
While Australia performed well in response to the global financial crisis, APRA acknowledged that improvements could be made in regulation. In November 2009, the regulator issued several Prudential Standards on governance mainly concerning remuneration.

The standards set out the minimum requirements that a registered institution (one subject to APRA regulation) must satisfy in the interests of promoting effective governance. The Standards can be found at

<http://www.apra.gov.au/Policy/remuneration-governance-extensions-November-2009.cfm>

Board Remuneration Committee

The standards required that the Board has a Board Remuneration Committee. An exemption may be obtained only in exceptional circumstances. The Committee must make recommendations to the Board on the individual remuneration of, at a minimum, the CEO and his or her direct reports.

The Committee must periodically review the Remuneration Policy to ensure that it remains appropriate. The Committee should also identify undesirable outcomes from existing policy. The existence of the Committee does not abrogate the Board's duty to receive and act on reports of the functioning of the Remuneration Policy, inside and outside Australia.

External Advisers

The committee must ensure that its external advisers are and remain independent (ie are not concurrently providing other advice or services to the Company) and that the Committee preserves its own independence in making recommendations to the Board.

Remuneration Policy

The policy must be suitable in detail and scope to the size and complexity of the Company itself. If the registered institution is part of a corporate Group, it can utilise the Group Remuneration Policy noting that that policy may need to be modified to comply with APRA's requirements.

The policy should cover all the classes of persons whose actions could put the institution's financial soundness at risk. These fall into three groups:

(a) Responsible persons including directors, executives and senior managers who make decisions affecting the whole or most of the business.

(b) Those whose primary role is risk and financial control (including risk management, compliance, internal audit, financial control and actuarial control).

(c) Those persons who receive a significant proportion of performance-based remuneration such as through bonuses or commissions.

Certain people will be members of one of these groups and also those on whose remuneration the Committee must make individual recommendations. The Committee should also make recommendations in regard to particular types of contractors and service providers.

Recommendations on remuneration should be based on adjusting remuneration structures to support prudent risk management procedures. Performance measurement must be sound and adjusted for risk.

Deferral should be used to help adjust for risk and time should be allowed at the end of financial years to allow for better assessment of performance. Balance should be maintained between fixed and variable pay so that the Board can exercise its discretion on a suitable proportion of remuneration.

It is required that the Board retain discretion to adjust rewards to compensate for unexpected or unintended outcomes caused internally or externally. Caution should be exercised when granting options as their effects can vary widely in different scenarios. Risk management of equity grants needs to take a long-term view.

Prudence is required in regard to executive loans or leveraging. The standards also prohibit hedging of exposure to financial risk by executives and unusual risk-taking behaviour before retirement, resignation or termination. Recruitment and termination payments (golden handshakes and golden parachutes) should be very carefully scrutinised to prevent their distortion.

While these rules affect companies regulated by APRA, we believe that the principles will have a flow-on effect across a wider spectrum of enterprises, with particular alerts for NEDs regarding risk in reported annual results and their alignment with criteria leading to incentive payments.

SERVICES AVAILABLE

Speak to us if you need advice on

- REMUNERATION PLANNING
- BOARD ADVISORY SERVICES
- CEO REWARD STRATEGY
- INCENTIVE PLAN DESIGN
- RETENTION PLAN DESIGN
- EQUITY INCENTIVES
- IPOs