working group supporting the Code of Banking Practice redraft. This includes one bank which is not yet a signatory to the existing Code. Many of the participating banks acknowledge the scale and complexity of the task of redrafting the Code in line with the recommendations of the Khoury Review, a task that is further complicated by potential overlaps with the current legislative and regulatory programs.

Specific reference was made to timing pressure which will come from seeking to settle the Code's independent oversight arrangements and submitting the Code for ASIC approval; and may also arise from additional content arising from other parallel developments e.g., the Small Business Loans Inquiry ('Carnell Inquiry') and credit card reforms announced in the Federal Budget. Participant banks recognise that the timeframe for the Code redraft is ambitious, but nevertheless have indicated that they are devoting significant resources to progress the redrafting and manage the risks, to the extent possible.

ING Direct (ING) has taken practical early steps to implement some of the findings from the Khoury Review, ahead of the Code redraft. This early work is illustrated in Case Study E.

Case Study E: Early steps to implement recommendations of Khoury Review

ING has introduced a process to cancel card recurring payment arrangements (Khoury - Recommendation 60)²⁹

We listened to our customer and in line with our Orange Code behaviours of 'making it our business to be a step ahead by understanding our customers' needs and providing solutions and helping others to be successful by listening and responding to the needs of our customers', we have signed up to the card scheme service to provide a solution to stop recurring payments (in certain situations) for our customers. While the scheme charges ING on a 'per transaction' basis, ING does not pass this fee to the customer – so the process is seamless and free to the customer.

ING's ability to make this change to benefit the customer is in part a function of our simpler operating model, including because we do not issue cards from all providers and also that we do not 'acquire' card transactions on behalf of business customers. Current limitations imposed by the card schemes would have made it much harder to find an appropriate customer solution if ING did not have our simple business model.

Against this background, and given the Khoury recommendation 60, the banking industry may need to take this opportunity to work further with the card schemes to develop an end-to-end process.

As the ABA and the banks step through the process of redrafting the Code, there will be judgements to be made to ensure consumer interests are properly protected. By the same token, it is not just a one-way street.

²⁹ Khoury Review, Recommendation 60: "Signatory banks should work with card scheme companies to build functionality and processes to enable signatory banks to carry out customer requests to cancel recurring card payment arrangements. The aim should be to put this in place within two years."

My discussions during the course of this review process have also emphasised the nature of the banker-customer relationship being two-way, with both banks and customers each having separate responsibilities. It is important that customers recognise that they must also carry responsibility for protecting their own interests. This of course applies to all commercial and contractual dealings by individuals, regardless of which industry they are dealing with. But just as the fact that banking decisions may be complex, long-lasting and involve significant amounts of money means that the onus on banks should be high, so too those same factors underline the importance of customers taking particular care and diligence in banking transactions.

It is in customers' best interests to research, engage and question to inform themselves about the products or services they are considering from a bank. In short, customers need to have their eyes wide-open when pursuing significant transactions with a bank to obtain cost-effective outcomes across the range of products and services provided to them. This is a personal responsibility. The flip-side is that customers should not be shy about asking direct questions of their banks about whether they are getting the best possible deal.

None of this detracts from the responsibility of banks to do the right thing, and is critical context and intent for the redrafting of the Code. As Mr Khoury said in his review, the Code is “a promise by the banks to the community”.³⁰

The proposed amendments to the Code of Banking Practice will provide a higher degree of protection for consumers; the full benefits of this will only accrue if consumers recognise their own responsibility to be diligent in informing themselves of, and protecting, their interests.

Initiative 6: Supporting ASIC as a strong regulator

Participant banks have been active contributors to ASIC's Enforcement Review, with a number making public submissions or undertaking consultations with Treasury and ASIC prior to the closure of submissions on 12 May 2017. One bank has indicated that it is taking early steps to undertake a comprehensive review of its breach reporting processes in order to streamline breach and incident management, while another has made improvements to centralise collection and monitoring of breaches and incidents.

In relation to ASIC's Industry Funding Model, a number of the banks have stated that they are working through the potential implications based on the recently published Regulations.³¹

³⁰ Independent Review of the Code of Banking Practice, 2017, Mr Philip Khoury, page 5

³¹ ASIC Supervisory Cost Recovery Levy Regulations 2017

3.3 Concluding remarks

This has been another productive quarter in which participant banks continue to make good progress in implementing measures under the initiatives.

Importantly, this quarter is the first where the positive impact flowing to individual customers through some of these initiatives is clearly visible. In particular, there has been quite a common theme from banks around the impact of the newly appointed customer advocates. A specific example of this is given in Case Study C.

More generally, consultations with bank Chief Executive Officers over the past quarter continue to show high levels of commitment to seeing the industry initiatives delivered because they are good for customers and good for business. That said, it is also apparent that for the smaller banks there is a proportionately high allocation of resources (both directly and indirectly) to the program overall. This to be expected at this stage of implementation of such a large change program and so it is important that both the industry as a whole, and the individual banks, remain focussed on the long-term benefits which will accrue to customers – and by definition in the case of banking – to the wider community.

Some banking groups that provide financial products and services in addition to retail banking products and services also have commented on the merit of applying relevant parts of the program to their wider group.

While understandably the reform program has a focus on the responsibilities of banks in articulating and delivering on service expectations for customers, my discussions about these issues with consumers and those in business, including in the banking industry, have also emphasised the nature of the bank-customer relationship being two-way, with both banks and customers each having separate responsibilities. The proposed amendments to the Code of Banking Practice will provide a higher degree of protection for consumers; the full benefits of this will only accrue if consumers recognise their responsibility to be diligent in informing themselves of, and protecting, their interests. A wider understanding of the bank-customer relationship is essential to many of the outcomes the industry is pursuing, particularly in making engagement by consumers easier and through the measures being taken by the banks to improve transparency and confidence.

As for any significant reform program, the Chief Executive Officers of the banks have a critical role to play in not only publicly promoting the good work being undertaken by their individual institutions, but also supporting the steps being taken by the industry as a whole. It is important that consumers are aware of the changes being made. Thus all opportunities to promote the changes and their benefits, and explain any significant issues which still need to be addressed, can be expected to contribute positively to the reform objectives.

Notwithstanding the good progress on implementation over the last quarter, there is still considerable work to be completed by individual banks, particularly in relation to Initiative 1 (Review of product sales commissions and product based payments) and Initiative 5 (Review of the Code of Banking Practice). Both are fundamental to the overall design integrity of the six initiatives as a whole and accordingly, will be subject to close review and a further update in my next quarterly report.

Appendices

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Appendix A

Implementation plan as at 20 July 2017

Initiative	Objective	Measures / Implementation Steps	Implementation Phases ⁽¹⁾			Summary Deliverable ⁽¹⁾	Milestone Step ⁽¹⁾	Primary Responsibility	
			Planning	Agreement of principles	Complete implementation				
1	Strengthen alignment of remuneration and incentives and customer outcomes	1.1 Immediately establish an independent review of product sales commissions and product based payments, with a view to removing or changing them where they could lead to poor customer outcomes	Jul-16 Complete	Mar-17 Complete	Mar-17 Complete	Independent review report on remuneration (*Timing contingent on ASIC review on mortgage broking)	a) Establishment of independent review b) Assessment of information gathered and submissions received c) Preparation of draft report and engagement with stakeholders d) Publication of final report	ABA Reviewer Reviewer Reviewer	
		1.2 Each bank commits to ensure it has overarching principles on remuneration and incentives to support good customer outcomes and sound banking practices	Apr -17 Complete	Aug-17 	Dec-17 	Individual bank policies on remuneration and incentives; informed by the independent review (*Changes and communication of changes and how they support good customer outcomes and sound banking practices may require additional time due to potential impact on agreements/contracts and alignment with performance reviews and other workplace-related matters)	a) Analysis of existing remuneration structures and practices and creation of initial framework b) Preparation of draft guiding principles to assist each bank meet the commitment c) Consultation and stakeholder engagement d) Finalisation of guiding principles e) Identification and development of overarching principles by each bank	Banks ABA/Industry ABA/Industry ABA/Industry Banks	
		1.3 Work with regulators to implement changes and, where necessary, seek regulatory approval and legislative reform	Apr-17 Complete	Jun-17 	Dec-17 	Potential regulatory approvals (egg authorisation, legislative reform) (*Timing contingent on preparation of report by independent reviewer and any regulatory approval processes required as well as legal requirements to be satisfied. Any necessary changes will need to be made across various agreements/ contracts and that may require further time)	a) Identification of responses and actions needed to remove or change product sales commissions and product based payments which could lead to poor customer outcomes b) Preparation of any documentation necessary to make any changes (such as submissions or applications for regulatory approvals) c) Regulatory approvals (where necessary) provided for banks to be able to make changes d) Banks change remuneration structures (where necessary) and communication of how and why these changes have been made	ABA/Industry ABA/Industry Regulators Banks	

Legend:



R1 R2 R3 R4 R5

Reported status

Status key:

> On target

> On alert for slippage against plan

> Adjustment required to original plan

> Next phase reliant on government

Implementation plan as at 20 July 2017

Initiative	Objective	Measures / Implementation Steps	Implementation Phases ⁽¹⁾			Summary Deliverable ⁽¹⁾	Milestone Step ⁽¹⁾	Primary Responsibility
			Planning	Agreement of principles	Complete implementation			
2 Making it easier for customers when things go wrong	Ensure retail and small business customers have a voice and problems are resolved more efficiently	2.1 Enhance the existing complaints handling processes by establishing a dedicated customer advocate in each bank to ensure retail and small business customers have a voice; and customer complaints directly relating to the bank, and the third parties appointed by the bank, are appropriately escalated and responded to within specified timeframes	Jul16 Complete	Dec-16 Complete	Jun-17 Complete	Industry position on the role of a customer advocate Appointment of a customer advocate in each bank	a) Assessment of customer advocate function and creation of initial framework b) Preparation of draft guiding principles to assist each bank meet the commitment c) Consultation and stakeholder engagement d) Finalisation of guiding principles e) Implementation of customer advocate function in each bank	ABA/Industry ABA/Industry ABA/Industry ABA/Industry Banks
		2.2 Support a broadening of external dispute resolution (EDR) schemes. Support the Government's announcement to conduct a review into EDR, including the Financial Ombudsman Service (FOS) conducting a review of its terms of reference with a view to increasing eligibility thresholds for retail and small business customers	Sep-16 Complete	Dec-16 Complete	Jun-17 	Industry position on operation of preferred EDR system completed for contribution to government review (*Timing of review to be determined by the government; potential impact on Code review)	a) Preparation of industry position on EDR b) Participation in government review of EDR c) Announcement by government (or relevant regulator) of findings of review and recommendations d) Adoption of industry position in new EDR system	ABA/Industry ABA/Industry Government ABA/Industry
	2.3 Work with ASIC to expand its current review of customer remediation programs from personal advice to all financial advice and products	Jul-16 Complete	Jul-16 Complete	Sep-16 Complete	ASIC regulatory guidance on client remediation programs issued (*Timing of regulatory guidance to be determined by ASIC)	a) Revised submission to ASIC on consultation paper on client remediation b) Adoption of industry position in new regulatory guidance c) Implementation of any changes to ensure banks' systems and practices support client remediation programs, including better record keeping	ABA Regulators Banks	
	2.4 Evaluate establishment of an industry wide, mandatory last resort compensation scheme covering financial advisers. Support a prospective scheme being introduced where consumers of financial products who receive a FOS determination in their favour would have access to capped compensation where an adviser's professional indemnity insurance is insufficient to meet claims	Sep-16 Complete	Mar-17 Complete	Sep-17 	Industry position and model for last resort compensation scheme settled	a) Identification of possible model for a last resort compensation scheme b) Preparation of industry position on a last resort compensation scheme c) Coordination of engagement and consensus building across stakeholders d) Consensus support for implementation of scheme e) Preparation of consensus submission to the Government f) Possible introduction of legislation to implement a scheme	ABA/Industry ABA/Industry ABA/Industry ABA ABA Government	

Legend:



R1 R2 R3 R4 R5
Reported status

Status key:

- > Cn target
- > Cn alert for slippage against plan
- > Adjustment required to original plan
- > Next phase reliant on government

Implementation plan as at 20 July 2017

Initiative	Objective	Measures / Implementation Steps	Implementation Phases ⁽¹⁾			Summary Deliverable ⁽¹⁾	Milestone Step ⁽¹⁾	Primary Responsibility		
			Planning	Agreement of principles	Complete implementation					
3	Reaffirming our support for employees who 'blow the whistle' on inappropriate conduct	Promote highest standards of whistle blower protections and ensure robust and trusted framework for whistleblowing	3.1	Ensure the highest standards of whistleblower protections by ensuring there is a robust and trusted framework for escalating concerns. Standardise the protection of whistle-blowers across banks, including independent support and protection against financial disadvantage.	Jul-16	Dec-16	Jun-17	Industry position on whistleblower protections Implementation of whistleblower framework aligned with industry principles in each bank	a) Assessment of whistleblowing policies and practices and creation of initial framework b) Preparation of draft guiding principles to assist each bank meet the commitment c) Consultation and stakeholder engagement d) Publication of guiding principles e) Bank implementation of highest standard of whistleblowing policies	ABA/Industry ABA/Industry ABA/Industry ABA Banks
4	Removing individuals from the industry for poor conduct	Demonstrate banks' commitment to improve practice and implement an industry register or mechanism to identify poor conduct across all bank employees, including customer facing and non-customer facing roles, and promote good conduct and ethical behaviour. ⁽²⁾	4.1	Implement an industry register or mechanism to identify individuals who have breached the relevant law, codes of conduct, standards or policies, so that employers can make their own informed recruitment decisions.	Sep-16	Jun-17	Dec-17 ⁽³⁾	Completion of position paper on an industry register Implementation of Conduct Background Check Protocol Industry register established (*Contingent on introduction of supporting statutory underpinning by Government)	a) Identification of possible model for industry register b) Preparation of industry position c) Coordination of engagement and consensus building across stakeholders d) Implementation of Conduct Background Check Protocol (from 1 July 2017 (major banks) and 1 October 2017 (non major banks)) e) Demonstrate industry engagement with Federal Government in support of a statutory register (end Dec 2017) f) Implement statutory register if introduced by Government	ABA/Industry ABA/Industry ABA/Industry ABA/Industry ABA/Industry
5	Strengthening our commitment to customers in the Code of Banking Practice	Ensure the Code of Banking Practice adequately covers expected standards for banks and their relationship with customers, including standards for engagement between both parties	5.1	Complete a review of the Code of Banking Practice by the end of the year.	Jul-16	Dec-16	Dec-16	Independent review report on the Code of Banking Practice	a) Establishment of independent review b) Assessment of information gathered and submissions received c) Preparation of draft report and engagement with stakeholders d) Publication of final report	ABA Reviewer Reviewer Reviewer
			5.2	Work with banks to implement changes to improve the operation of the Code of Banking Practice within their individual organisations	Jun-17	Dec-17 ⁽⁴⁾	TBC	New Code of Banking Practice (*Contingent on EDR review by government; transitional period and subsequent implementation of changes dependent on the extent of the changes)	a) Identification of responses and actions needed to improve the operation and performance of the Code b) Preparation of any changes to the Code and associated materials c) Publication of the new Code d) Banks make changes to reflect the standards contained in the new Code	ABA/Industry ABA/Industry ABA Banks

Legend:

 R1 R2 R3 R4 R5
 Reported status

Status key:
 On target
 On alert for slippage against plan
 Adjustment required to original plan
 Next phase reliant on government

Implementation plan as at 20 July 2017

Initiative	Objective	Measures / Implementation Steps	Implementation Phases ⁽¹⁾			Summary Deliverable ⁽¹⁾	Milestone Step ⁽¹⁾	Primary Responsibility
			Planning	Agreement of principles	Complete implementation			
6 Supporting ASIC as a strong regulator	Demonstrate banks' commitment to a well-regulated banking and financial services industry	6.1 Work with the Government and ASIC to implement a 'user pays' industry funding model to enhance the ability for ASIC to investigate matters brought to its attention	Aug-16 Complete	Oct-16 Complete	Jun-17 Complete	Industry agreement on funding model (*Implementation will be subject to consultation with an agreement by government)	a) Participation in consultation on users pays funding model b) Consideration of industry position in new model c) Implementation of an industry funding model which is accountable, transparent and encourages better and more efficient regulatory activities	ABA/Industry ABA/Industry Government
		6.2 Work with ASIC to enhance the current breach reporting framework	Aug-16 Complete	Oct-16 Complete	Dec-16 			

Legend:



R1 R2 R3 R4 R5
Reported status

Status key:

- On target
- On alert for slippage against plan
- Adjustment required to original plan
- Next phase reliant on government

Footnotes:

1. Assessment based on advice from the ABA and/or entity/entities with primary responsibility for implementation
2. One bank has advised that they have substantially adhered to the Guiding Principles, as explained in footnote 27 in Chapter 3.
3. Complete implementation of the measure still requires further consultation with key stakeholders and support for appropriate statutory underpinnings
4. Previously this item has been 'TBC'. Accordingly only a chevron for R5 has now been added. This is described in Section 2.2

Appendix B

Participant banks

The following member banks of the ABA have confirmed their participation in the package of initiatives:

- AMP Bank³²
- Arab Bank Australia
- Australia and New Zealand Banking Group
- Bank Australia
- Bank of Queensland
- Bank of Sydney
- Bendigo and Adelaide Bank
- Citigroup Australia
- Commonwealth Bank of Australia
- Defence Bank
- HSBC
- ING Direct
- Macquarie Bank
- ME Bank
- MyState Bank
- National Australia Bank
- Qudos Bank
- Rabobank
- Rural Bank
- Suncorp Group
- Westpac Banking Corporation

³² AMP Bank has advised its commitment to the package of initiatives is subject to relevance to the bank and alignment with AMP Group.

Appendix C

Stakeholder consultations undertaken

Discussions were held or input was provided by the following organisations in the preparation of this report:

Banks:

- AMP Bank
- Arab Bank Australia
- Australia and New Zealand Banking Group
- Bank Australia
- Bank of Queensland
- Bank of Sydney
- Bendigo and Adelaide Bank (including Rural Bank)
- Citigroup Australia
- Commonwealth Bank of Australia
- Defence Bank
- HSBC
- ING Direct
- Macquarie Bank
- ME Bank
- MyState Bank
- National Australia Bank
- Qudos Bank
- Rabobank
- Suncorp Group
- Westpac Banking Corporation

Other stakeholders:

- Australian Bankers' Association
- Australian Prudential Regulation Authority
- Australian Securities and Investments Commission
- Edelman Intelligence

Appendix D

Summary of external reviews

Body	Review title	Consultation close	Findings due	Initiatives potentially impacted					
				1	2	3	4	5	6
House of Representatives Standing Committee on Economics	Review of the Four Major Banks ('Coleman Inquiry')	Feb/Mar 2017	Ongoing	x	x	x	x	x	x
Parliamentary Joint Committee on Corporations and Financial Services	Whistleblower protections in the corporate, public and not-for-profit sectors	Feb 2017	Aug 2017			x			
Senate Economic References Committee	Consumer protection in the banking, insurance and financial sector	Mar 2017	May 2018		x			x	
Senate Select Committee on Lending to Primary Production Customers	Regulation and practices of financial institutions in relation to primary production industries	May 2017	Oct 2017		x				
ASBFEO	Small Business Loans Inquiry ('Carnell Inquiry')	Dec 2016	Completed		x			x	
ASIC	Review of mortgage brokers remuneration structures	Dec 2016	Completed	x					
Treasury	Review of the financial system external dispute resolution framework ('Ramsay Review')	Oct 2016	Late 2017		x			x	
Treasury	ASIC Enforcement Review	Ongoing	Dec 2017					x	x
Treasury	ASIC Industry Funding Model	Jun 2017	Completed						x
Treasury	Tax and corporate whistleblowing	Feb 2017	Ongoing			x			
Treasury	Product design and distribution obligation and Product intervention power	Mar 2017	Ongoing						x

Note: This table includes the major reviews impacting the banking industry package of initiatives. Other reviews are underway by ASIC, APRA and the Government that may also have some effect on the package of initiatives.

Appendix E

Glossary and abbreviations

Term	Definition
ABA	Australian Bankers' Association
AFCA	Australian Financial Complaints Authority
APRA	Australian Prudential Regulation Authority
ASBFEO	Australian Small Business and Family Enterprise Ombudsman
ASIC	Australian Securities and Investments Commission
Banking industry	Banks and banking industry associations
Banking system	Regulators, industry bodies, banks, laws and regulations
CALC	Consumer Action Law Centre
Carnell Inquiry	Small Business Loans Inquiry being undertaken by the ASBFEO, Ms Kate Carnell AO, into the laws and practices governing financial lending to small business
COSBOA	Council of Small Business of Australia
EDR	External Dispute Resolution
FOS	Financial Ombudsman Service
FSU	Finance Sector Union
Implementation plan	Detailed program of work, including provisional timetables for each phase of the project, planned to address each initiative
ISWG	Industry Strategy Working Group. A committee of senior bank representatives convened by the ABA to oversee implementation of the package of initiatives
Khoury Review	Code of Banking Practice – Independent Review 2016
Major banks	ANZ, CBA, NAB and Westpac
Package of initiatives	Six programs of work announced by the ABA on 21 April 2016
Measures	Actions specified to achieve the objectives of ABA's package of initiatives
Milestones	Interim deliverables required to be achieved in order to implement each measure
Performance indicators	Key performance indicators to assess the effectiveness of measures in meeting the objectives of the initiatives. Referred to as Success Indicators (Outcome Indicators) in Report 1 and Report 2.
Ramsay Review	Treasury's 'Review of the financial system external dispute resolution framework'
Sedgwick Review	Retail Banking Remuneration Review

