Annexure A

RESPONSE TO THE DISCUSSION GOVERNANCE PAPER FOR THE AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY

Proposal 1 – Skills and Capabilities

Require regulated entities to:

a) identify and document the skills and capabilities necessary for the board overall, and for each individual director,

b) evaluate existing skills and capabilities of boards and individual directors,

c) take active steps to address gaps through professional development, succession planning and appointments.

Current requirements

Prudential standards CPS 510 and SPS 510 require boards collectively to have the necessary skills, knowledge and experience to manage regulated entities appropriately. Each director must have 'skills that allow them to make an effective contribution to board deliberations and processes.' Boards are required to evaluate their collective performance on an annual basis. There is no explicit requirement to set minimum requirements for individual directors or to respond to any shortcomings.

Problem statement

Regulated entities have substantial discretion as to how they define their skill and capability needs, and how to assess the extent to which their boards and directors satisfy these requirements. As a result, APRA has observed wide variation in the effectiveness of these processes. While many entities adopt a robust forward-looking approach and take care to ensure their boards have the necessary skills and capabilities to support their strategy, others adopt more cursory processes and fail to address gaps. Shortcomings APRA observes include:

• adopting a vague or a narrow view of necessary skills and capabilities, including a failure to specify expected experience, qualifications or behavioural capabilities – and failing to consider how these can be measured

• failure to specify minimum skills and capabilities that individual directors need to fulfil their role

• not verifying skills or capabilities, often relying heavily on self-assessments

• failure to take steps to address gaps and weaknesses through professional development and succession planning.

These kinds of deficiencies tend to be most prevalent among small banks and in parts of the superannuation sector. For example, a 2021 cohort-based thematic review of mutual banks found that almost 50 per cent of boards had no directors or only one director with contemporary

industry experience. Some RSE licensees have boards that are deficient against their own skills matrices, for example not having directors adequately skilled in key areas such as investment and risk management. However, APRA notes such issues are present in all industry cohorts.

Ongoing failure to address skill and capability needs will result in boards that are inadequately prepared to deliver on their organisational strategy or to anticipate and address challenges that arise.

Addressing the problem

APRA proposes to require all regulated entities to, on an ongoing basis, identify and document the skills, capabilities and behavioural attributes that the board needs to deliver its organisational strategy and perform its role. These attributes should be clearly defined and documented in a skills matrix. They should include specific expectations for the chair, chairs of board committees and other individual directors. Skills should be measurable and verifiable, and behavioural attributes should be observable. The targeted skills, capabilities and minimum criteria should be proportionate to an entity's business needs, size and complexity.

Second, APRA proposes to require regulated entities to evaluate the skills and capabilities their boards already have and be able to demonstrate to APRA that they are taking active steps to remedy gaps through professional development, succession planning and new appointments. In considering nominees to the board, APRA expects entities to consider existing skills gaps so that each new appointment makes progress towards addressing them.

This proposal is intended to raise minimum standards for directors and boards across the financial system, irrespective of the nominations process or board structure. Requisite skills should be considered by those making the nomination. It should not impact entities that already adopt proactive and forward-looking approaches to board capability. Listed entities are already subject to similar expectations under the ASX Corporate Governance Principles and Recommendations.

These changes would also better allow APRA to hold regulated entities to account for the calibre and development of their boards.

To be clear, this proposal, as well as Proposal 2 below, would not involve any changes to the equal representation model under which employer and employee groups have the right to nominate directors to some RSE licensee boards. The focus of the proposals is on ensuring that directors of these entities have the necessary skills, capabilities and character – regardless of how they are nominated, the ownership model or board composition requirements in legislation.

Links with other proposals

Proposals 1 and 2 overlap and reinforce one another. A regulated entity's fit and proper regime (Proposal 2) should set and assess a baseline of acceptable behaviour, character and qualifications to be on a financial services board or in other responsible person roles (effectively, being fit and proper is the 'ticket to play' as an industry leader). Proposal 1 should inform regulated entities' assessment of whether a fit and proper individual is the right fit for their board. Specifically, entities would need to identify for their own board the specific skills and capabilities mix needed to deliver their organisational strategy – and act to achieve it. Lack of skill and capability should inform ongoing fit and proper assessments and therefore a director's prospects

for reappointment. It should also flow through into board renewal and succession planning (Proposal 8). Triennial reviews of SFI board and director performance (Proposal 5) will verify progress on skills and capabilities, and make recommendations as needed.

InsidEntity Response

a) Identify and document the skills and capabilities necessary for the board overall, and for each individual director.

We support the requirement fully, and below our submissions:

1. Skill can only be gained during one working at a particular Entity, and we define the skill as a working experience at a particular or combined Entities for at least a period of 5 years. A period served on the Boards not taken into account.
   Many Boards across the Globe don't disclose this information, and mainly state directorships the Director is holding.
   We submit that the Board must disclose the working experience (provable skill) of each director – for example, Ms May has worked at NAB from January 2010 to August 2023.
2. Capacity of each director is very crucial and should be disclosed as follows:
   a) Directorships each director is holding, and this will demonstrate whether the director has capacity to serve on the Board and contribute meaningfully.
   b) Skills / experience the Board has, and minimum Board representation should be the following:
      i) Industry experience
      ii) Finance experience
      iii) Legal experience
      iv) Industry, and Finance qualifications as a minimum
3. The above information must be publicly available at any time, unlike only being published annually.

Our Platform assesses the above for each director, and the average score for the Entity is given. The Platform will allocate a score to each director for each experience as per above, and a director with more than 5 directorships will score Nil.

b) Evaluate existing skills and capabilities of boards and individual directors.

We support the requirement fully.

c) Take active steps to address gaps through professional development, succession planning and appointments.

We support the requirement fully.

Proposal 2 – Fitness and propriety

Require regulated entities to meet higher minimum requirements to ensure fitness and propriety of their responsible persons.

Require SFIs, and non-SFIs under heightened supervision, to engage proactively with APRA on potential appointments.

Current requirements

Fit and proper policies are a key part of a regulated entity's risk management framework.

Regulated entities must prudently manage the risks that responsible persons who are not fit and proper pose to their business and financial standing. Entities must have policies and procedures for determining the fitness and propriety of responsible persons, including directors, senior managers and certain other individuals prescribed by industry legislation, including auditors and actuaries.

The definition of fitness and propriety encompasses a person's core skills, experience and knowledge as well as their honesty and integrity. Conflicts are to be considered as part of the assessment, although there is no reference to potential or perceived conflicts. While APRA guidance lists matters that should be considered by a regulated entity in considering the fitness and propriety of a responsible person, it is generally left up to the entity to decide.

Fitness and propriety must, except in very limited circumstances, be assessed prior to initial appointment and reassessed at least annually. Regulated entities are obliged to conduct a full reassessment of a responsible person's fitness and propriety if concerns emerge, but are not obliged to notify APRA unless they determine that person is not fit and proper. Where an individual is assessed as not fit and proper, the entity must take all reasonable steps to ensure that they are not appointed to, or do not continue to hold, a responsible person position. Entity policies must specify actions to be taken in those instances.

There is no requirement in the relevant prudential standards for regulated entities to consider important matters such as time capacity to fulfill the role, all criminal offences 7 or reputational risk.

Problem statement

APRA has observed substantial variation in how regulated entities conduct fitness and propriety assessments. Poor practice is typically characterised by a narrowly defined process that fails to generate meaningful outcomes. For instance, APRA observes weaknesses such as:

• entities being focused on process compliance rather than outcomes

• taking a narrow view of what constitutes fitness and propriety 8

• inadequate consideration of a person's fitness (skills, capabilities, experience and knowledge)
• little consideration of the capacity of directors to balance multiple roles and professional obligations

• limited verification, with excessive reliance on self-assessments and other 'light touch' checks
• treating annual reviews of incumbent responsible persons as cursory exercises, rather than part of an enduring obligation to ensure the ongoing fitness and propriety of responsible persons.

On occasion, regulated entities have been unwilling to initiate a reassessment of a responsible person's fitness and propriety where concerns emerge, even where they created reputational or prudential risk to the entity. There have also been instances where entities have been reluctant to engage with APRA where APRA has held concerns about the fitness and propriety of potential appointees.

Addressing the problem

APRA proposes to strengthen baseline expectations for fitness and propriety by:

• reinforcing entities' responsibility for outcomes, as well as following a robust process set out in their fit and proper policy

• being more specific about what fit and proper means, and the need to verify conclusions. APRA proposes to incorporate existing guidance and additional matters into the standard for consideration, such as:

  o actual, potential and perceived conflicts of interest and duties

  o criminal and conduct records, for example contraventions arising out of civil, criminal or regulatory matters that may give rise to concerns

  o character or regulatory references to evaluate performance in other roles, including the financial and reputational performance of previous organisations

  o the ability to commit sufficient time to their role, including consideration of specific roles on other boards, for example chair or committee chair

  o reputational risk.

• clarifying triggers for a fit and proper reassessment, for example:

  o there are grounds to believe that an individual is not meeting their obligations under FAR, or otherwise not meeting minimum fitness or performance expectations

  o material misconduct or behaviour inconsistent with an entity's code of conduct

  o adverse findings in criminal, civil or professional proceedings

  o changes in personal circumstances posing potential reputational risk.

• requiring regulated entities to notify APRA when concerns arise that may reasonably impact a person's fitness and propriety, even before a determination has been reached.

As set out in Chapter 1, several overseas jurisdictions can approve or veto appointments to prudentially regulated entities. 9 While APRA does not have formal approval or veto powers, APRA seeks to heighten its oversight of, and entity focus on, the suitability of individuals in responsible person roles.

The FAR requires regulated entities to take reasonable steps to deal with APRA in an 'open, constructive and cooperative way'. Consistent with this obligation, and to enable APRA to form a view of potential and incumbent responsible persons, APRA proposes to:

• enable APRA to require an entity-led reassessment if concerns about a responsible person or candidate are not addressed by the entity in a timely manner. For example, a reassessment may be prompted in response to material regulatory findings (e.g. via prudential review) or performance assessment (e.g. via board performance review)

• require that SFIs, and non-SFIs subject to heightened supervision, keep APRA informed of succession plans and nominations prior to appointment or public announcement

• in prudential practice guidance, note that APRA may request an interview with any candidates for responsible person roles, prior to appointment or reappointment. This is on an exceptions basis, where further information is needed to allay any concerns it may have.

Where APRA is not satisfied with a regulated entity's proposed or incumbent responsible person(s) or board performance, APRA will share its views with the regulated entity. If the entity does not act to address concerns, this will inform the intensity of APRA supervision. APRA may also trigger a reassessment of an individual's fitness and propriety if they are already in a responsible person role (Proposal 2) or use its other supervisory or enforcement powers to address outstanding risk to the regulated entity.

In strengthening their fitness and propriety regimes, APRA also expects regulated entities' written agreements with their accountable persons will adhere to both fit and proper criteria and the FAR.

Links with other proposals

This proposal complements Proposal 1 (skills and capabilities) as minimum director skills will overlap with broader fit and proper criteria. This proposal also relates to Proposal 3 (conflicts management). APRA seeks to ensure that all entities integrate forward-looking skills assessments with their fit and proper processes. APRA's approach to conflicts aims to minimise structural conflicts by ensuring that they are routinely identified and addressed.

Links with FAR There is some overlap between the reporting obligations that apply to regulated entities under APRA's fitness and propriety requirements and statutory requirements under the FAR. The FAR has commenced for banks and commences on 15 March 2025 for insurers and RSE licensees. To reduce reporting obligations, APRA will examine whether it can align role definitions and rely on reports it receives under the FAR rather than requiring two sets of reports (although this will not apply to categories of responsible persons who are not accountable persons under the FAR).

InsidEntity Response
APRA has advanced a number of proposals in the Discussion Paper regarding the Fitness and Propriety of responsible persons to meet higher minimum requirements. The paper defines fitness and propriety as a person's core skills, experience and knowledge as well as honesty and integrity that must be considered and assessed prior to initial appointment and reassessed at least annually or when concerns emerge.

We support that the existing guidance and additional matters as proposed be incorporated in the standard to ensure consistent application by all regulated Entities. Persons appointed and continue to serve on the Boards must meet the higher minimum requirements to ensure safeguarding on interests for all the stakeholders.

Proposal 3 – Conflicts management

Extend current RSE licensee conflict management requirements to banks and insurers so they are also required to:

a) proactively identify actual and potential conflicts of interest and duty

b) avoid or prudently manage conflicts

c) take remedial action when conflicts are not disclosed or managed properly.

Require regulated entities to consider perceived conflicts, in addition to actual and potential conflicts.

Current requirements

To be considered fit and proper, responsible persons of banks, insurers and RSE licensees must either have no conflict of interest in performing their duties or, if the person has a conflict, it would be prudent for a regulated entity to conclude that the conflict will not create a material risk that the person will fail to perform their duties properly.

More broadly, banks and insurers have different conflict management prudential obligations to RSE licensees. The risk management standard CPS 220 requires bank and insurer risk management policies and procedures to include a process for identifying, monitoring and managing potential and actual conflicts of interest.

RSE licensees are subject to a separate standard on conflicts of interest (SPS 521), which is more detailed and applies for the purposes of section 52(2)(d)(iv) of the SIS Act. The standard requires RSE licensees to:

• have a conflicts management framework to identify, assess, mitigate, manage and monitor all conflicts

• develop, implement and review a conflicts management policy that is approved by the board

• identify all relevant duties and relevant interests

• develop registers of relevant duties and relevant interests and make them public.

The associated guidance (SPG 521) provides more insights about avoiding and managing conflicts.

Across all three industries, there are no requirements in the standards covering perceived conflicts, nor is there any explicit obligation to have regard to reputational risk.

Problem statement

APRA's current requirements are inconsistent across its regulated industries. APRA has observed some weakness in entities' identification and treatment of conflicts across the regulated population. The most common challenges relate to personal financial dealings of responsible persons, directors performing multiple roles within a group, relationships with suppliers, and personal affiliations.

Across regulated industries, there have been instances of inadequate identification of conflicts with service providers and responsible persons' group affiliations. Some entities do not have adequate processes for identifying and managing director conflicts on a continuous basis, other than through declarations at board meetings. There APRA • Governance review discussion paper March 2025 21 have also been instances where directors and senior managers have held roles or had relationships, either directly or through family relationships, with service providers, and these conflicts were not appropriately addressed.

Contemporary good practice generally involves officers and directors identifying actual, potential and perceived conflicts of interest; disclosing these conflicts to the board and other stakeholders; actively managing conflicts including through recusal from decisions and structural changes where necessary; and documenting and sharing information as appropriate.

Addressing the problem

To address the issue of differing conflict management requirements across sectors, APRA proposes to create a single cross-industry set of requirements. This would include requirements that currently apply only to RSE licensees (e.g. having a conflicts management policy, and the public disclosure of registers of duties and interests). It is proposed that all regulated entities would be subject to these requirements. However, APRA seeks feedback on whether banks and insurers should be required to maintain and disclose registers of duties and interests and what the effect of this would be.

APRA also proposes to strengthen the requirements that are currently in SPS 521 by incorporating some material that is currently in the guidance into obligations, which would apply to all regulated industries. This includes the guidance that, as well as actual conflicts, potential or perceived conflicts and conflicts that affect the reputation of the business should be actively managed. This will ensure entities, and if necessary, APRA, can respond more effectively to instances of poor conflict management.

APRA will also use this as an opportunity to streamline certain requirements which currently apply to RSE licensees under SPS 521. For example, the standard requires an annual and triennial review of a fund's conflicts management framework. For SFIs, the annual conflicts framework review may be integrated into the triennial board review outlined in Proposal 5.

Links with other proposals

This proposal is connected to Proposal 2 (fitness and propriety) where APRA expects that consideration of an actual, potential or perceived conflict will be a component of the fit and proper assessment. APRA is also proposing that review of the conflicts management framework should be incorporated into the triennial board review (Proposal 5). Finally, Proposal 4 seeks to reinforce the expectation that independent directors can exercise truly independent judgement.

InsidEntity Response
Our comments below for the two proposals by the APRA: 1. We would support the requirement that Banks and Insurers to also be required to maintain and disclose registers of duties and interests. This will also promote transparency. a) We are not in the position to comment on the effect of the requirement to publicly disclose registers of duties and interests by Banks and Insurers.

2. Full support of any measure/s to actively manage conflicts that could affect the reputation of the business. Value of the business will be negatively affected should the reputation of the business be compromised.

Proposal 4 – Independence

Note: This proposal relates to banking and insurance entities only. The definition of independence for RSE licensees is prescribed by legislation and would not be affected by this proposal.

Strengthen independence on regulated entity boards by:

a) requiring that at least two of their independent directors (including the chair) are not members of any other board within the entity's group

b) making minor amendments to the independence criteria, including extending the prohibition on directors who are substantial shareholders in a regulated entity or group from being considered independent, to include material holdings of any type of security

c) extending the current requirement for bank and insurer boards to have a majority of independent directors to include boards of entities with a parent that is regulated by APRA or an overseas equivalent.

Current requirements

APRA prudential standard CPS 510 requires boards of banks and insurers to have an independent chair and a majority of independent directors. An independent director is currently defined as:

'a non-executive director who is free from any business or other association — including those arising out of a substantial shareholding, involvement in past management or as a supplier, customer or adviser — that could materially interfere with the exercise of their independent judgement.'

CPS 510 allows the independent directors on the board of the parent company or its other subsidiaries to sit as independent directors on the board of the regulated entity.

The standard also prohibits directors who are substantial shareholders in a regulated entity or group from being considered independent.

While APRA-regulated boards in banking and insurance must generally have a majority of independent directors, locally incorporated entities that are subsidiaries of a prudentially regulated parent have slightly different requirements. The boards of these subsidiaries must have a majority of non-executive directors, but they do not all need to be independent. CPS 510 requires three independent directors (including the chair) on a board of up to seven directors, and four (including the chair) on larger boards.

Problem statement

Intra-group conflicts

As noted in relation to Proposal 3 (conflicts management), APRA has observed instances of poor conflict management where entities do not fully consider potential or actual intra-group conflicts, particularly in the context of board members. APRA has seen instances where directors considered to be independent under the current prudential standard have shown a lack of independent judgment by failing to prioritise the best interests of an APRA-regulated entity over other group entities.

APRA's observation is that the current prudential standard does not take sufficient account of the potential for conflict between the interests of different group entities. The extent of these conflicts varies across groups. At one end of the spectrum, there are groups where interests are well aligned. In these cases, independent directors can serve on multiple boards and not encounter significant conflicts. At the other end, there are groups where interests are not well aligned. In these groups there is much higher potential for conflict between the interests of the regulated entity and other group entities. Particularly where conflicts of interest between parent and subsidiary exist, APRA has intervened to require entities to address these conflicts by restructuring boards, taking specific actions to address conflicts, and appointing additional independent directors. In some instances, APRA has imposed capital overlays to encourage these governance concerns to be addressed.

Other conflicts

While CPS 510 prohibits directors who are substantial shareholders in a regulated entity or group from being considered independent, it does not acknowledge that holding other types of securities may create similar conflicts which may interfere with a director's judgement.

Inconsistent requirements for board composition

CPS 510 sets inconsistent requirements for bank and insurer entity boards. While there were concerns about available directors for subsidiaries with APRA-regulated parents or overseas equivalents more than a decade ago, there is limited evidence to support different treatment now.

Addressing the problem

A proposed revised definition of independence is provided below. APRA welcomes feedback on this definition:

'a non-executive director who is not an employee of the entity, or the group to which it belongs, and who is free from any business or personal relationship that interferes, or could reasonably be perceived to interfere, with their exercise of objective judgement or acting in the interests of the regulated entity.'

Intra-group conflicts

There are several ways APRA could address this issue in its prudential standards. All options involve trade-offs between supervisory efficiency, entities' ease of application, risk mitigation and industry disruption. They range from removing the current clause which allows directors to sit on multiple boards and retain their independent status, through to mandating that independent directors on the board of a regulated entity cannot sit on other boards within the group. 10 The former would involve considerable review and judgement by entities, in consultation with APRA, to determine which directors are independent. The latter would cause considerable disruption and director turnover, even where entity and group interests are highly aligned.

To strike a pragmatic balance between these objectives, APRA proposes to mandate that on each regulated entity board, at least two of the independent directors (including the chair) must not be directors on any other board within the relevant group.

Irrespective of which option is ultimately chosen, APRA expects regulated entities to effectively manage intra-group conflicts for every member of their board.

Other conflicts

APRA also proposes to update the criteria currently in Attachment A of CPS 510 to ensure that substantial holders of any security issued by the regulated entity or the group to which it belongs cannot be considered independent. The original intent remains the same - to prevent material financial conflicts. The amendment would simply acknowledge that substantial debt holders, for example, may be subject to the same influence as substantial equity holders.

Consistent requirements for board composition

APRA proposes to extend the requirement for bank and insurer boards to have a majority of independent directors, to also apply to subsidiaries of parents regulated by APRA or overseas equivalent. APRA is conscious that the proposed changes may require recruitment of additional independent directors, and a reasonable transition period. Any final requirements that would require changes to board composition would embed suitable transitional arrangements for affected banks and insurers.

InsidEntity Response
We support the following proposals: 1. The revised definition of independence as detailed on the Discussion Paper, March 2025. 2. For Intra-Group conflicts, we also support the proposal by APRA that at least two of the Independent Directors (including the chair) must not be directors on any other Board within the relevant Group of Companies. Their impartiality might be impaired should they serve on more than one Board within the Group. 3. Directors of the substantial holders of any security issued by the regulated Entity or Group must not be considered independent. 4. Support the proposal to extend the requirement for Bank and Insurer Boards to have a majority of independent directors, to also apply to Subsidiaries of Parents regulated by APRA or overseas equivalent.
At InsidEntity, we take Independence as the lifeline of any Entity that must always be intact at least for the majority of the Non-Executive Directors. Below are some of the requirements for the directors to be deemed Independent per our Independence Standard: 1. director fee is less than 5% of ones total income from all sources, and 2. the director is not holding shares in the company for more than 0.10% of issued equity (directly or by representation).

Proposal 5 – Board performance review

Require SFIs to commission a qualified independent third-party performance assessment at least every three years which covers the board, committees and individual directors.

Current requirements

APRA standards require boards of all regulated entities to have procedures for assessing board and individual director performance at least annually. APRA's guidance for the boards of health insurers and RSE licensees (HPG 510 and SPG 510) sets the expectation that the assessment of board performance should by undertaken by an external party at least every three years.

Problem statement

APRA's supervisory experience is that board performance assessments vary substantially in scope and depth. Some reviews are thorough and forward-looking, while others lack rigour and credibility. Some entities commission external board reviews, although these can still fall short of expectations. APRA reviews of performance assessments have identified three key areas where reviews have scope to improve:

• they focus on the collective board and do not capture committee and individual director performance

• they are not informed by robust evidence, instead relying solely on self-assessments or peer input

• chairs fail to take a leadership role, either in the assessment process or in ensuring that emerging recommendations are addressed.

The ASX Corporate Governance Principles and Recommendations for listed entities support the principle that performance assessments should cover individual directors and committees, stating that listed entities should 'have and disclose a process for periodically evaluating the performance of the board, its committees, and individual directors.' The principles also encourage considering periodic use of external facilitators. The Australian Institute of Company Directors (AICD) has similarly recognised the value of internal and external board evaluations.

Addressing the problem

To address these problems, and to take a proportionate response, APRA proposes to require SFIs to:

• commission external independent performance assessments of boards, committees and individual directors by credible and appropriately qualified experts every three years

• have their chair take a leading and accountable role for the satisfactory completion of performance assessments and for ensuring that recommendations are addressed appropriately
• submit the independent triennial report to APRA.

Given the anticipated rigour of the triennial review, APRA expects to narrow the scope of annual performance assessments for SFIs (to focus on progress on recommendations from the independent assessment).

APRA recognises that commissioning an external board assessment may be disproportionately costly for smaller entities and has stopped short of mandating this exercise for non-SFIs. However, APRA still expects non-SFIs to improve the overall quality and rigour of their annual performance reviews. Non-SFI chairs are also expected to take active leadership of the process and resulting programme. This will be reflected in guidance.

APRA proposes SFI triennial external reviews would cover, at minimum:

• board, committees and individual director performance

• engagement between directors and senior management

• the chair's effectiveness

• board and committee workloads and meeting cadence

• quality of reporting to enable risk-based decision-making and oversight

• conflicts management

• strategic alignment of the skills matrix and gap analysis against current state

• effectiveness of overall decision-making.

The independent assessment should recommend tangible actions that will assist the board and its committees to be more effective. Findings should feed into renewal and succession planning, skills matrices and, where relevant, fit and proper assessments. Boards of SFIs must be able to demonstrate to supervisors how they are acting upon the recommendations of external reviews.

InsidEntity Response
1. We agree and support the three proposals as articulated in the Discussion Paper.

Proposal 6 – Role clarity

Define APRA's core expectations of the board, the chair and senior management.

Provide additional guidance on which APRA requirements may be delegated to board committees and senior management.

Current requirements

APRA standards include a short, high-level definition of the role of the board of a regulated entity ('the board is ultimately responsible for the sound and prudent management of the institution'). They include even less on expectations concerning the role of the chair. Detailed guidance on what boards should do is limited to the roles and responsibilities of board audit, risk and remuneration committees. This contrasts with other relevant standard setters, including the BCBS, the IAIS and the ASX Corporate Governance Council, which each provide guidance in their principles on the role of the board.

CPS 510 gives authority to the board of a regulated entity to delegate responsibilities to senior management. Delegations must be in writing and boards must have systems in place to monitor the exercise of delegated authority. Boards remain ultimately responsible for matters delegated to management.

Problem statement

APRA has observed a tendency for some board agendas to be overweight on operational matters, sometimes at the expense of strategic issues. An APRA governance thematic review found that many boards were spending less than 30 per cent of their time on forward-looking strategy and risk oversight.

APRA's current prudential requirements and guidance relating to boards have emerged over many years. The prudential standards currently set around 150 requirements for a typical entity board. Of these requirements, about 25 per cent relate to reports to the board. A further 25 per cent require the board to review or approve specific matters. The remainder assign responsibility to boards for oversight or management of specific prudential obligations. APRA has received feedback that it would help entities if prudential standards and guidance were clearer about the core responsibilities of the board, and what can be delegated to board committees or senior management.

The final report of the prudential inquiry into the CBA emphasised the importance of boards holding management to account, and management providing the board and committees with sufficient and succinct information to make effective decisions.

The prudential inquiry into the CBA also emphasised the crucial contribution of board chairs to effective governance. APRA has observed poor outcomes at some regulated entities where chairs have failed to provide adequate leadership and oversight of board functions. These include lack of challenge to management, groupthink, a failure to include relevant stakeholders in deliberations and insufficient attention to board performance and renewal.

Addressing the problem

To address these problems, APRA proposes to amend its prudential standards to include a clear articulation of the primary roles of the board, the chair and senior management. While APRA

appreciates that most APRA-regulated boards understand their responsibilities, the purpose of the proposal is to be clear on APRA's expectations, and to facilitate better delegation to board committees and management. This should empower boards to spend more time on forward-looking strategy, risk and oversight.

Responsibilities APRA considers to be central to the board include:

• articulating the purpose and values of the entity, and desired culture

• overseeing development, approval and execution of the entity's strategy, objectives and risk appetite

• overseeing the effectiveness of governance and risk management frameworks

• providing leadership and constructive challenge to senior management.

APRA also proposes to identify the core responsibilities of the chair in prudential standards. APRA expects that this would include responsibility for culture, board performance and fit and proper assessments.

In relation to the role of senior management, APRA proposes an outcomes-focused definition that supports the execution of the regulated entity's activities in line with the board-approved strategy, risk appetite, culture and values, and ensures senior management deals with the board in a clear, timely and transparent manner. Senior management should be responsible for briefing the board effectively, with succinct and relevant information to support decision making, rather than briefing with a view to satisfy compliance requirements.

While CPS 510 and SPS 510 already allow boards to delegate certain functions to senior management and board committees, APRA is seeking feedback on more specific examples of processes and policies APRA has assigned to the board that would be appropriate for delegation to committees or senior management.

APRA will also commit, as it revises other prudential standards, to review existing requirements placed on boards to ensure that they remain appropriate.

Links with other proposals

As the board is responsible for overall governance, oversight and strategic direction, this proposal overlaps with all the other proposals. The proposal to clarify the key role of board chairs in prudential standards overlaps with Proposal 2 (fitness and propriety) and Proposal 5 (board performance review), under which chairs would have explicit responsibility for the assessment process and for ensuring that recommendations are addressed and fed into succession planning.

InsidEntity Response
1. We support the proposal that APRA amends its prudential standards to include a clear articulation of the primary role of the Board, the Chair and Senior Management (Executives). 2. The problems as documented on the Discussion Paper does not state what could have been the root causes of the issues. 3. We can assume a number of issues with the boards that might include the following: a) Board members do not have sufficient Industry Knowledge,

b) Majority of Board members are not independent, scared that if they challenge Senior Management their membership might be terminated thereby losing the board fee,
c) Directors on the Board who are representing the Significant Shareholder/s, or
d) The company is lead by a significant CEO who they fear.

4. The fundamental principle that Boards must know is that Senior Management reports to them and not the other way. This issue is not only in Australia but in many jurisdictions and companies.

Proposal 7 – Board committees

Extend the current requirement for bank and insurer boards to have separate risk and audit committees, to apply to SFI RSE licensees as well. Repeal this requirement for non-SFI banks and insurers, allowing flexibility for smaller entities.

Mandate that only full board members can be voting members of APRA-required board committees.

Current requirements

APRA currently requires banking and insurance boards to maintain separate risk and audit committees. RSE licensee boards are only required to have an audit committee, whose responsibilities include risk. There is no requirement for a separate risk committee.

For all industries, there are no provisions that prevent non-board members of board committees, such as external advisers, from voting on committee matters.

Problem statement

APRA requires banks and insurers to establish separate audit and risk committees to help ensure that adequate time, focus, skill and experience are allocated to matters in line with three lines of defence principles. Consistent with contemporary good practice, most large RSE licensees have already established separate risk committees. In some instances where there is no separate risk committee, APRA has observed weaker risk oversight and risk capability.

APRA has observed the practice of external experts joining board committees of RSE licensees. These individuals can have specialist skills that are lacking among board members. APRA is not opposed to external advisers attending and advising committees. However, APRA considers that external advisers should not be full voting members, and they should not be relied upon to resolve critical board skills gaps.11

Addressing the problem

While having separate risk and audit committees is better practice, APRA recognises that this may create additional cost and complexity for smaller entities (non-SFIs). APRA therefore proposes to remove the current requirement for all bank and insurers to separate these committees.

For SFIs, APRA proposes to extend the requirement for separate committees to RSE licensees that are classified as SFIs. The aim is to sharpen the focus of large and systemically important RSE licensees on risk governance and underpin the effectiveness of the three lines of defence.

APRA also proposes to specify that only full board members can be voting members of APRA-mandated committees. This reflects APRA's view that boards should address gaps in skills and capabilities through appropriate director appointments, succession planning and training. Advisers may continue to attend committee meetings to provide expert advice and complement director experience. Restricting voting to full board members is intended to ensure clear board accountability.

Links with other proposals

This proposal links to Proposal 1 (skills and capabilities) and Proposal 5 (board performance review).

InsidEntity Response
1. We support all the 3 proposals advanced in the document with reasoning provided.
Our Platform separates Risk & Compliance Committee from Audit Committee which is aligned to your requirement for the SFIs.

Proposal 8 – Director tenure and board renewal

Impose a lifetime default tenure limit of 10 years for non-executive directors at a regulated entity.

Require regulated entities to establish a robust, forward-looking process for board renewal.

Current requirements

APRA standards require boards to have a formal policy on board renewal. These policies must consider whether directors have served for a period that could, or be perceived to, materially interfere with their ability to act in the best interests of the regulated entity. Requirements for RSE licensees are more prescriptive, with SPS 510 mandating that policies must state maximum tenure limits. The associated guidance states that APRA expects there are limited circumstances in which tenure limits beyond 12 years would be appropriate.

Problem statement

Appropriate limits on director tenure are an important part of good governance. Well managed turnover of directors facilitates stability, continuity and expertise – while also promoting fresh ideas and renewal. Overly long tenure is likely to erode a director's capacity to exercise impartial judgement and to challenge management effectively. It can limit openness to new ideas and different approaches and be a barrier to an unvarnished assessment of an entity's culture.

An APRA governance thematic review of ADI mutuals found that while many directors agree that long tenure can erode their ability to challenge management, some boards find it difficult to address these concerns effectively. Entities continue to convey to APRA that it can be difficult for chairs and directors to challenge colleagues on this issue.

Over the years APRA has invested considerable effort to address instances of overly long tenure in certain cohorts where this has been a widespread issue. While some progress has been made, APRA assesses that there remain almost 200 directors with tenure greater than 10 years, including almost 150 directors with tenure greater than 12 years. This does not account for instances in which a merger has effectively 'reset the clock' for director tenure. Around 30 directors have tenures over 20 years. To put this data in context, APRA estimates there are around 1,500 non-executive directors across all APRA-regulated entities. Approaches to board renewal are varied. While entities generally comply with the requirement to have a formal renewal policy, APRA has observed several weaknesses. These include lack of specificity about appointment processes, limited connection to board skills matrices, and a lack of early and effective succession planning.

Addressing the problem

APRA proposes to introduce a 10-year lifetime tenure limit on a regulated entity board for non-executive directors, with the possibility of an extension at APRA's discretion. This includes where an entity has undergone a merger. The purpose of this proposal is to establish a consistent and appropriate baseline in the prudential framework to which all regulated entities will be held.

APRA acknowledges there are genuine trade-offs associated with this proposal. Many directors of long tenure are highly experienced and make a strong contribution throughout their directorships. For this reason, APRA proposes to reserve the right to make case-by-case exceptions upon entity application. This would allow APRA to grant a two-year extension in limited

and exceptional circumstances. This approach seeks to strike a balance, recognising both the benefits and risks associated with long tenure.

Introduction of a 10-year tenure limit is consistent with contemporary governance benchmarks and the relevant literature, which suggest that independent non-executive directors should ideally serve for a maximum period of between nine and 12 years. Overseas prudential regulators have not set hard limits on non-executive director tenure, although several have issued guidance to indicate that director independence may be affected after 10 years on a board. APRA recognises that introducing a firm time limit would make Australia's framework more prescriptive. However, APRA considers this is justified because, unlike some regulators, it lacks formal power to address tenure through the reappointment process, and excessive tenure remains an issue despite considerable supervisory suasion.

In implementing this proposal, APRA will be mindful of the need to provide regulated entities with sufficient time to implement the new requirements. APRA would welcome feedback from industry on the type of transitional arrangements that may be necessary.

With respect to board renewal, APRA proposes to extend the current prudential requirements to explicitly require:

• consideration of the full cycle from nomination and appointments through to succession planning

• detail on director nominations, appointment process, length of term and maximum number of terms

• how results of board and director performance assessments will feed into succession planning and renewal.

These changes are intended to drive renewal of regulated entity boards, and ensure those processes are integrated with other relevant considerations such as skills and tenure. In supervising these new requirements, it is anticipated that APRA will focus on outcomes. As such, an entity can either maintain a separate renewal policy, integrate renewal into its fit and proper policy or adopt another process that the entity deems appropriate.

InsidEntity Response
1. We support a lifetime default tenure limit of 10 years for non-executive directors. 2. Not only that the overly long tenure would likely erode a director's capacity to exercise impartial judgement, to some extent the independence of a director would be questionable for periods in excess of 10 years. 3. Should APRA approves the extension for a director to serve on the board longer than 10 years, then the director must not be disclosed in any reporting as Independent.
InsidEntity Platform, automatically shows the director as Not Independent for a tenure longer than 10 years. This will have a downward impact on the overall score on the Company Rating for the Company.