Retail Banking
REMUNERATION REVIEW

Retail Banking Remuneration Review

Final Report

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Executive Summary

This is the Final Report of an independent review initially commissioned by the Australian Banking Association (ABA) in July 2016 to examine product sales commissions and product-based payments in retail banking in Australia.

The 2017 Review recommended substantial changes, which were designed to remove or reduce an unacceptable risk of promoting inappropriate behaviour that is inconsistent with the interests of customers. The proposals were holistic, addressing the industry's approach to remuneration, performance management and culture; and the leadership, governance and other capabilities required to support better approaches in respect of each. It was acknowledged that the proposals affected banks, and roles within banks, differently. Some banks believed, for example, that their culture was more closely aligned than others with the desired culture. However, the need for change within the industry was substantial and would take time. It was proposed that implementation should be completed by the performance year that began in 2020. The purpose of this review is to establish whether that deadline has been met.

In brief, the report concludes, with few exceptions, the industry's policies have changed in line with the letter and intent of the 2017 Recommendations for staff in-scope for this Review. In particular:

- Links between remuneration and sales are now rare and, where present, only indirect. Indeed, with few exceptions, the value of any variable remuneration payment secured by a seller is only very indirectly susceptible to their personal sales performance.
- The maximum variable rewards potentially available have been substantially wound back. Most banks, with few exceptions, now offer a maximum variable pay opportunity that is 40 percent or less of fixed pay for in-scope roles. One significant bank continues to offer a maximum variable pay opportunity that exceeds 50 percent of fixed pay for a small proportion of its home lenders. However, it has committed to reducing this immediately to 50 percent or less of fixed pay for new hires, and progressively to other home lenders during a brief transition period[1]. Some banks have removed altogether variable remuneration for some roles, especially Teller-like roles; and another plans to do so shortly.
- Performance assessments and access to variable rewards are now typically assessed on a 'whole of role' basis, having regard to both the 'what' and the 'how', which minimises the risk that good sales secured by poor behaviour is rewarded. These systems are better aligned, further reducing risks that staff will receive 'mixed messages'.
- Discretionary judgement by managers is now the dominant mechanism whereby performance ratings are assigned and any access to variable pay is determined, which reduces scope for gaming and breaks previously formulaic links between performance and rewards.
- Many banks have invested heavily in refreshing their values, consequence management framework, cultural expectations and leader, manager and staff capability to strengthen the focus on the customer. Most banks actively encourage staff to 'speak up' if they see something inappropriate and some further encourage staff to ask, 'should we' rather than just 'can we'.

These are substantial achievements, supported by substantial investments by many banks to better articulate a customer-centric ethos and to build leader and manager capability in support of it. The risks of mis-selling and poor outcomes for customers in retail banking are substantially reduced consequently. The

[1] New hires are henceforth subject to the 50 percent cap. The transition will allow orderly adjustments for some existing home lenders.

exceptions involve some aspects of the policies of a few banks and are concentrated in home lender roles. I call on those banks to move to full implementation as soon as possible.

The review has also been supported by a purpose-built independent survey of the perceptions of staff regarding bank culture. Although results vary somewhat between banks, the overall finding is that staff perceive bank culture to be more customer centric than sales centric. This is a pleasing result. However, a significant minority assessed their employer less favourably, implying there is still scope for improvement – possibly in respect of both internal communication and the lived experience of some staff.

Unlike previous reviews, aggregators and mortgage brokers are not in-scope for this review. This is because government policy and the regulatory environment favour continuation of sales volume-based commission payments. Introduction of a requirement that brokers act in the best interest of clients and removal of some additional payments previously linked to the value of sales are important countervailing factors. However, such payments substantially increase the risk of mis-selling compared to payments determined by the effort required to arrange a loan, which the 2017 review had recommended.

Although the changes at industry level since 2017 have been substantial, vigilance is required to ensure that the promise offered by these policy changes is realised consistently into the future. Reform to date has been supported by strong external pressures, including the findings of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry and regulatory responses to some high-profile compliance breaches. An issue for the review is 'what will sustain the pressure to achieve customer-centric culture and practices?' once memories fade, market conditions change and Boards and senior leadership of at least some banks come under pressure to better achieve the bank's strategic objectives. The current focus across virtually all banks on building their share of the mortgage market, coupled also with the need for banks to offer attractive remuneration to their home lenders against the background of the dynamics of the commissions-dominated labour market for mortgage brokers, pose particular challenges.

Sustaining a customer-centric focus will require continued efforts to ensure that each bank's lived culture aligns with its desired culture; and that each bank's leaders, managers and staff have the capabilities and attitudes necessary to manage any tension inherent in their desire to be customer centric while remaining profitable. Reputational and remediation costs are not small when things go wrong. Moreover, community trust is difficult to restore, once lost. Boards, industry leaders and regulators all have roles to play to check regularly that the letter and intent[2] of the 2017 Recommendations continue to be adhered to as time passes and the industry consistently demonstrates a customer centric, ethical culture. It is especially important that:

- The maximum achievable variable remuneration payments are always no more than (and preferably considerably less than for non-specialist roles) 50 percent of fixed pay;
- The proportion of variation in variable reward outcomes within a role explained by sales performance is less than 33 percent (noting that the role played by scorecards is much reduced when manager discretion finally determines performance management ratings and/or the scale of variable rewards – see also penultimate comment below);

[2] The Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (FSRC: *Final Report*) recommended that 'banks should implement fully the recommendations' of the (Sedgwick) Review in 'letter and spirit'. (FSRC: Final Report, Recommendation 5.5, Volume 1, p36 and p370.

- Assessments leading to variable reward outcomes are truly balanced between the "What" and the "How";
- Communications with staff credibly explain the rationale for all productivity and similar metrics, keep the focus on the achievement of good outcomes for customers, and avoid the perception that reporting to staff about such matters is simply a 'target /sales culture in disguise';
- Leaders and managers possess the requisite skills to administer discretionary schemes consistently and well and in support of customer-centric norms;
- The exercise of manager discretion is subject to strong oversight and an effective internal challenge function to ensure that judgements are consistently applied and are free from sales bias, unconscious or otherwise; and
- Banks are transparent and publicly accountable for their culture.

The report includes suggestions about how those objectives might be achieved.

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1 Introduction

1.1 Context of this Review

This is the Final Report of an independent review initially commissioned by the Australian Banking Association (ABA) in July 2016 to examine product sales commissions and product-based payments in retail banking in Australia.

The first report, the 2017 *Retail Banking Remuneration Review* (2017 Review[3]), made 21 recommendations (2017 Recommendations) which the ABA and several member banks committed publicly to implement[4]. These proposals were designed to remove or reduce an 'unacceptable risk of promoting behaviour that is inconsistent with the interests of customers'[5], and assist to address a 'significant trust deficit'[6] that key industry leaders believed had emerged. In effect, the social licence for banks to operate had changed and some practices were no longer acceptable to the public[7].

Recognising the scale of the proposed changes, the 2017 Recommendations included that banks should begin immediately and complete implementation by the performance year that begins in 2020[8]. The Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (FSRC: *Final Report*) recommended that 'banks should implement fully the recommendations' of the (Sedgwick) Review[9] in 'letter and spirit'[10].

The ABA commissioned an interim 'Assessment of Progress' that reported in February 2019 (the 'Interim Report'). It found that, although banks were moving at different speeds and the required scale of adjustment varied between banks, substantial progress had occurred in the industry overall to put policies in place aligned to the 2017 Recommendations, with further reform in prospect. Some uncertainty was evident, however, about how much the practices of some banks had changed to fully reflect the intent of their policy changes. Progress was slower and mixed in implementing recommendations in respect of third parties, especially Mortgage Brokers and Aggregators. This Final Report assesses whether the key policies and culture applicable to in-scope staff of retail banks now fully align with the 2017 Recommendations.

In summary, the 2017 Review examined product sales commissions and product-based payments then widely available in retail banking in Australia. Such payments were linked to the number or value of products sold, offered, or distributed to retail and small business customers. The Recommendations of

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[3] Sometimes referred to as the 'Sedgwick Review'. It can be found at https://www.ausbanking.org.au/retailremreview/

[4] See, for example, the ABA's statement at https://www.ausbanking.org.au/banks-to-change-the-way-they-pay-their-staff/

[5] 2017 Review, P 4.

[6] Ibid.

[7] As Section 2 of the 2017 Issues Paper explains, Australian banks were not alone in facing such criticism.

[8] Recommendation 1 of the 2017 Review states: *"I recommend that all banks begin to implement the recommendations in this Report as quickly as systems and other changes can be introduced. If transitional arrangements are necessary, full implementation should be achieved by no later than the performance year that begins in 2020."*

[9] FSRC: Final Report, Recommendation 5.5, Volume 1, P36.

[10] 'In my view, full implementation of the Sedgwick recommendations is an important first step towards improving front line remuneration practices. But implementation will only improve these practices if banks implement the Sedgwick recommendations both in letter and in spirit' op cit, p370.

the 2017 Review built on the Future of Financial Advice (FOFA) reforms[11]. They also suggested the principles that banks might apply when structuring remuneration more generally and addressed related issues concerning bank culture and approaches to performance management.

1.2 Scope of this Review

The 2017 Review specifically examined the arrangements that led to incentives, commissions and bonus payments (variable reward payments) for retail staff of banks (Tellers, Sellers and their supervisors and near managers (Managers)) as well as third parties (including Brokers, Aggregators, Franchisees, Introducers and Referrers) and made recommendations intended to reduce the risk that practices current at the time could lead to poor outcomes for customers. These roles remain in-scope for the current exercise except for Mortgage Brokers and Aggregators. The Recommendations in respect of the latter roles have been excluded from this final assessment because key regulators subsequently adopted a different approach and banks are therefore generally non-compliant with those elements of the 2017 Recommendations[12]. The in-scope roles may deal with a range of products, including various deposit accounts and loans such as mortgages, and a range of insurance products, including consumer credit insurance (CCI).

A key principle of the 2017 Review (and the Issues Paper that preceded it) is that rewards and incentives arrangements do not operate (and are best not assessed) in a vacuum. They:

- *'Work alongside (and may, in part at least, rely upon) the formal performance management system, which is typically designed to provide clarity to staff about what is expected of them and facilitate a measure of accountability to more senior managers; and*
- *Are discharged in the context of each workplace's culture (as, indeed, is the performance management system)'[13].*

A feature of the approach proposed in the 2017 Recommendations was that banks should 'address the issues holistically, meaning that they [should] each act to ensure that their approaches to remuneration, performance management, leader development and cultural renewal are aligned' [14]. The 2017 review also said:

'Effective leadership is key. Leaders drive culture. Whether they do it by accident or design, and whether culture is set by those at the top of the organisation or by "local leaders" in each work group, depends on the credibility, consistency and quality of the systems and governance senior leaders put in place'[15].

This was reinforced by the findings of the Interim Report, which suggested that many banks were in transition such that changes to practices in work groups may have lagged their policy changes. I recommended in 2019 that the final review should be conducted in the first half of 2021 and that it should be supported by 'appropriate data… not only about then current policies but also about how they are

[11] Corporations Amendment (Future of Financial Advice) Act 2018.
[12] Recommendations 16-19 of the 2017 Review. The 2019 Interim Report noted that some progress had been made to implement relevant Recommendations. A critical exception was that banks typically continued to pay mortgage brokers value-related commissions (upfront and trail). There has been no further assessment made for the purposes of this review. Third parties are discussed further in Sections 3 and 4.
[13] Issues Paper, section 2.2, p13. See also section 5.1 of this report.
[14] 2017 Report p (i).
[15] 2017 Report, p5.

implemented in practice, and the state of contemporary bank culture'[16]. The scope of this review has been broadened compared to the first two reports to include the development and administration of a purpose-built survey of staff perceptions of certain aspects of each bank's culture. This valuable resource has enabled a more systematic assessment of relevant aspects of bank culture than has been possible to date. Previously, consultations with members of the FSU have provided useful insights into matters of this kind. Examples of some non-customer-centric practices cited in the 2017 Issues Paper and the two subsequent reports were heavily informed by these consultations and the evidence members provided to support them.

The Terms of Reference are set out in Appendix D. In summary, this work involves the collation and analysis of three primary sources of data, namely:

1. Responses to a Questionnaire that was designed to capture information about each bank's policies relevant to an assessment of their implementation of the 2017 Recommendations, together with any supporting evidence banks provide.
2. Interviews with the Senior Leaders of each bank intended to ensure their policies, their approach to securing their desired culture, and the support available to build leader and manager capability are properly understood.
3. Staff responses to a purpose-built Staff Survey designed to ask how sales or customer centric staff perceive their bank's culture and practices to be.

1.3 Approach and Conduct of the 2021 Review

As noted previously, a significant data gathering exercise again supports this assessment. However, the data gathered has been expanded significantly this time to include staff perceptions of aspects of bank culture.

As with earlier reviews, a questionnaire was issued to each bank seeking information about their arrangements regarding performance management and variable remuneration in respect of in-scope staff, their near managers and more senior managers. Information was also sought about each bank's assessment of their current and desired culture and the steps they take to build awareness and capability in support of any changes they seek that affect in-scope staff. The Questionnaire was issued on 28 January 2021, with responses requested by 26 February 2021. A copy of the questionnaire is available on the Review website[17]. Banks were asked to support their responses with evidence and usually provided a substantial volume of documentation. Additional material was also subsequently requested by us to inform our understanding. Over 600 documents were provided in total. Seventeen member banks, including the four largest banks, responded to the questionnaire[18]. Our understanding of each bank's circumstances, intentions and practices has been greatly assisted by subsequent discussions with senior representatives of each bank, at times including the CEO.

In addition, a survey was developed and administered to in-scope staff to capture their perceptions of bank culture and practices relevant to the review. This was a recommendation of the Interim Report in 2019.

[16] Interim Report, section 2.3.1, p13.
[17] https://www.ausbanking.org.au/priorities/retailremreview/
[18] Information about the policies of an an additional bank, which had declined to complete the questionnaire because of resource constraints, was obtained during an interview with its senior leaders. Staff of that bank participated in the perceptions Survey.

Development of the survey was oversighted by the ABA with support from specialists drawn from a large number of banks[19] that comprised the Remuneration Review Survey Working Group[20], and a Secretariat supplied by the Nous Group. I was heavily involved in survey design, specified the objectives it was to address and, consistent with the independence of this review, exercised final sign off rights. Ten banks, typically the larger banks, administered the survey directly to their in-scope staff and provided the raw responses to the Secretariat for analysis. The Secretariat administered the survey to in-scope staff on behalf of 8 banks. Respondents were guaranteed the results would not allow individual responses to be identified irrespective of how the survey was administered to them. The survey was open between 15 February and 5 March 2021. The launching time varied between the banks, but staff had approximately two weeks to complete the survey.

The population for the survey was defined as customer-facing sellers in in-scope roles and their near managers. Around 37,000 staff are estimated to be in-scope. Some 13,760 effective responses were received, a respectable response rate of 37 percent. The results[21] are summarised in section 5.2.3, with a fuller presentation of the survey questions and findings available in Appendix A. The survey results provide statistically robust insights at the population level, some of which surprised some banks. Pleasingly, after the data was cleaned, banks typically responded to a surprise result with 'why is that so?' rather than 'that can't be!'.

As with both previous Reviews, I have been assisted greatly by consultations with the leadership of banks at multiple levels and discussions with some members of the Financial Sector Union (FSU). These have provided an invaluable perspective 'from the banking chamber'.

The focus of this report is at the level of the industry, and examines the policy and practice changes that banks have adopted, taken as a whole. The report provides indications of the range of practices and policies in place, where this can be done without identifying specific banks. I have separately provided direct, individual feedback to some banks about the completeness of their interpretation of the 2017 Recommendations and/or the pace of their reform efforts.

1.4 Acknowledgements and thanks

Participation in this process requires a substantial commitment of time and resources by the member banks of the ABA to help develop and respond to the questionnaire, assemble supporting documentation, and respond to additional requests for clarification or documentation. Similarly, significant efforts were required to assist in the development and administration of the staff survey. The assessment has only been made possible because of the generous contribution of time and ideas from many quarters. I especially thank participating banks for the timeliness and comprehensiveness of their responses to requests for information, for their active support of the survey of staff perceptions, and for the cooperative spirit in which our subsequent exchanges took place.

I also thank the more than 13,760 retail bank staff who took the time to respond to the survey, members of the FSU that contributed their perspectives in focus group discussions, and Ms Angrisano, National

[19] This group was known as the Remuneration Review working group.
[20] This is a subcommittee of the ABA's Remuneration Strategy Working Group.
[21] Responses were weighted by age, gender and bank to adjust for any non-response bias and ensure inferences and estimates cited in this report can relate to the in-scope population as a whole, not just the sample.

Secretary of the FSU, for providing a confidential submission and arranging the group discussions with members.

As usual, I was greatly assisted by subject matter experts who provided invaluable technical advice namely: David Heazlett of AON in respect of the questionnaire and remuneration matters; Gilbert + Tobin in respect of legal matters; staff of the ABA, who secured resources, contributed to the development of the staff survey, and managed initial logistics; Peter Ellis and Li Zhaoyuan of Nous Group who helped to develop, administer and analyse the staff survey; and, most especially, Tony Fiddes, Ed Hughes, Dinushki Tennakoon, and Lori Rayner of Nous Group who comprised the members of a small, independent secretariat, who lent good humour, deep expertise and commitment, and professional support to this work. Their assistance was critical to getting this Report completed to a professional standard and on time.

All parties have respected the independence of this Review. Of course, the opinions contained herein are my own. This Report has been based on information provided by the banks and other parties which I have assumed for the purposes of this Report is accurate and complete. However, neither I nor any other person involved in the preparation of this Report undertakes responsibility arising in any way from reliance placed by a third party on this Report. Any reliance placed is that party’s sole responsibility.

1.5 Report structure

This report contains five sections:

1. Introduction;
2. Overview: are we there yet?;
3. Performance Management;
4. Variable Remuneration structures for in-scope staff; and
5. Workplace culture.

It is supported by five Appendices:

6. Retail banking staff perceptions of remuneration practices;
7. Implementation of the 2017 Recommendations;
8. Level of discretion applied in performance management and variable remuneration;
9. Terms of Reference; and
10. Glossary.

2 Overview: are we there yet?

2.1 What did the 2017 Review recommend 'there' should look like?

The 'social licence to operate' of many financial institutions, in Australia and elsewhere[22], was under serious challenge in 2016, when this review was initiated. In Australia, for example, the FOFA Reforms[23] were underway. Adverse public commentary about the practices of a broad range of financial institutions was occurring regularly, which helped to erode public trust in many financial institutions. This ultimately led to the establishment in December 2017 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. The January 2017 Issues Paper reported that concerns had been expressed about a sales rather than customer culture in retail banking and about products being sold inappropriately to customers by consumers, consumer advocates, media and members of parliament as well as other stakeholders[24]. Senior banking industry figures, including the Governor of the Reserve Bank of Australia[25], publicly acknowledged the existence of a 'trust deficit' which, they argued, the industry should address urgently.

Some in the industry, including the ABA, argued in submissions to the 2017 Review that change was required across the retail banking industry and, for competitiveness reasons, should be pursued on an industry wide basis. However, collaborative action may risk contravening the *Competition and Consumer Act.* The ABA proposed that the 2017 Review could provide a way forward. But, in the absence of legislative change (the timeliness and scope of which was uncertain), each bank would need to decide whether to embrace the 2017 Recommendations having regard to its own assessment of risk and reward in doing so.

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[22] Although the circumstances are different, concerns about sales cultures in banks was not unique to Australia at this time. For example, the Issues Paper, at p10, reports concerns that both the US and UK regulators were dealing with around this time.

[23] FOFA introduced a range of legislative reforms in respect of the provision of financial advice (both general and personal advice). FOFA was a regulatory response to a series of product and services provider collapses following the Global Financial Crisis. Among other things, conflicted remuneration arrangements were banned such as commission payments relating to product sales and financial advice. At the time, the relevant Minister, the Hon Chris Bowen, stated that two overriding principles guided the reforms, namely: 'financial advice must be in the clients best interests... distortions to remuneration, which misalign the best interests of the client and the adviser, should be minimised.' (*The Future of Financial Advice information Pack*, 26 April 2010, p2) - see Section 2.3.2 of the Issues Paper

[24] 2017 Review, p10.

[25] For example, The Governor of the Reserve Bank of Australia had commented: "In terms of behavioural issues…I think it comes down to incentives within the organisations, and that is largely remuneration structures…If there was one thing I could focus on…is making sure that the remuneration structures within financial institutions promote behaviour that benefits not just the institution but its clients". See: http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/Four_Major_Banks_Review; http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/RBAAnnualReport2015/Public_Hearings

The 2017 Review did not find sufficient evidence of systemic risks of poor outcomes for customers to support an outright ban on all product-based payments in retail banking. Nonetheless, it argued that certain practices carry an 'unacceptable risk of promoting behaviour that is inconsistent with the interests of customers and should therefore be changed'[26]. The review took a holistic approach and proposed:

'… each retail bank should review their approaches to tasking and managing the performance of staff, the way they structure variable rewards and incentives payable to them and the workplace experience of retail staff to ensure these systems reinforce each other and are progressively aligned with the recommendations below.

Adoption of these recommendations will mean, over time, that:

- *Incentives are no longer paid to any in-scope retail staff based directly or solely on sales performance (see Recommendations 2 and 7);*
- *Instead, eligibility to receive any personal variable reward and incentive payments will have regard to an assessment of that individual's contribution across a range of measures, of which sales (if included at all) will not be the dominant component (Recommendations 3, 4, 5, and 6) and the maximum available payments will be scaled back significantly for some roles (Recommendation 8);*
- *Retail bank culture will be demonstrably ethically and customer oriented (Recommendation 9);*
- *A significant investment will have been undertaken, as necessary, to ensure that performance is managed consistently with such a philosophy, supported by proactive steps to develop leadership and management skills at all levels so that management practices match the intent of the recommendations (Recommendations 10, 11, and 12); and*
- *With clear and consistent leadership shown by the Board and the most senior managers of the bank (Recommendations 13 and 14). '* [27]

The numbering of recommendations, above, aligns with the 2017 Review. The 2017 Review also noted that the nature of the task facing banks to align their policies with the Recommendations of the 2017 Review was not uniform:

'Both remuneration practices and the extent to which culture is dominated by sales vary significantly across banks, and sometimes even between groups or roles within banks. Accordingly, the implications of adopting these recommendations will be different for different banks.'[28].

2.2 We're nearly there...

In summary, the 2019 Interim Report found:

'Although the pace of change varies, substantial progress has already occurred in the industry overall to put policies in place aligned to my Recommendations. The clear trend is towards policies that will be fully consistent with the Recommendations in respect of in-scope staff well in advance of the target date, that is, before the performance year that begins in 2020. Of course, it will be for later judgement whether that promise is realised in all cases. Moreover, as previously noted it is too early to assess how well bank

[26] 2017 Review, p4.
[27] 2017 Review, p7.
[28] 2017 Review, section 2.4, p.6.

practices and bank culture have changed to conform with the revised policy intent. There are reasons to believe that the pace of change even within a bank may be uneven.'[29]

Details will be fleshed out in Chapters 3, 4 and 5. In summary, however, the clear finding of this review is that, with few exceptions (which are further discussed below and in subsequent chapters), the industry's policies have changed substantially and are typically in line with the letter and intent of the 2017 Recommendations for staff in-scope for this Review[30]. The risks of mis-selling and poor outcomes for customers in retail banking are substantially reduced consequently. As previously noted, the scale of policy changes required has varied between banks and between roles within banks. Conscious of that reality, the focus of this assessment has been on the end state banks have reached, with less concern about whether there has been change for its own sake if little was required.

Although the changes at industry level since 2017 have been substantial, vigilance is required to ensure that the promise offered by these policy changes is realised consistently into the future. This will require continued efforts to ensure that each bank's lived culture aligns with its desired culture; and that each bank's Board, leaders, managers and staff have the capabilities and attitudes necessary to manage any tension inherent in their desire to be customer centric while remaining profitable.

Pleasingly, this review has found that, in respect of in-scope staff:

- Links between remuneration and sales are now rare and, where present, only indirect.
- Toxic mechanisms like accelerators[31] linked to sales have gone.
- Scorecards, where they are influential, are typically product neutral (with few exceptions, for example in respect of the sale of insurance products in a few cases).
- Performance and access to variable rewards are now typically assessed on a 'whole of role' basis (see section 2.3.1, below, for a discussion of the contemporary role of scorecards).
- Typically, (though it must be said not always) the same assessment instrument is used to rate employees both for performance management purposes and to determine access to any variable reward, reducing the risk that staff will receive 'mixed messages' about what is valued.
- There is a strong focus on continuous assessment, performance management and coaching of staff rather than periodic 'high stakes' assessments.
- Both the 'what' and the 'how' are assessed to minimise the risk that good sales secured by poor behaviour is rewarded (poor behaviours will typically disqualify an individual from access to variable reward, though some banks allow exceptions in very limited circumstances or reduce the reward that might otherwise have been paid in line with the severity of the offence[32]).

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[29] 2019 Interim Review, p5.

[30] Which excludes mortgage Brokers and Aggregators.

[31] An arrangement whereby a higher rate of reward is earned with higher levels of performance, for example increasing volumes of sale. The review also captured 'accelerator like mechanisms' i.e. mechanisms that had a similar effect irrespective of how the mechanism is described.

[32] If disqualification for reward applies, behaviours act as a gate opener for reward. Discretion about how to respond to a conduct breach is sometimes applied in a gateway model to enable managers to respond fairly to, for example, an inadvertent or technical breach. Alternatively conduct matters may operate as a modifier, viz variable remuneration that an individual might otherwise be entitled to receive is reduced in proportion to the assessed severity of the breach. Modifier models examined by the review always include an option of 'nil' variable pay for sufficiently poor behaviour.

- Discretionary judgement by managers is now the dominant mechanism whereby ratings are assigned and any access to variable pay is determined for virtually all roles, which reduces scope for gaming and breaks previously formulaic links between performance[33] and reward.
- For almost all banks the sum of money an individual may receive as variable rewards is linked to group or entity level performance, not solely personal performance (and has regard to a mix of financial and other indicators). Effectively, with few exceptions in respect of particular roles[34], an individual's performance will affect the share they receive of a pool of funds that is not known in advance and, if a seller, is only very indirectly susceptible to their personal sales performance.
- Some banks have removed access to variable remuneration altogether for some roles such as Tellers and equivalent front-line staff. Another plans to do so shortly.
- Maximum achievable variable remuneration has been scaled bank dramatically and is now (or, in one case, shortly will be) typically 50 percent or less of fixed remuneration, substantially so for non-specialist roles (noting that 50 percent is a benchmark, not a target).
- Recognition schemes (which provide small sums or gifts) are mostly values or behaviours based nowadays, with a few exceptions.
- Many banks have invested heavily in refreshing their values, consequence management framework, cultural expectations and leader, manager and staff capability to strengthen the focus on the customer. Most banks actively encourage staff to 'speak up' if they see something inappropriate and some also encourage staff to ask, 'should we' rather than just 'can we'.

The above list represents a very substantial number of achievements in support of the objectives of the 2017 Review. Moreover, the results of the staff survey show that employees generally perceive that their employer is more customer-centric than sales-centric, and in some cases by a significant margin[35]. Several senior staff told us during interviews that their bank responds to customer concerns differently these days than it did 5 years ago, citing the industry's response to vulnerable customers during COVID-19 as an example that generates particular pride.

However, while acknowledging that in each of the cases cited below substantial progress has also been made, further action is needed to better meet either the letter or the spirit of 2017 Recommendations in four areas:

- *Financial measures* – a few banks had assigned an effective weight to financial measures in their scorecards for at least some roles that exceeded the recommended 33 percent. For one bank this occurred because the scorecard specifically assigned a higher weight than recommended. More typically it occurred because the scorecard included 'customer' or 'productivity' measurements that could be perceived by staff to be financial in character (for example, activity measures such as

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[33] Many schemes examined for the 2017 Review included mechanisms whereby performance relative to a sales target led to a calculatable amount of variable reward, subject to any gateways. Once a pre-determined sales threshold had been crossed, an individual had great capacity to determine their variable reward if they wished. There are almost no schemes of that kind currently. Moreover, where schemes are formula driven in respect of at least some elements of a scorecard, which tend to be in respect of home lenders, the size of the reward pool is rarely within the control of an individual staff members to determine. Reward pools are now typically constructed along similar lines to a group or entity level profit share mechanism.
[34] In a few banks, the schemes that apply to home lenders still determine variable remuneration more formulaically than other roles.
[35] the Survey also reveals that a significant minority of staff believe their employer has further to travel to become customer centric.

general insurance sales or mortgage settlements). However, even after such a reclassification[36] the apparent weight was typically not dramatically more than 33 percent[37]. Moreover, the role of scorecards has changed for many banks and the significance of this point as a reflection of an industry norm should not be overestimated (see discussion in section 3.2.2 below).

- *Customer measures* – many banks are experimenting with customer-oriented metrics beyond the various manifestations of the Net Promoter Score (NPS). Greater use is being made of customer feedback and complaints, not only to improve product offerings and processes but also to assess the quality of service and the relevance of the assistance provided to customers by teams or, less frequently, individual bankers. A small number employ a mystery shopper to assess staff interactions with customers. Most employ call monitoring and/or ex post examination of product application documentation, records of conversations, and the like to assess the 'quality' of a conversation between customer and staff member. But, as an industry, there has been limited progress to capture data correlated with customer outcomes achieved (other, for example, than the assumption that a mortgage enables a customer to satisfy a need to purchase an investment property or a home or that taking out insurance cover reduces a customer's financial risk) and some staff reported to us that they continue to doubt assurances that a conversation that does not result in a sale is viewed as a 'success' by their manager.
- *Leaderboards* – almost all banks[38] state they have discontinued the use of formal leaderboards to monitor and share data about the performance of teams or individuals compared to targets. Leaderboards can be interpreted by staff as a device, including through peer pressure, to encourage individuals to achieve targets, including sales targets, possibly at the risk of delivering a poor outcome to customers. However, a significant proportion of staff in every participating bank responded to the staff survey[39] that either a leaderboard was in use in their workplace, or they knew who were the best and the worst sellers in their workplace. This implies there is a risk that staff perceive the messages they receive about the significance of sales performance to be different to the message that senior managers intend to send. Some staff[40] that we consulted believed that their manager has changed the language but not the intent of their messaging. Intriguingly, however, in two cases, staff in the survey nonetheless rate their bank relatively highly for their customer centricity despite significant numbers confirming continued use of leaderboards, implying in each case that the bank's cultural messaging is paramount about the relative importance of giving good service to the customer.
- *Maximum achievable variable reward* – the 2017 recommendations favour a substantial reduction in the maximum variable reward that should be available to in-scope staff compared to the practices of 2017. The 2017 Review opted not to set a hard target but proposed that the industry should progressively reduce the maximum variable rewards available to in-scope roles, as a

[36] It was not always possible to identify the weight to be reclassified, typically because the measure was one of several within a group.

[37] See Table 2, section 3.2.3.1.

[38] Leaderboards compare the performance against target of individuals with others within the team/business unit. Only 1 bank stated in their response the questionnaire that they retained leaderboards. Some others acknowledged that they provide teams with data about their performance relative to other teams.

[39] Across all banks, 15 percent or more of staff responded positively to questions in the staff survey about either the existence of leaderboards or their knowledge of the identity of the best and worst sellers in their workgroup. (See Appendix A for details).

[40] This observation needs to be treated with care. Statistically, the survey responses are a more reliable indicator of industry level perceptions. The Survey responses reveal that a significant minority of staff believe that their bank has a way to travel to become customer centric.

proportion of fixed pay, and that such pay should be ‘a relatively small proportion of fixed pay’ by the 2020 performance year. Virtually all banks that offered variable remuneration in 2016 have taken substantial steps to comply with this recommendation, instituting a significant rebalancing between fixed and variable pay for some roles. Some banks have not had a cap on variable remuneration achievable by an individual at any point during the three reviews but in practice do not pay variable rewards to in-scope staff that exceed the proposed cap. In a few cases, banks that previously offered variable reward to some in-scope roles no longer do so (typically Tellers and other customer service or sales roles in branches and contact centres). Across the sector, nearly all banks now have a maximum variable remuneration opportunity that does not exceed 50 percent of fixed pay and, with a few exceptions, is much less. In my view 50 percent for specialist bankers is an upper limit, not a target, and with a bias towards something significantly lower, especially for non-specialist roles. Although their variable pay maximum opportunity is now substantially lower than previously, one significant bank, however, currently offers a maximum for some roles, typically associated with home lending, that exceeds 50 percent of fixed pay, albeit for a relatively limited number of staff. It is pleasing that this bank has committed to reducing this maximum to no more than 50 percent of fixed pay – immediately for new hires and progressively over a relatively brief period for others currently eligible for more than 50 percent. I sincerely hope that each bank accepts that ’50 percent’ is recommended as a cap, not a target to which all should aspire!

2.3 Vigilance is required into the future

Three themes have given us cause for thought as this review has unfolded. Each poses a challenge to an informed interpretation of current practice. Each represents an area that will repay vigilance into the future to ensure that the objectives of the 2017 review continue to be achieved. These can be summarised:

- Manager discretion has advantages but also poses challenges that require careful and continuous attention;
- Painstaking, ongoing attention to culture and communication are keys to ensuring a bank remains profitable, adhering to its strategy yet customer-centric; and
- The industry has survived a maelstrom of criticism and change. It needs consciously to ensure that the focus on the customer is not diluted over time.

2.3.1 Manager discretion requires support

Increased recourse to manager discretion was a clear trend at the 2019 Interim Review and is strongly in evidence in this review. Such discretion can be exercised at one or more of several points in the end-to-end process to assess the performance of an individual and, ultimately, to allocate variable pay. These include, for example: when assessing an individual’s behaviours relative to a standard required to open a remuneration gateway; when determining an individual’s personal performance or development objectives (sometimes referred to as Key Performance Indicators); when assigning a rating against specific elements of a scorecard; when assigning an overall rating to an individual’s performance, with or without the assistance of a scorecard; when determining an individual’s entitlement to a specific amount of variable pay. Sections 3.2.2 and 4.2.4 have a fuller discussion of the approaches currently employed.

Manager discretion is not inconsistent with the 2017 Recommendations. It has several advantages. A manager can more readily consider the ‘how’ as well as the ‘what’ of an individual’s achievements when discretion is exercised. Discretionary systems are less open to gaming than formulaic ones, which, amongst other things, can encourage sales banking or overzealous seller behaviour to boost bonus payments.

Discretionary systems more readily enable a manager to consider the 'degree of difficulty' staff experience in addressing the KPIs embedded in their scorecard or in otherwise addressing performance expectations[41]. Discretion can give appropriate weight to qualitative indicators or elements of performance that are difficult to measure reliably and more readily lends itself to a holistic assessment than a formulaic one, especially as conditions change.

However, discretion also poses challenges, particularly in ensuring consistency between managers and equitable treatment of individuals.

Discretion brings complexity and can lack transparency. Discretion reduces the significance attached to the weights assigned to particular elements of scorecards. Discretionary decision making may appear to emerge from a 'black box'. Some schemes require a complex assessment to be made against a significant number of quantitative and qualitative indicators – the incentive managers face in reality to simplify the factors considered in making their judgement could be strong. Boards (and staff) need assurance that managers can demonstrate that their judgements align with the intended performance norms and customer-centric behaviours and are consistently applied between individuals.

Most banks provide training, coaching and other support to managers. They also seek to clearly communicate with affected staff about how the process should work and their rights to 'speak up' if their experience is inconsistent with the professed norms.

Most, though not all, have also established formal calibration / moderation arrangements intended to ensure consistency and equitable treatment. The effectiveness of these arrangements depends on the insightfulness of managers, the quality of their judgements and the documentation they provide to support them, and the creation by leaders of a 'psychologically safe' environment that both permits and requires respectful challenge. The trend towards continuous performance assessments poses additional challenges for how calibration sessions should evolve to ensure consistency in assessments given to staff throughout the year. This issue is further discussed in section 4.2.1.

Both initiatives (viz. training / communication and calibration / moderation) are expensive and time consuming. They need to be pursued consistently, over time. It is far from clear to me why participation in well-designed calibration / moderation processes would not be mandatory at all banks that rely on manager discretion.

The involvement of parties not directly in line roles in calibration can provide an important challenge perspective. Human Resources (HR) and the risk functions have important roles to play in challenging the judgements made, including to surface any conscious or unconscious biases in respect of these matters. Internal audit could possibly play a role auditing that calibration is working as intended. It could also be wise for external oversight bodies such as APRA and ASIC to pay particular attention to how banks are ensuring their performance management arrangements, variable remuneration practices and lived culture provide incentives in favour of ethical conduct and a focus of the customer, not simply sales, including in retail banking. One area of examination, for example in the context of ASIC's Close and Continuous Monitoring Program, could be whether challenge roles are discharged effectively within the calibration / moderation arrangements. Conduct risk can too easily be viewed as a compliance rather than an ethical

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[41] During interviews, several banks cited the exercise of such discretion during various COVID-19 events as an illustration that the achievement of sales or other targets were no longer an overriding consideration in the assessment of performance and eligibility for rewards, whether financial rewards or otherwise.

issue. Leaders[42] need to ensure that a narrow interpretation is not adopted in their organisation. More than one bank[43] has found in recent years that a collaborative culture can diminish the value placed on 'challenge', to the entity's detriment.

2.3.2 Banks still need to run profitable businesses - Communication and Culture are key

A stable banking system is essential to support the effective operation of the Australian economy. Cost control, adequate and profitable sales, effective management of risk and adequate reserves are key to securing that objective. Many banks have incorporated what they aim to be productivity measures into the scorecards or other assessment criteria used to monitor performance and assess individuals or teams for access to variable rewards. These are typically activity measures of various kinds – examples include the time taken from loan application to approval, the number of conversations conducted with customers, the proportion of transactions executed digitally (although some banks view measures like this to be 'customer' metrics, the validity of which inference may vary between customers), amongst others. Many also employ sales targets of some kind, especially at more senior levels within the organisation. Understandably, a many banks identify as a strategic objective, an increase in their bank's share of the home mortgage market – but this should not come at the cost of customer outcomes (and it is mathematically impossible for every bank to attain such an objective). As a generalisation, executive scorecards designed to focus on the relative position rather than the absolute outcome, risk placing undue pressure on frontline staff to make sales when executives are not meeting their targets.

As time passes, it will remain important that communication from senior leaders about such matters does not inadvertently convey pressure to sell or pressure to pursue productivity measures irrespective of a customer's needs. A lesson from the responses to the staff survey developed for this review is that authentic and consistent values-based messaging from the top down is powerful in conditioning behaviour. It was remarkable, for example, that one or two banks whose staff believed they could identify the best and worst sellers (possibly because of the unauthorised existence of a leaderboard) nonetheless perceived their bank as being relatively customer-centric. In effect 'tone from the top' was seen to counter a possible bias towards sales inherent in the use of a leaderboard.

A sales culture was deeply embedded in the DNA of many (not all) banks in 2016. It had built up over years, including in response to the objective of regulators that Australian banks should be 'unquestionably strong' – an objective that stood Australia in good stead during the Global Financial Crisis of 2008. Against that background and their lived experience, some staff are not fully convinced that the changes their leaders have promulgated since 2016 are yet permanent. Moreover, culture is not 'set and forget'. Virtually all banks accept that cultural change is a journey and, even when a state is achieved of high alignment between the lived and desired cultures of an organisation, continual reinforcement is the key to preserving that state. Most banks have plans to continue to invest substantially in leader and manager capability to achieve their desired customer-centric culture and practices into the future.

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[42] The Board and, more directly, the CEO and their direct reports.

[43] The Prudential Inquiry into CBA found that a key cultural theme was "an overly collegial and collaborative working environment that lessened constructive criticism" (APRA, *Self-assessments of governance, accountability and culture,* May 2019, p7). Other major banks have also publicly stated in their self-assessments on governance, accountability and culture, that a collaborative culture can at times create a reluctance to challenge outcomes in the bank.

2.3.3 What will sustain the incentives banks currently face to 'put the customer first'?

The pressure the industry has faced in recent years to reform practices and cultures to reduce the risk that staff place sales above customer interests has been substantial and sustained. Some of this pressure has been self-generated as the ABA and senior industry leaders have reflected on the performance of their industry and the need to build trust and strengthen their social licence to operate. However, the external pressures to change have been substantial and pervasive. They include the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, increased regulatory oversight occasioned by those events but also by some significant regulatory lapses by some banks, and possibly, in respect to roles within scope, even this review process and the public reporting associated with it. It is inevitable that attention (both internal and, also, externally driven) will be diverted elsewhere as time passes and conditions change. A question we have pondered is: what sustains the pressure to remain customer-centric as time passes and those external forces dissipate or fade from view?

The answer to that question is multi layered and, most likely, still a work in progress. It seems likely, for example, that customer expectations of what kind of service is acceptable have been heightened and are now deeply entrenched. Empowered customers can help keep the industry focused. Regulatory reforms to improve customer access to data[44] and facilitate (sufficient) switching between banks can give expression to such empowerment. Competition from new entrants into the payments system is also likely to preserve the pressure on the industry to maintain the trust of their customers.

Nevertheless, leaders would be wise to adopt and promulgate an attitude similar to 'lest we forget' by frequently telling stories that remind staff of the consequences for the bank and for customers of poor practices in the past. Reputational and remediation costs are not small when things go wrong. Moreover, community trust is difficult to restore, once lost.

Indeed, the lesson of history is that leaders matter. Just as the current leadership of key banks have initiated the reforms reported upon in this review, new leadership responding to different external conditions or other factors can take their banks in different directions over time. There is always a risk, for example, that a significant bank or a significant number of banks that are seen to be failing to deliver against their strategic goals may adopt stances that staff perceive shift the balance back towards a too sales-centric culture.

It is impossible to speculate how likely is such an outcome. However, there are scenarios in which it becomes more likely than seems to be the case currently. One not wholly implausible scenario could be associated with the current objective that many banks have of growing their share of the mortgage market, for example. Not all banks can achieve such an objective simultaneously, which could provide such a trigger in some circumstances. Options available to attempt to boost market share include: (a) changes in the variable remuneration banks offer their home loan sellers that more directly link payments to personal sales or (b) placing greater reliance (possibly with enhanced payments) on third party channels that are

[44] The Australian Government introduced the consumer data right (CDR) in the banking sector to improve consumers' ability to switch products and services by enabling consumers to safely share their existing banking data with a prospective bank or CDR-accredited website/app. Some small banks have argued to the review, however, that the costs of full participation in CDR are prohibitive for them, which limits their capacity to offer prospective customers an efficient switching channel inwards compared to their legal obligation to facilitate the smooth exit of customers to other institutions.

remunerated on a commission basis under the current regulatory arrangements. Commissions linked to sales value (rather than to the effort required to effect the sale) increase mis-selling risk[45].

Boards and regulators need to remain vigilant to ensure that ethical conduct and a focus on good outcomes for customers remain the priority as banks respond to changing market dynamics. Regulators need oversight arrangements that enable them to be satisfied that conduct risks[46] – defined broadly to include both legal compliance and mis-selling risks- are adequately managed and subject to effective internal monitoring by each bank's risk function. I have suggested previously that regulators could usefully periodically investigate the effectiveness of challenge functions within banks to ensure that calibration and moderation functions work as intended. In addition, publication of data that throws light on behaviour towards customers could also assist, such as ASIC data in relation to bank performance against ASIC's approved standards regarding Internal Dispute Resolution procedures. Greater transparency about bank cultures could also assist. Options include a commitment by banks to regularly survey staff and publish the results about staff perceptions of culture using instruments similar to those adopted for the staff survey developed for this review. The ABA could usefully facilitate such a development. There may also be a role for APRA.

2.4 Where to next?

The purpose of this section is not to repeat the analysis of preceding sections but to bring together some thoughts drawn from the preceding analysis about next steps required to reduce the risk that the good work of recent years may be unwound as memories fade and conditions change. I make the following 6 concluding observations and strong suggestions about further steps to ensure that the pro-customer orientation the industry currently displays can be maintained and enhanced:

1. A few banks have been assessed as not having fully implemented one or more of the 2017 Recommendations. In almost all cases the further adjustments required are not large if there is the will to adjust. Other market participants already have! Accepting that each bank must make its own decisions to implement in the most appropriate way for its organisation, I recommend that these few banks take remedial action as soon as possible. The banks concerned are aware of what is required[47]. Some banks have already committed to making the necessary adjustments.
2. Manager discretion is now pervasive in performance management and the award of variable remuneration. As discussed above in section 2.3.1, and in sections 3.2.2.1 and 4.2.4, effective operation of such an approach with a consistent customer-centric orientation requires a number of things to 'go right'. Banks need to continue to invest in the systems and capability uplift necessary to support good and transparent decision making. Effective calibration / moderation arrangements, an empowered challenge function, operating in a 'psychologically safe' workplace in which respectful challenge is

[45] The standard commission model involves the payment of upfront and trailing commissions based on the value of the loan drawn down. Regulatory refinements since the 217 Review, which recommended modifications to the standard model, amongst other things, include the introduction of a 'best interests' test – a requirement that the broker must recommend a product that is in the best interests of the customer.
[46] Much of the regulatory framework in respect of conduct risk is aimed at senior managers and those who manage significant risks that could imperil the bank (and, in an exceptional case, the financial system). The consequence of mis-selling is more likely to be felt by consumers than the bank, except in the case of systemic compliance breaches or systemic mis-selling that requires wide-scale remediation. Amongst other things, the GFC was triggered by inappropriate behaviour in retail banking.
[47] They have not been publicly identified since this review reports at the level of the industry rather than in respect of each individual bank.

accepted and rewarded are vital to ensure equitable treatment and to minimise the risk of a bias towards sales behaviour (whether conscious or unconscious). I encourage the few banks that do not mandate calibration / moderation in these situations to review this position. Moreover, both HR and the internal risk function should be actively involved in providing regular assurance to the CEO and the Board that calibration / moderation arrangements are robust and effective in dealing with conduct risk, defined broadly to include the risk of mis-selling because of inappropriate signals being sent through the exercise of manager discretion and performance discussions. I also believe that regulators can usefully assist by periodically checking the effectiveness of calibration arrangements and publishing relevant data.

3. Banks should continue their efforts to develop good measures of customer outcomes, not simply customer satisfaction / advocacy. How else can leaders be confident that the bank's culture is truly customer-centric?
4. Boards and regulators should pay explicit continuing attention to ensuring that each bank's approach to remuneration, performance management and culture in respect of their retail banking operations are mutually reinforcing and provide incentives for ethical behaviour and minimise the risk of poor outcomes for customers. For example, HR and the internal risk function should be actively involved in providing regular assurance to the CEO and the Board regarding their continued adherence to the letter and spirit of the 2017 Recommendations. It is important, also, that regulators such as ASIC, or the industry's external dispute resolution scheme AFCA should continue to publish data related to disputes resolution processes within banks and their complaints handling performance, and that APRA continue to pay attention to culture, including in retail banking.
5. The ABA should facilitate / coordinate arrangements that would enable each bank to report annually to its Board and publicly against a common survey of in-scope staff perceptions of bank culture along lines substantively aligned with those developed for this review. APRA might usefully consider the scope to address such matters in the context of the risk culture survey it has under consideration.
6. Retail banking typically poses a significantly smaller systemic risk to the financial services sector than many other areas of the financial services sector. Yet the GFC provided a clear example that poor retail practices nonetheless cast a long shadow over the financial system (and the world economy). Moreover, the consequences of poor banker behaviour leading to mis-selling can be serious for individual customers. Regulators need oversight arrangements, supported by effective internal monitoring by each bank's risk function, that enable them to be satisfied that conduct risks are properly addressed within retail banking remuneration and performance management systems (i.e. oversight that extends beyond the material risk takers that rightly attract considerable attention from APRA and ASIC). Regulators such as APRA and ASIC could also usefully introduce periodic oversight arrangements to ensure ongoing adherence to the letter and spirit of the 2017 Recommendations.

3 Performance management

3.1 Context of this section

From its beginnings in 2016 this Review has acknowledged that remuneration arrangements, performance management and culture effectively work as 'three legs of a stool' supporting the sales or customer orientation of the organisation. Together with its governance norms, consequence management framework and risk appetite, these have a profound impact on behaviour and practice in any commercial entity. Organisations work most effectively and efficiently when these three systems of incentives and signals about what is valued are aligned and are consistent with the organisation's strategic objectives (see section 5.1 for a fuller discussion). Discrepancies lead to confusion and inefficiency.

Previous reports in this series have paid attention to the signals embedded in all three of these systems and processes. It is fair to say, however, that the principal focus of the assessment initially was on the remuneration component, noting the linkages to the other two. As time has passed the weight attached to the other two legs of the stool has increased, reflecting changes also in the practices of banks.

There is much closer alignment now between the scorecards and similar devices used to assesses performance, and the mechanisms used to determine variable rewards. As a result, the risk is much reduced that staff will receive 'mixed messages' about what is valued in assessments made of their performance compared to the assessments that lead to the award of variable reward payments. This section, and sections 4 and 5, identify key themes that emerged from this review. A concise assessment of current arrangements compared to the 2017 Recommendations appears in Appendix B.

3.2 Assessment of implementation of recommendations by 2021

3.2.1 Overview - Performance management and variable remuneration systems are closely aligned

A striking feature of the current arrangements is that most banks have simplified their systems and typically (with a few notable exceptions for some roles), the same assessment instrument is used to rate in-scope employees both for performance management purposes and to determine access to any variable reward. This significantly reduces the risk that staff will receive 'mixed messages' about what is valued. Those arrangements are designed to assess an individual's performance against the whole of their role, with much reduced emphasis on sales activity per se (indeed, with a few important exceptions, discussed below, without <u>direct</u> links between sales activities and the overall performance rating).

There is a risk when separate ratings are developed for performance discussions and variable reward eligibility that different weights will be applied to elements of the assessment, which in some cultures could result in a greater emphasis being placed on sales performance in one context compared to the other. A common refrain we heard from staff consulted in 2017, for example, was that mis-selling incentives were greater in the context of performance management discussions than in assessments relating to rewards. Their perception was that sales performance heavily influenced whether they retained their job or were thought suitable for promotion, which carried a stronger mis-selling risk than the small variable rewards then available to most in-scope staff (except for home lenders). With a few exceptions, banks now typically rely on a single assessment process for both performance and reward.

There is also a clear trend towards adopting 'continuous', documented performance management conversations with a much heavier emphasis than previously on the exercise of manager discretion. More frequent discussions reduce the risk that staff will perceive there is an incentive to game the system – banking or postponing sales, for example – in the lead up to a single high stakes performance discussion. More frequent discussions also yield richer and more consistently documented data about 'whole of year' performance to inform the end of year performance rating. Such processes, if implemented well, can increase the reliability and availability of data to justify outcomes, including during calibration / moderation sessions.

However, when coupled with considerable manager discretion, continuous assessments pose additional challenges for how calibration should evolve to ensure consistency in assessments given to staff throughout the year. This issue is further discussed in section 4.2.1.

3.2.2 Scorecards have a 'whole of role' focus but are most often used as a signalling device

Virtually all banks use a scorecard or a similar device to identify the main elements against which an individual will have their performance assessed. They usually contain a mix of qualitative and quantitative indicators. These may, but do not always, have precise weights attached to them. An examination of performance against these indicators, taken together, can enable an assessor to take a 'whole of role' perspective on an individual's performance. Details are further discussed below but as a generalisation the industry exhibits a high degree of compliance with the 2017 Recommendations, with a few exceptions.

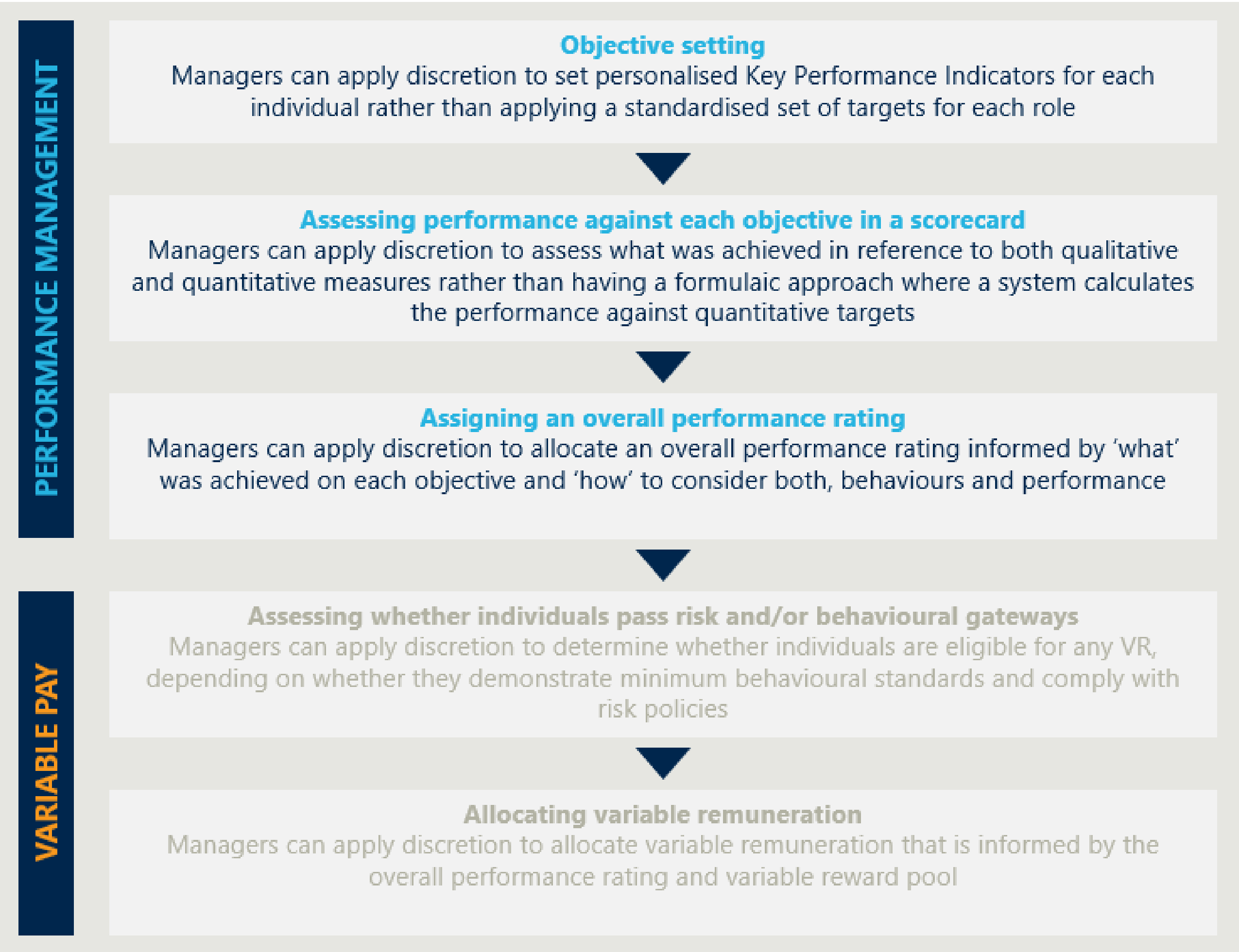
However, the pervasive application of discretion has changed the role that scorecards and similar devices now play. Weights in practice are meaningless unless the manager's thinking processes reflect the priorities that the weights are intended to convey. Indeed, in some cases the same point can be made about the performance indicators themselves. This risk rises as the number grows of quantitative and qualitative indicators that managers are required to take into account in making their assessments. The more complex the required assessment the more likely a manager will (possibly unintentionally) adopt a simpler approach in practice.

Arguably, therefore, in many cases scorecards are now used principally to signal what is important rather than to provide a basis for a mechanical calculation (or quasi-mechanical assessment) of an overall performance rating. As noted above, the dominant model previously involved a more rigid and formulaic approach to performance measurement, where scorecards were used as a monitoring device – tracking performance against (largely quantitative) indicators. Some banks required their managers to apply discretion, but they were significantly in the minority. A critical issue today, therefore, is whether each bank's internal checks and balances ensure that the signals are correctly followed through in the assessments that managers make (and the performance discussions they conduct). The quality of both documentation and calibration processes underpin the effectiveness of such checks and balances.

3.2.2.1 *Discretion: an aid in assessing performance*

Discretion can be applied across different stages of the end-to-end process from performance assessment to the allocation of variable remuneration, as shown in the diagram below. The stages applicable to performance management are highlighted:

Figure 1| Stages where manager discretion can be applied



There are varying levels of discretion managers apply when assessing performance. For the purposes of this review, the categories below indicate what the typical levels of discretion can look like:

- **Low:** the performance assessment is largely formulaic; staff are assessed on their performance against mostly quantitative measures, which are standardised for each role and provide a calculated performance rating. Managers can apply limited discretion to adjust the calculated rating within a defined range and establish the final performance rating.
- **Medium:** the performance assessment includes a mix of quantitative and qualitative measures, which may include some personalised KPIs. Managers apply discretion to determine the performance rating against each category in a scorecard but there is no direct formulaic link between performance against objectives and the final performance rating. A "guided" distribution may be used to keep performance ratings overall within a defined range.
- **High:** some guidance is provided to guide the manager's assessment of the final performance rating, but this is highly discretionary and based on a holistic assessment of performance against a range of indicative measures, where measures may not be weighted. Performance objectives may be standardised at a division level but are highly personalised for each individual and may include a focus on individual development objectives.

Most banks apply either a medium or high level of discretion across these stages of performance management. However, this varies from role to role. The performance assessment for home lenders is often more formulaic than other roles. Section 4.2.4 provides consolidated data for the number of banks that apply each level of discretion, in respect of each in-scope role.

3.2.3 There has been a marked shift in how performance is measured

3.2.3.1 *Emphasis on financial measures has reduced*

The weight applied to financial measures in scorecards has fallen substantially since the 2017 Review. Tables 1 and 2 below show that between 2018 and 2021 the maximum weight allocated to financial measures for all in-scope roles across the industry has declined substantially. Most banks now have scorecards in which financial measures attract a weight less than 33 percent, the maximum recommended in the 2017 Review.

However, the effective weight exceeds the recommended maximum in some instances, as follows:

- One bank has formally allocated more than a 33 percent weight to financial measures. However, the bank has its scorecards under review and expects to formally reduce the weight of financial measures.
- Some banks categorise certain productivity measures as 'customer' metrics that some observers perceive are more correctly viewed as financial measures. For example, a few banks capture the number of referrals made by a banker or a team in some roles as a productivity measure, but a successful referral is defined as one that leads to a subsequent sale. Other customer measures that seem more correctly categorised as 'financial' include increasing customer conversion rates to sales and 'needs met' (where success is dependent on a sale). In some instances, reclassifying these measures to 'financial' increases their overall weight to over the recommended maximum of 33 per cent, although typically not drastically so. In other instances, it was difficult to assess the implications for the overall weight of financial measures of such a reclassification because the scorecards did not separately identify the weight of the reclassified measure. This occurred where the relevant 'productivity' measures were components of a larger group along with other genuine customer measures, or where key categories were not separately weighted in the scorecard.

In addition, some banks have uncapped performance on financial measures in a reasonably formulaic model, meaning that strongly above target performance can contribute directly into a higher overall performance score without limit. This effect is likely to be small in the few cases in which it applies, and these banks have not been rated as non-compliant in respect of this recommendation.

The role played by referrals in scorecards has changed considerably since the 2017 review. Even so, seven banks have referral targets for at least some of their roles. Most of these banks do not include specific product-based referral targets but where they exist, they typically refer to general insurance / business banking. A risk with including metrics based on referrals is that staff will perceive a referral is only valued by their manager if it results in a sale. As previously noted, at least one bank is explicit that a successful referral or customer conversation is one that results in a sale. However, during consultations banks generally were consistent in their position that managers do not operate on that basis. The important issue for them is not whether a sale was made but whether the referral reflected a correct understanding of that customer's circumstances and potential needs. Banks that make such arguments also assert that their arrangements to monitor the quality of conversations with customers provide the checks and balances necessary to deter unwarranted referral activity driven by targets rather than customer needs.

Some staff we spoke to were sceptical on this point. The staff survey conducted as part of the Review provides helpful insights. Thirty seven percent either agreed or agreed strongly with the statement: *I believe that my manager's assessment of my referral performance is based largely on whether my referrals result in sales*. Another third neither agreed nor disagreed, while a similar proportion disagreed (some strongly). This suggests that there is still a significant communication task for managers.

The tables below show the range of *target* performance weights allocated across all banks for each role. These have been adjusted when necessary to reclassify some productivity measures as financial measures. However, as mentioned above, several measures could not be reclassified, as they were grouped with other genuine customer measures and were not separately weighted in the scorecard. The general reorientation away from financial metrics and towards greater emphasis on appropriate behaviours and risk is plain, though less evident in respect of home lenders than other roles. However, weights such as those listed below are not applicable to some banks, as they have not allocated weights to each category and instead adopt a more discretionary approach to assess overall performance.

Table 1 | Scorecard weighting range - 2018

Performance measure	Teller	Seller (General)	Seller (Home Lender)	Seller (Financial Adviser)	Manager
Financial	0% - 45%	8% - 100%	10% - 85%	13% - 40%	0% - 100%
Customer	10% - 100%	8% - 60%	0% - 40%	13% - 50%	8% - 50%
People	10% - 50%	0% - 41%	10% - 33%	10% - 20%	10% - 41%
Process	0% - 30%	0% - 40%	0% - 30%	N/A	0% - 30%
Risk	n/a	0% - 10%	0% - 10%	0% - 13%	0% - 10%
Other	0% - 50%	0% - 50%	0% - 50%	10% - 38%	0% - 55%

Table 2 | Scorecard weighting - 2021

Performance measure	Teller	Seller (General)	Seller (Home Lender)	Seller (Financial Adviser)	Manager
Financial	0% - 30%	0% - 35%	13% - 35%[48]	0% - 25%	13% - 35%
Customer	18% - 100%	0% - 50%	0% - 50%	25% - 30%	0% - 40%
People	0% - 25%	0% - 25%	0% - 25%	N/A	0% - 25%
Process	0% - 25%	0% - 25%	0% - 45%	0% - 45%	0% - 25%
Risk	0% - 16%	0% - 25%	0% - 25%	0% - 25%	0% - 25%
Behaviour	0% - 50%	0% - 50%	0% - 50%	0% - 25%	0% - 50%
Other	0% - 15%	0% - 10%	0% - 40%	0% - 30%	0% - 10%

3.2.3.2 *How results are achieved receives greater emphasis*

Previously, many banks had behavioural or risk gateways – setting a minimum behavioural standard to be eligible for variable reward. These gateways remain (see section 4.2.2.5). In addition to behavioural gateways, there has been a trend to strengthen the focus not just on the 'what' was achieved but also 'how' it was achieved. This has been supported in many banks by initiatives intended to strengthen their

[48] There was one instance where financial measures accounted for 80 percent of the weight. However, the scorecard is under review and we are informed that new scorecards will be released to employees.

workplace culture around ethical decision making in the best interests of the customer. This is further discussed in section 5.2.1.3.

Banks have taken different approaches to incorporate how results are achieved into overall assessments of performance:

- Several banks have an overall performance assessment that is equally weighted between what was achieved, and how it was achieved. Thus, behaviour now attracts a weight of 50 percent in their performance assessment. For some of these banks the ‘what’ and ‘how’ receive separate ratings, whilst for others they are ultimately combined into one overall rating.
- Many banks include behaviour and/or risk measures as discrete elements within the performance scorecard. Individuals are assessed on their behaviours and/or risk management, alongside performance on other aspects of their role (e.g. financial, customer). Performance on each of these measures (behaviours, risk, financial, customer etc) are then brought together into an overall performance assessment. Typically, leaders have discretion, with some guidance, to determine the overall rating with reference to the underlying assessments.
- In addition to the behavioural and risk rating contributing to the overall performance assessment, a few banks use the behavioural and risk rating as modifiers – reducing maximum achievable overall performance ratings if behaviours and risk are only partially met or not met.
- Some banks operate a wholly discretionary system in which managers make an overall assessment of performance, including an assessment about how well the individual staff member demonstrates the bank’s values. The evidence in support of this judgement could include formal findings in respect of the Code of Conduct but also the manager’s assessment of the impact of the individual’s behaviours on customers and other members of the team.

Many banks also gain intelligence about the ‘how’ through direct analysis of the quality of customer interactions. This issue is further discussed in section 3.2.3.6. By their nature, assessments of ‘how’ results have been achieved are typically more discretionary than assessments of ‘what’ was achieved.

3.2.3.3 *Several approaches are used to ensure financial measures are product neutral*

A key finding of the 2017 Review was that many banks had incorporated measures in their scorecards or similar devices that were intended to encourage staff to promote the sale of particular products (including cross sale targets) or require referral activities intended to secure the same result. Practices varied. Some banks, for example, had specific separately remunerated targets for specific product sales or cross sales. In other cases, cross sales or referrals operated as a gateway. In 2017, almost every role had some evidence of this reflected in their scorecards for at least some banks. Financial measures that are not product neutral increase the associated risk of mis-selling and poor customer outcomes.

Nowadays, scorecards, where they are influential, are typically product neutral (with one or two exceptions, for example in respect of the sale of insurance products in a few cases). Different approaches are used to maintain product neutrality:

- Most banks use “widget” counts where all products are treated as “1” (weighted equally).
- Several banks have developed weights that are intended to reflect the relative effort required to make sales of certain products compared to others. The weights are applied in a scorecard context to compute an aggregate value for sales or ‘notional revenue’. All these banks maintain the weights are independently assessed outside of the sales team (for example, by internal audit or the executive leadership team) to ensure they genuinely reflect the relative effort required.

- A few banks use both approaches – typically using "widgets" for front-line roles, and notional revenue for relationship management (where a banker manages a portfolio of clients) or leadership roles.

These two different approaches were also applied at the time of the 2017 Review by banks concerned to achieve product neutrality. The debate remains unresolved about the relative merits of weighting or not weighting if staff deal with multiple products. It would seem to be an empirical matter, related to the validity of the approach taken to establish the weightings and staff perceptions of them, rather than one of principle. The 2017 Review concluded on this matter:

The Review makes no finding in principle about which approach to product neutrality is preferred. Banks, however, should be prepared to defend, both to their Board and, if necessary, publicly, the decisions they make in this regard. Sale based measures have the advantage of simplicity. They need to be applied with care, however, to minimise the risks identified…[49]

That remains the position of this Review.

For some roles in most banks (for example, home lenders, or smaller banks with a restricted product line) product neutrality is assured because specialised teams are responsible for the relevant product category. In these cases, the principal issue is the management of mis-selling risks. Some banks (including some of these banks) can include cross-sales referrals (for example, insurance products) as a performance measure in scorecards. Typically, though not always, the criteria for 'success' in these instances is whether a conversation took place with the customer and not whether the referral leads to a sale. The banker may be separately assessed (for example, as a customer metric) about the 'quality' of such a conversation – see section 3.2.3.6 for a discussion of this aspect.

However, some banks still have measures that are not product neutral for in-scope roles – e.g. general insurance sales or referrals. Moreover, many banks include mortgage sales targets, possibly expressed in terms of increasing the bank's market share, in the scorecards of senior managers and executives.

3.2.3.4 *Customer measures have evolved, but still don't measure customer outcomes*

The 2019 Interim Report found:

My impression is that customer metrics are far less sales oriented than was the case previously. However, this should be tested with survey or other evidence about contemporary practices. This, too, should be a focus of any subsequent assessment in 2021. The analysis needs to occur at two levels: the policy, and the practice at branch[50] *level. Data gathering to support this analysis also should be planned and executed in advance of the actual assessment. Despite good intentions, it has proven difficult to develop significant scalable new measures of customer experience that accurately capture both the customer experience and the outcomes secured by a customer from an interaction with a bank, including over time. This is common across the world.*[51]

The ABA accepted the recommendation made in 2019 to support this analysis of bank policies with a staff survey designed to capture practices / culture. The results of that survey are summarised in Section 5.2.3

[49] 2017 Review P16.
[50] 'Branch' should be taken to cover other workplaces such as call centres or specialised retail business units.
[51] 2019 Interim Report P14.

and presented in more detail in Appendix A. This section addresses the policy position the industry has adopted.

In summary, there has been progress since 2019. But, in my view, the development of compelling customer metrics that address outcomes customers achieve remains a work in progress. I had recommended in 2019 that the ABA establish whether it could auspice[52], in collaboration with ASIC and ACCC as necessary, collaborative work to guide the development of principles that should underpin metrics that capture the outcomes customers achieve. That has not occurred. The issue remains unresolved.

There appears to be an assumption in some quarters that a sale is itself evidence that the customer achieved a desirable outcome. A mortgage, for example, is taken as conclusive proof that the customer's need for shelter was met. The existence of the mortgage does not provide proof, however, that the mortgage was the best option for that customer – whether in respect of its terms or its amount. Indeed, the customer may not know for some time whether they have overcommitted themselves and whether borrowing less for shelter may have secured a better outcome overall.

Net Promoter Score (NPS) remains predominant. It provides the metrics employed by most banks for at least some roles. It is a measure of the extent to which the customer who responds to a survey is prepared to advocate for the bank / brand or a range of other 'lens' onto the bank's acceptability[53] to the customer. However, the metrics now captured in the 'customer' space have become more sophisticated and more widespread since 2019. They have also broadened to address 'efficiency' measures such as the time taken to resolve complaints or applications.

Importantly, most banks are capturing richer customer feedback through their examination of verbatim comments customers provide as part of their response to the NPS survey and through paying greater attention to the substance of and staff responses to customer complaints. A slight majority of banks apply such data to their assessment of individuals, although a sizeable minority believe that sample sizes are too small to apply to individual assessments. Where complaints data is used in the context of individual staff assessments, banks are typically cautious about how it is used (other than highly complimentary feedback). Complaints and comments are frequently mined both to improve product offerings and to provide feedback to teams about how to improve the experience they offer customers.

In summary, there is clearly more focus now on:

- Whether customer enquiries or complaints are resolved the first time to improve customer experience;
- The time it takes to process an application (a quality conversation is assumed to generate the data required to support a shorter approval time);

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[52] ***Recommendation 2:*** *ABA establish whether there is sufficient support for collaborative work to develop principles that should underpin metrics that capture the outcomes customers achieve.* NOTE: *Although some banks have expressed interest in such an initiative in discussions, others have expressed reservations on the basis that the resolution of this issue is an important strategic business asset. If necessary, this work may involve a subset of the ABA membership. Consultations with ASIC and the ACCC may be necessary to identify and assist with navigating any competition law issues. Interim Report p 14*

[53] An NPS survey asks: "How likely is it that you would recommend [insert item here] to a friend or family member". It can be measured at multiple 'levels' (whole of organisation, product, branch, individual banker) and at different stages (random interval, after a specific interaction or transaction) Two surveys (for example, in respect of both individuals and an organisation or unit) may be administered together.

- Improving digital engagement (a complex issue, see section 3.2.3.5, below); and
- Contemporary or after-the-fact analysis of the quality of conversations with customers. Contemporary observations involve managers sitting in on conversation with customers. After-the-fact analysis involves either a later examination of the documentary record of the conversation or review of a recording (for example of the calls made or received by contact centre staff). Both approaches raise important issues - see section 3.2.3.6 below.

The table below indicates the number of banks that employ each type of customer measure in their scorecard. In interpreting this table:

- Quantitative measures in scorecards are measures where quantitative targets are factors in the performance assessment, for example the target number of customer conversations per week;
- Qualitative measures are measures where a manager is required to apply discretion to assess the individual's performance, for example by assessing the quality (as opposed to quantity) of customer conversations;
- 'Total' indicates the total number of banks that use each customer measure. Where a bank uses both quantitative and qualitative measures, this is counted as only 1 in the total column; and
- 'Other' includes a wide range of measures. Some banks include a qualitative assessment of engagement in the community in which the bank operates while other banks include a measure for managers to upskill their staff to have effective customer conversations.

Table 3 | Number of banks using customer measures in performance assessments

Customer measure	Quantitative measures	Qualitative measure	Total[54]
Customer advocacy (NPS)	11	9	13
Customer satisfaction	3	2	4
Customer conversations	7	9	12
Digital engagement	6	5	9
Verbatim feedback and complaints	1	11	11
Efficiency to customer outcome measures	7	11	14
Other	4	9	10

Many banks are also taking steps to assess and learn from the quality of customer interactions. This is further discussed in section 3.2.3.6.

3.2.3.5 *Digital engagement by customers attracts substantial attention*

The digital channel presents this review with a conundrum. It has been clear since the beginning of this process in 2016 that, in the strategic analysis of many banks, digital channels present them with cost and, for some customers, convenience opportunities that individual banks (and, in some respects, the industry) ignore at their peril. Their imperative is to deliver a more engaging digital experience, supported by incentives / encouragement for digital dinosaurs (both staff and customers) to 'get on board'.

[54] Total indicates the total number of *banks* that use each customer measure. Where a bank uses both quantitative and qualitative measures, this is counted as only 1 in the total column.

During our consultations for this review, banks consistently argued that the trend to digital is consistent with customer needs. They often, and not unreasonably, asserted that COVID-19 not only proved that ‘there is no alternative’ to digital engagement with banks but that, with appropriate support, customers are open to adopt it. Measures in scorecards relating to digital engagement generally focus on digital education to assist customers to understand the digital channels available and to choose those that best suit their needs. Such measures preserve customer agency and can improve customer experience. However, some banks set digital engagement targets, for example, where staff are required to open a specific proportion of new accounts as internet banking accounts or to facilitate completion online of a certain proportion of their customers transactions, or to ensure that a certain proportion of customers adopt the bank’s mobile app. In some instances, targets have been set as high as that 98 per cent of customers are digitally enabled. There is a risk that such targets can drive behaviour that is not in the best interest of the customer.

3.2.3.6 *Quality customer interactions / conversations are sought*

As sales performance has been de-emphasised in the performance assessment process for in-scope roles, the attention paid to the number and quality of conversations with customers has assumed greater prominence. This movement was nascent at the time of the 2017 Review. It is quite strong currently.

Most banks have customer measures intended to capture the quality of customer conversations for at least some roles, but especially seller roles and contact staff roles. Banks consistently argued during consultations that ‘quality’ is not assessed by whether a sale is secured. The language used varies. The sentiment, though, is that ‘quality’ is determined by a range of factors, such as: whether the banker listened actively to the information provided by the customer and correctly diagnosed what, if any, assistance they need; whether the banker was empathetic and assisted the customer to articulate their needs; whether the banker’s explanations were clear; etc.

The importance attached to this issue is reflected in the fact that many banks have created or significantly updated their customer conversation frameworks. Moreover, many banks undertake contemporary or after-the-fact analysis of the quality of conversations with customers[55]. Contemporary observations involve managers sitting in on conversations with customers (or listening in to live customer calls). After-the-fact analysis involves either a later examination of the documentary record of a conversation or review of a recording (for example, of the calls made or received by contact centre staff). In some cases, banks acknowledge that the frame of reference for such assessments is how closely the banker adhered to the customer conversation framework. Typically, banks that undertake such analysis say they use it to inform coaching or training of their staff. It can be difficult to monitor how such coaching sessions are conducted in practice. Similarly, it is difficult to assess the degree to which these conversation frameworks are truly customer centred compared to sales conversation frameworks.

A risk attached to such coaching and the emphasis on analysis of customer conversations is that staff will perceive the end objective and the measure of success as still being to achieve a sale. Some frontline staff we consulted during the review were firmly of the view that ‘while the language has changed, the focus still remains on making sales’. It is difficult to assess such views, which appear to be genuinely held. However, such views are not necessarily inconsistent with the staff survey responses. The responses suggest that

55 This is consistent with information provided during interviews or in responses to the questionnaire. However, these analyses can serve different purposes. Some banks draw directly on such work to inform their assessment of an individual’s performance. Others use it in their assessments of compliance and similar matters. Banks that adopt the latter approach are not included in the table in section 3.2.3.4 unless it is directly included in their scorecards.

most staff are clear about the importance the banks in general attach to making sales that suit customer needs, but a substantial minority still perceive pressure to sell, in some instances inappropriately:

- Eighty five percent agreed or strongly agreed with the statement: *My manager shows by their behaviour that the customer is at the heart of all decisions;*
- Seventy five percent agreed or strongly agreed with the statement*: If I inform a customer about the potential unsuitability of a product they are considering, this is viewed positively by my team leader or manager;*
- Seventy five percent agreed or strongly agreed with the statement: *Where staff have made sales that do not seem likely to result in a good outcome for the customer, I have seen my manager respond with appropriate actions e.g. managing the performance or behaviour of the staff member, teaching the staff member how to better serve the customer or implementing appropriate training;*
- Seventy eight percent agreed or strongly agreed with the statement: *I am encouraged by my team leader, manager or senior leaders to proactively tell a customer, at the point of sale, if a product is unsuitable;*
- Forty three percent agreed or strongly agreed with the statement: *My career progression in the bank depends mostly on my sales results; and*
- Eighteen percent agreed or strongly agreed with the statement: *I feel pressured to make sales, to the detriment of customer outcomes.*

3.2.3.7 *Productivity measures often feature in performance assessments*

A stable banking system is essential to support the effective operation of the Australian economy. Cost control, adequate and profitable sales, effective management of risk and sufficient reserves are key to securing that objective.

Almost all banks have incorporated what they claim to be productivity measures into the scorecards or other assessment criteria used to monitor performance. These are typically activity measures of various kinds. Examples include:

- The time taken from product application to approval;
- The number of conversations conducted with customers;
- The average time taken to handle a customer query;
- The proportion of transactions executed digitally (although some banks view measures like this to be ‘customer’ metrics, the validity of which inference may vary between customers);
- The number of successful referrals to other specialised parts of the bank (where almost all banks state that ‘success’ is making a suitable referral rather than whether a subsequent sale is made); and
- The number or percentage of marketing leads provided to a banker that the banker acts on (irrespective of whether a sale occurs).

As time passes, it will remain important that communication from senior leaders about such matters does not inadvertently convey pressure to sell or pressure to pursue productivity measures irrespective of a customer’s needs. A lesson from the responses to the staff survey developed for this review is that authentic and consistent values-based messaging from the top down is powerful in conditioning behaviour (see also section 3.2.4).

3.2.4 Frontline staff believe leaderboards still exist

A classical leaderboard conveys information about how each banker is performing relative to their financial, and as appropriate, non-financial targets. There is a risk that peer pressure could encourage mis-selling or other poor behaviours towards customers in order to achieve acceptable performance against targets.

The 2017 Review addressed leaderboards in the following terms:

Consistent with the need to send clear signals to frontline staff that a better balance is to be struck between sales and customer oriented measures of performance I propose that banks reconsider the use of leaderboards… with a view to phasing them out whenever possible.

A strong case can be made that the continued use of leaderboards… will be perceived as the continuation of an embedded sales culture. If their continued use is sanctioned, however, this should only occur if the focus includes a range of customer and other measures that reflect the breadth of the goals applicable to the role[56]*.*

All but one bank told this review that they no longer employ formal leaderboards to motivate staff. However, there is a clear disconnection between the perceptions of frontline staff and those of their senior executives. The survey of staff perceptions indicated that across the industry, on average over 30 percent of staff agreed or strongly agreed with the statement "*my team uses a 'leaderboard' of some sort showing which individual is making the most sales and which individual is making the least*". Indeed, in every bank, 15 percent or more of the staff agreed or strongly agreed with that statement or with the statement 'I generally know who in my team is making the most sales and who is making the least'.

The FSU has provided examples of the continued use of individual rankings at a branch level for some banks against key measures such as the number of referrals and customer needs met, which is visible for all staff in that branch (and sometimes, visible to others as well). Similarly, the FSU has provided evidence that some branches of some banks provide individual rankings for home lenders by sales volume. Some leaderboards provided to the review record only branch activity relative to other branches such as the number of customer conversations conducted in total, the total number of referrals or the proportion of complaints actioned. Staff perceptions of manager views of what constitutes a successful customer conversation, or a productive referral are discussed in sections 3.2.3.6 and 3.2.3.7. However, some of the examples provided to the review were highly personalised, showing planned and actual activity at an individual level, sometimes stopping at the level of the number of customer conversations, though often going further to record sales outcomes (using different nomenclature).

During our consultations, senior executives were generally surprised by and curious about those perceptions. It is possible that, although not officially sanctioned, leaderboards may still exist at a branch level in some cases. Alternatively, they suggest that data made available to branches and teams about their performance relative to other teams may have been interpreted as a leaderboard, albeit not one that identifies the respective performance of individuals. In other cases, the finding may simply reflect that individuals generally know how they stand relative to their peers within a team, especially if the team is small. I'd encourage a deeper analysis of this finding.

Pleasingly, nearly 50 percent of staff across the industry also agreed with the statement "*If a leaderboard is used, sales are balanced with other measures such as customer, risk or people measures*". It was remarkable, moreover, that in one or two banks whose staff believed they could identify the best and

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[56] 2017 Review, p26.

worst sellers (possibly but not necessarily because of the unauthorised existence of a leaderboard) those staff nonetheless perceived their bank as being relatively more customer-centric than the rating staff of other banks had given their employer. In effect 'tone from the top' was seen to counter a possible bias towards sales inherent in the use of a leaderboard.

3.2.5 Third party governance arrangements have been reviewed

The 2017 Review made recommendations to reform substantially the remuneration arrangements and governance and oversight by banks that apply in mortgage broking. It specifically recommended that the standard commission model of the payment of upfront and trail commissions related to the value of mortgages written by the broker should be replaced by payments more closely aligned to the effort required to service the customer and assist them to successfully source a mortgage.

At the time of the Interim Review, it was clear that governance and bank oversight had been strengthened in many cases. Moreover, some other value-based additional payments and incentives had been significantly scaled back, removed or recast to reduce the risk of mis-selling[57]. However, the standard commission model remained in place, although payments were triggered only in respect of the loan drawn down (net of offsets, in at least some cases) rather than the loan limit. Government policy has favoured the continuation of the standard commission model, albeit supported by a new legal requirement that mortgage brokers must act in the best interests of their clients irrespective of the financial incentives offered to the broker. In that respect, however, all banks that use the services of mortgage brokers do not comply with the 2017 recommendations in respect of the standard commission model.

Given the government's policy position, mortgage brokers and aggregators have been excluded from the scope of this review. However, non-mortgage retail brokers, introducers, referrers and franchisees remain in-scope.

The 2017 Review recommended stronger oversight by banks of these third parties to reduce mis-selling risks. It also found:

Both this Review and the ASIC Report[58] have found that Introducers and Referrers receive almost as much upfront commission as Mortgage Brokers and Aggregators[59]. Given the limited work undertaken by Introducers and Referrers compared to Mortgage Brokers, the upfront commission paid to them for a successful 'sale' appears to be disproportionately high…[60]

Remuneration arrangements in respect of in-scope third parties are discussed in section 4.2.6.

Banks report that they: have reviewed governance arrangements with non-mortgage retail brokers, introducers, referrers and franchisees; have strengthened their controls and processes for onboarding and offboarding introducers / referrers, including (in several cases) by insisting on mandatory training or accreditation; and have invested in stronger processes and controls to ensure third parties meet minimum conduct and compliance standards. Some banks report also that they have significantly reduced the number of such third parties with whom they deal, which simplifies their oversight task.

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[57] These concern: volume based incentives that are additional to upfront and trail commissions; temporary increases in commissions to support campaigns to increase product sales; and soft dollar payments.
[58] ASIC, *Report 516: Review of mortgage broking remuneration,* March 2017.
[59] Refer to Section 4.2.3 of the Issues Paper and Finding 11 of the ASIC Report.
[60] 2017 Review, p39.

All banks that have introducer and referrer programs state they monitor the quality of applications received through arrangements such as:

- Credit assessments are conducted by the bank's credit risk team;
- Banks complete quality assurance checks on applications to inform the need for further training; and
- Some banks also monitor customer feedback as it relates to these third parties to inform decisions about the continuation of these arrangements.

Some banks have also strengthened the consequence management framework to ensure there is a clear process with appropriate remuneration clawbacks and other options (such as termination of the relationship) to manage misconduct and breaches in policies.

These take further initiatives that have been unfolding since 2017. It is far from clear, however, that the scope for pro-customer improvement has been exhausted.

Relatively few banks operate franchisee models. These banks reported that they have reviewed their governance arrangements with franchisees. For some banks, the performance management system for franchisees is identical to that of the bank, which includes system prompts when remuneration for staff of the franchisee networks fall outside reasonable guidelines (which in some, not all, cases are said to be in line with the recommendations of this review). Banks have stated that they have regular branch audits and review the risk policies of franchisees to ensure they are aligned to the recommendations of this review. Almost all banks have stated that they have strengthened their consequence management framework as it relates to franchisees to examine any poor audit and behaviour outcomes to apply a consistent approach to any reductions in remuneration (or termination if required). Overall, banks believe they have strong operational oversight of franchisees.

3.3 Future directions

Although the industry has very substantially implemented the 2017 Recommendations that relate to the design and conduct of performance management, some banks have relatively small further adjustments to make. I would encourage them to do so. The most significant further steps relate to the effective weight assigned to financial measures in some systems.

3.3.1 A few banks should ensure the effective weight of financial measures is less than 33 percent

The one bank that formally assigns financial metrics a weight in scorecards in excess of 33 percent has undertaken to review and address the matter. I trust this is rectified promptly.

A more problematic finding is that some activity measures that some banks track as indicators of 'productivity' or 'customer' performance may be perceived as more sales related than intended. Oddly, that risk may be higher in heavily discretionary systems that assess a range of indicators in what appears to be a 'black box' before assigning a rating or other metric intended to capture relative performance. Banks face an inherent tension between needing to remain profitable and 'unquestionably strong' while being legitimately customer-centric and projecting a customer-centric persona. I cannot in good conscience argue that banks should eschew monitoring of genuine measures of banker productivity and effectiveness. I argue strongly, however, that the design and communication of such measures has to credibly address and resolve that tension. Banks exist to manage risk. The risk of miscommunication in this area is high and, in my view, should be addressed cautiously.

As a guide, input measures such as number of customer contacts, lead actioning rate, or time from application to drawdown are clearly productivity measures. Measures that require a sale to be made to provide evidence of appropriate contact with a customer or referrals where credit is only given if the referral results in a sale, are most likely to be interpreted by staff as sales measures. They should be considered as such. Public trust, once lost, is difficult to recapture. The industry's responses to COVID-19 may have generated a positive trust dividend. Pandemics are hopefully not an everyday event, however.

3.3.2 There is unfinished business in leaderboards and capturing customer outcomes

Other 'unfinished business' that emerges from this chapter includes:

- There has been little progress to capture customer outcomes. Although many have interesting work in hand to better capture customer feedback, most banks continue to focus on customer advocacy. I had suggested in the Interim Report that the industry might consider undertaking collaborative work, auspiced by the ACCC and/ or APRA as necessary, to progress this issue. The idea still appeals, though I understand the reluctance of some industry leaders to collaborate to develop a tool that may undermine a potential strategic advantage that they may have secured through their own efforts.
- Staff perceptions that leaderboards are more commonly in use than senior leaders believe needs further examination. One possibility is that informal arrangements apply in at least some branches despite formal bank policies to the contrary. Others include that performance dashboards that display branch- and/or individual- level 'productivity' measures can be interpreted as leaderboards, including because publicly displayed metrics include both personalised targets and performance against those targets. If so, my earlier comments remain apposite.

3.3.3 A customer-centric organisational culture, robust calibration processes and leader capability are crucial to effective application of discretion

Two themes dominate this final assessment of the industry's responses to the 2017 Recommendations. These are:

- The challenges posed by the emergence of manager discretion as the dominant paradigm for both performance assessment and rewards assignment; and
- The pervasive influence, for good or ill, of leader capability and organisational culture.

The challenges posed by manager discretion will be further considered in Chapter 4. For the present purpose, it is sufficient to note that it is essential that banks provide adequate training and resources to build the capability of managers and ensure that they exercise discretion with predominantly an ethical and customer service focus. This needs to be supported with robust calibration arrangements, clear guidelines that balance financial and non-financial performance, and commonly understood definitions of high and concerning performance. Calibration sessions should foster a psychologically safe environment where leaders feel safe to speak up and challenge decisions, especially as it relates to 'how' individuals perform, to promote a focus on customer service and ethical behaviour. A trend towards 'continuous' performance assessment rather than one or two high stakes performance discussions annually poses particular challenges for calibration.

Findings and emerging themes in respect of culture will be addressed in chapter 5. Successfully addressing both the challenges posed by discretion and culture are fundamental to ensuring that performance management arrangements in practice underpin a strongly customer-centric and profitable bank.

4 Variable remuneration structures for bank staff

4.1 Context of this section

The 2017 Review examined product sales commissions and product-based payments received directly or indirectly by people selling retail banking products. Such payments are linked to the number or value of products sold, offered, or distributed to retail and small business customers. The 2017 Review found that some payments carried an unacceptable risk of promoting behaviour that is inconsistent with the interests of customers and should therefore be changed. This risk stemmed from the way incentives and remuneration were structured to provide specific incentives to retail bank staff to achieve sales, possibly with less concern for the needs of their customers than is desirable.

In summary[61], in respect of variable remuneration, the 2017 Review recommended that:

- Banks remove variable reward payments and campaign related incentives that are directly linked to sales or the achievement of sales targets;
- Eligibility to receive any variable rewards should be based on an overall assessment against a range of factors that reflect the breadth of each person's responsibilities, with financial measures not predominant in that assessment and calculated in way that does not encourage the sale of one product over another (i.e. be 'product neutral');
- Variable reward payments no longer include financial gateways or accelerators or measures with similar effect related to financial measures;
- The scale of variable reward payments should be reduced, significantly so in the case of some roles such as home lenders, and ultimately amount to a relatively small proportion of fixed pay; and
- Credible behavioural or equivalent values gateways be applied to determine whether an individual can access any variable rewards to which they might otherwise be entitled.

As previously noted, these recommendations were seen as components of a broader approach to better align performance management practices, bank culture and governance to reduce incentives for mis-selling and poor outcomes for customers.

4.2 Assessment of implementation of recommendations by 2021

4.2.1 Overview – rewards are rarely directly linked to personal performance now

Four features of the current interactions between the performance management and variable rewards systems have significantly reduced mis-selling risks compared to 2017 in most banks.

First, most banks have simplified their systems and typically (with a few notable exceptions for some roles), the same assessment instrument is used to rate in-scope employees both for performance management purposes and to determine access to any variable reward. As discussed in section 3.2.1, this significantly reduces the risk that staff will receive 'mixed messages' about what is valued.

[61] See Appendix B for the full set of 2017 recommendations that are in-scope for this review.

Second, a striking feature of current arrangements is that the link between performance and the scale of a reward payment is much looser now, and more difficult for staff to predict in advance. This also helps to reduce mis-selling risks.

In 2017, for many sales roles at many banks, performance ratings and access to variable rewards were frequently calculated formulaically. The size of a reward payment could depend on an overall 'score' derived from the weighted sum of scores assigned to specific components of a scorecard. It could also link directly to specific indicators, including the absolute value of sales achieved or sales relative to a target. For some roles, especially home lending, outperformance against target could frequently lead to significantly higher variable pay through an accelerator mechanism or something similar. Payments could be made monthly, quarterly, biannually or annually depending on the parameters of the reward scheme in operation. In a small number of cases either the performance rating or the reward assignment was heavily influenced by manager discretion, which could dull staff perceptions of the link between their activities and their bonus pay. The predominant paradigm, though, was scorecard based and formulaic. As a result, many in-scope bankers could discern a clear link between their performance against targets, especially sales targets, and the variable reward they would become eligible for. That is far less likely to be the case today. Links to sales, if they exist, are typically indirect. Exceptions tend to be home lender roles in some banks.

Third, there is a clear trend towards adopting 'continuous' documented performance management conversations with a much heavier emphasis than previously on the exercise of manager discretion. More frequent discussions pose some challenges for calibration but reduce the risk that staff will perceive there is an incentive to game the system – banking or postponing sales, for example – in the lead up to a single high stakes performance discussion.

Fourth, the link between the performance assessment process and the amount of variable pay awarded to an individual can be subtle. Discretion is frequently applied to translate a performance outcome into a variable pay entitlement. In almost all cases, moreover, while pay outcomes are likely to be correlated with performance (including sales in some contexts), the amount of variable pay available for allocation to individuals is determined by the performance of a business unit or the organisation as a whole. The correlation means that better performance consistent with desired cultural norms is a no regrets option – it raises the likelihood that you will receive a higher variable reward payment than otherwise. However, uncertainty about how much extra pay is achievable reduces the likelihood that an individual can discern a quantifiable link between their personal sales activities and the amount of variable pay they may receive. Again, the exceptions, where they exist amongst in-scope roles, are more likely in the case of home lenders.

Continuous assessment and manager discretion offer significant advantages. However, they also pose challenges to ensure that individuals are treated equitably and that there is not an unconscious bias towards sales exercised by managers. These matters are discussed further in section 3.2.2.

The following sections provide a more detailed overview of current practices compared to the 2017 Recommendations. Appendix B provides a concise assessment of compliance against the recommendations.

4.2.2 Variable remuneration structures have changed substantially

4.2.2.1 *Approaches vary but the industry has largely moved away from formulaic approaches to variable remuneration*

As noted above, the quantum of variable reward an individual is eligible to receive is far more difficult to predict in advance than the typical arrangements in place in 2017. The quantum is rarely directly linked to sales performance (and the exceptions typically apply to home lenders) and only infrequently linked directly to a specific outcome (i.e. rating) from the performance assessment process.

Precise arrangements vary between banks and, in many cases, between roles (see, for example, section 4.2.4.1). However, the industry, as a generalisation, has moved away from approaches that relied on a slightly different data base to inform performance assessments and assessments for entitlement to variable reward payments, and away from a predominant model in which relatively formulaic approaches were applied to translate each assessment rating into a variable pay quantum. At times, the link between the achievement of specific targets, especially sales or cross sales targets, and a quantum of pay was quite direct in 2017.

Arrangements are now quite different. As discussed in section 3.2.3.1, financial metrics such as sales achieved are now considerably less influential in determining an overall performance assessment. The range of measures, financial and non-financial, quantitative and qualitative, that managers now consider when reaching an overall assessment of performance varies widely.

A few banks have adopted quite complex arrangements that require managers to reach an 'on balance' judgement about an individual's performance after having considered a large number of both quantitative and qualitative indicators. Such complexity risks a reaction from managers, namely, to simplify their decision making by focusing on the easily measured aspects of performance, including sales performance. It is impossible to predict whether such responses will predominate in the few banks that face this risk in any serious way. Similarly, it cannot be predicted what impact such a simplification will have on variable reward payments. Effective operation of such systems clearly requires conscious support for managers to maximise the likelihood that their decisions are as well based as is reasonable, coupled with challenging calibration / moderation arrangements to guard against unconscious bias in favour of sales.

Accelerators, mechanisms with an accelerator-like effect and financial gateways no longer exist. Substantial progress in addressing this issue had been reported at the Interim Review. This review has shown that there are currently no banks that use such mechanisms.

There has been a shift from monthly and quarterly incentive payments to mostly annual payments, or, in some cases biannual payments. This is encouraging as it can reduce the risk that individuals focus on short-term outcomes to maximise their variable remuneration payments.

4.2.2.2 *Organisational performance moderates the quantum of variable remuneration available to individuals*

In 2017, there was a reasonably predictable link, especially for some in-scope roles, between personal effort and the quantum an individual could expect to receive as variable remuneration. By contrast, the predominant model today, although not the only model in use, especially in respect of some roles such as home lenders, is that the total quantum of variable reward payments available for retail bankers (the 'variable reward pool') is determined by organisational or divisional financial outcomes with appropriate risk modifiers, and in some instances, modifiers related to customer and/or people outcomes as well[62]. An individual's share of that pool is determined by their assessed performance relative to other bankers. This substantially reduces mis-selling risk previously associated with access to variable remuneration payments.

4.2.2.3 *Some roles are no longer eligible for variable remuneration*

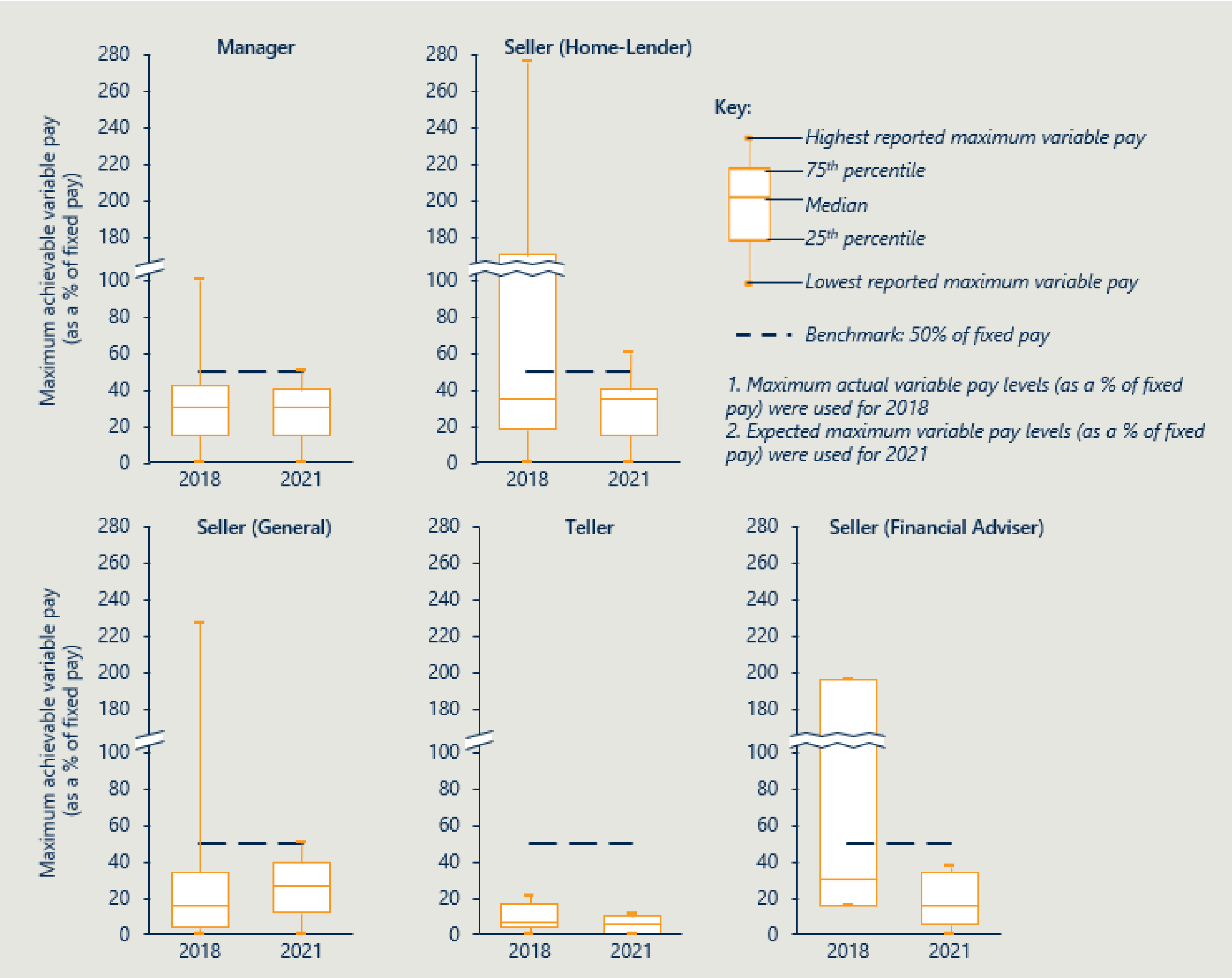
Some banks apply a company bonus scheme to some in-scope roles, which is not linked to individual performance, or only offer fixed pay. In one or two cases (but not the majority of banks for which this is now true) this has been their practice throughout the whole period of these reviews. These approaches are less likely to apply to home lenders than to other roles. Five banks no longer offer bonuses to Tellers. Another bank plans to take this step for Tellers and similar roles shortly.

Banks have stated that the purpose of moving staff away from individual variable pay is to shift their focus to performing their role and servicing the customer's needs without having to worry about how their financial performance will influence their remuneration outcome.

[62] Many banks have employed variable reward pools as a budgeting mechanism for decades. However, historically, formulaic sales incentive scheme payments were typically either funded separately, or were paid from the pool throughout the year before the final variable reward pool available was confirmed for annual payments. Therefore, variable reward pool adjustments affected head office staff and executives, typically on discretionary annual incentive schemes, more so than staff on formulaic sales incentive schemes.

4.2.2.4 *Maximum VR opportunities have reduced*

Figure 2 | Distribution of maximum achievable variable pay (as a percentage of fixed pay) across the sector



The 2017 Recommendations included that the industry should progressively reduce the maximum variable rewards available to in-scope roles, as a proportion of fixed pay. It proposed that such pay should be 'a relatively small proportion of fixed pay' by the 2020 performance year. The 2017 Review noted:

An issue for consideration is whether to provide guidance about the appropriate maximum variable reward. In providing guidance to implement the FOFA reforms ASIC was persuaded not to specify precise guidance. After much reflection, I, too, have been persuaded to adopt that approach. In adopting it, however, I want to be clear that some variable reward pay currently available seems to be excessively large and in those cases the mix between fixed and variable reward needs to be rebalanced, beginning as soon as possible. That applies particularly to some Home Lenders[63]*.*

The 2019 Interim Report addressed the question, 'what constitutes a relatively low proportion'? It noted that in at least one jurisdiction, the Netherlands, there is a regulatory cap of 20 percent on variable remuneration, including in respect of in-scope managers. I had expressed a preference not to mandate a precise cap, as a general rule, but also observed:

[63] 2017 Review, p21.

For the purposes of the current assessment I have been encouraged by the fact that almost all Teller and equivalent roles now have access to variable remuneration no higher than 15 percent of fixed pay. The maximum remuneration of specialist bankers such as mortgage lenders has fallen significantly, though the pace of change is not uniform, and some are uncertain about the end point. The professed tendency of most of the major banks, who set the tone for this market, is downwards. I have tentatively concluded that target variable remuneration for such specialist roles by 2020 should be no more than 50 percent of fixed remuneration, and preferably less. However, the reviewer in 2021 will need to form a view having regard to market conditions at the time. [64]

Box plots in Figure 2 above show a significant reduction in the highest reported maximum variable pay achievable for staff performing in-scope roles over the period covered by these reviews. By 2019 most banks had reduced their variable reward maximums to less than 50 percent of fixed and, the median is now significantly less than 50 percent. This downwards adjustment over time is particularly evident for home lenders and Sellers (General)[65]. Banks report that fixed pay has been adjusted in some cases, especially for individuals that consistently used to attract bonus payments in excess of their current maximum. Note also that the median of the maximum achievable variable pay across all roles remains relatively unchanged from 2018 to 2021, which suggests most movement in variable reward opportunity has occurred at the top end.

Across the sector, nearly all banks now have a maximum variable remuneration opportunity that does not exceed 50 percent of fixed pay and is typically much less. In my view, 50 percent for specialist bankers is an upper limit, not a target, and with a bias towards something significantly lower. In interpreting this very encouraging outcome so far, it is important to note:

- One significant bank still offers maximum achievable variable pay for some home lenders higher than the industry norm and above (in a few cases well above) a reasonable interpretation of what constitutes 'a relatively small proportion of fixed pay' in 2021. The risk is that having a significant player above the recommended cap may legitimise similar future behaviour by others, which may provoke a competitive upwards spiral, and significantly increase the risks of mis-selling. It is pleasing that this bank has committed to reducing this maximum to no more than 50 percent of fixed pay – immediately for new hires and progressively over a relatively brief period for others currently eligible for more than 50 percent. I sincerely hope that each bank accepts that '50 percent' is recommended as a cap, not a target to which all should aspire!
- Some banks have stated that the maximum achievable variable pay levels are hypothetical caps given that most staff have little prospect of achieving the required level of performance.
- Some banks do not have a formal cap on the maximum achievable variable pay level and argue that in practice the variable opportunity remains much less than 50 percent of fixed pay. These banks should include processes to ensure variable reward opportunity is formally capped at 'a relatively small proportion of fixed pay'.

4.2.2.5 *Risk and behavioural gateways are adopted widely*

Most banks require a minimum standard of behaviour or adherence to the bank's values before a banker is considered eligible to access variable rewards (called a **'gateway'**[66]). Most rely on monitorable indicators

[64] Interim Review, p 31, which also provides a discussion of relevant factors to be considered.
[65] The 2017 Review notes: 'Based on the data gathered, there were instances where home lenders received a variable reward which was almost up to six times their fixed pay and Managers received up to 1.5 times their fixed pay as a variable reward' (p 20, footnote 58).
[66] Several banks also hard wire behavioural indicators into their performance scorecard. See section 3.2.3.2.

such as formal determinations of a breach of the Code of Conduct, a formal warning etc. Some, however, also allow managers to decide based on their observation of each individual, including their interactions with customers and other team members. Other gateways may relate to the timely completion of obligatory training and compliance with policies intended to manage the bank's compliance risks in some contexts. Where gateways apply, failure to reach the standard required to open a gate renders the banker ineligible to participate in variable rewards (with other consequences also possible if an indiscretion is sufficiently severe).

In a few systems, failure to meet such a requirement may not lead to automatic ineligibility. The system may enable a manager, usually subject to high level oversight within the bank, to exercise discretion about whether access to variable rewards should be withdrawn or simply reduced. The assessment in respect of these requirements (which may themselves include elements of a discretionary assessment in some instances) operates as a **modifier** i.e. it reduces the reward to which the individual would otherwise be entitled. In some systems the decision about how much to reduce an entitlement may also be discretionary. In every such case, the manager retains the option to reduce the reward available to nil.

Discretion in the enforcement of gateways and modifiers is intended to allow exceptional cases to be managed with care. Exceptions to some gateways, for example, might be allowed if the failure did not have serious consequences, occurred through ignorance or inadvertence, and is remedied promptly. Similar factors could bear on the extent of reduction to otherwise accessible rewards if a modifier is triggered. Such discretion is always subject to high level oversight and detailed justification.

Across the banks surveyed[67], there was an equal split between the use of modifiers and gateways:

- Half the banks apply risk or behavioural **modifiers**. These modifiers reduce payments otherwise available to an individual judged not to have met the standards required, with the scale of the reduction determined by the severity of the breach. Typically, moderate breaches can reduce the achievable reward by at least 20 percent. Severe breaches reduce the opportunity to zero.
- Half apply risk or behavioural **gateways**.[68] When gateways are applied eligibility to receive any variable pay is subject to meeting minimum behavioural standards and following compliance procedures.

4.2.2.6 *Recognition programs focus on reinforcing desired behaviours*

Many banks continue to administer recognition schemes that identify exceptional performance and provide a typically small reward (financial or otherwise)[69]. In 2017, sales performance could have been a significant element of performance singled out for additional recognition. That is rarely the case currently. Current approaches typically recognise and celebrate as role models individuals who demonstrate the bank's values or show consistent risk compliance. This can encourage staff to demonstrate exceptional risk or ethical behaviour rather than only meeting the minimum standard to pass the gateway for variable reward payments. In a few cases, though, banks run recognition programs for home lenders that include financial performance as a specific criterion, either directly, or as a component of a balanced scorecard type approach.

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[67] This assessment was made based on the banks that provided data on risk and behavioural modifiers. Some banks do not award variable remuneration for in-scope staff. These banks were not included in the assessment.
[68] Behavioural gateways include demonstrating ethical behaviour, company values and/or the code of conduct.
[69] Though some in-kind awards, such as attendance at off-site professional conferences, can entail a significant cost to the bank.

4.2.3 Home lenders are treated differently to other roles

Different labour market dynamics operate for home lenders than for other in-scope roles. This arises because banks and mortgage brokers recruit talent from a linked labour market in which remuneration practices differ. Mortgage brokers are still remunerated on a commission basis, which is related directly to the value of mortgages drawn down by their customers. Commission is initially payable upfront, when the mortgage is initially activated. In addition, mortgage brokers can still access trail commissions over time, which can be attractive to home lenders with a large customer base. Home lenders who are bank employees currently have significantly different remuneration arrangements – a higher proportion of fixed pay and less upside potential. Banks need to craft an attractive package, having regard to total remuneration and the individual's tolerance for risk regarding their remuneration.

Some banks reported that some bankers left their employers as a result of the changes introduced to comply with the 2017 Recommendations. Some may have exhibited behaviours that the bank considered too risky in the context of its currently desired culture. Undoubtedly, though, these included good sales staff who also behave ethically with the customer's interests at heart. This risk of losing good people who find a commission-based remuneration model more attractive will most likely be an enduring issue for banks to manage.

This tension is reflected in the fact that home lender schemes figure reasonably consistently as anomalies in the descriptions of bank practices that support the findings of this review. Compared to other roles, for example, the scorecards for many home lenders within the industry still conform to a more formulaic calculation of scorecard outcomes, implying a more direct line of sight between sales performance and performance rating than more discretionary schemes. Similarly, some home lender schemes apply relatively formulaic relationships to translate the scorecard rating into a variable pay outcome, providing a clearer line of sight between sales performance and pay than other schemes.

Moreover, home lender schemes are more likely to be counted amongst those schemes that have an inappropriately large emphasis on financial indicators than other schemes. The relatively rare recognition programs that still pay attention to financial metrics are all programs that operate in respect of home lenders (see section 4.2.2.6). Finally, as section 4.2.2.4 shows, although now typically lower than in previous years, home lenders also have available to them a considerably higher variable reward opportunity than most other roles.

Banks are currently competing for share in mortgage markets. Not all banks can succeed in securing that objective simultaneously. Against that background there is a real risk to the longevity of the current widespread adherence to both the letter and the intent of the 2017 Recommendations that require no direct links between sales and variable pay with variable pay only a relatively small proportion of fixed. The industry needs to manage this risk in ways that avoid undoing the good work of the last 5 years and again undermine public trust.

4.2.4 More discretion is applied in Variable Remuneration decisions

4.2.4.1 *Discretion is applied in multiple ways*

As discussed in sections 3.2.2.1 and 4.2.2.5, manager discretion can be applied in different stages of the performance management process and to allocate variable remuneration, as summarised in the figure below:

Figure 3 | Stages where manager discretion can be applied

PERFORMANCE MANAGEMENT

Objective setting
Managers can apply discretion to set personalised Key Performance Indicators for each individual rather than applying a standardised set of targets for each role

Assessing performance against each objective in a scorecard
Managers can apply discretion to assess what was achieved in reference to both qualitative and quantitative measures rather than having a formulaic approach where a system calculates the performance against quantitative targets

Assigning an overall performance rating
Managers can apply discretion to allocate an overall performance rating informed by 'what' was achieved on each objective and 'how' to consider both, behaviours and performance

VARIABLE PAY

Assessing whether individuals pass risk and/or behavioural gateways
Managers can apply discretion to determine whether individuals are eligible for any VR, depending on whether they demonstrate minimum behavioural standards and comply with risk policies

Allocating variable remuneration
Managers can apply discretion to allocate variable remuneration that is informed by the overall performance rating and variable reward pool

It is possible to categorise the application of discretion in the following ways:

- **Low** - The variable reward outcome is principally calculated based on a formula. A rating is established as the weighted sum of metrics that capture performance against targets in each element of a scorecard, which entitles the individual to a predetermined amount or share of the pool of funds available. Managers may have some discretion to override some elements of the formula, though this would only be rarely applied.
- **Medium** – Variable rewards are determined largely formulaically based on performance ratings, but managers can exercise discretion and determine a reward payment within a defined range.
- **High** - Managers determine variable reward payments, with relative performance and the size of the variable reward pool available the primary determinants of the judgement the manager ultimately makes. These decisions may be subject to some guidance / calibration to ensure consistency, but variable reward decisions are ultimately fully discretionary.
- **No individual bonus opportunity exists** – As noted in section 4.2.2.3 there are several banks where there is no variable reward opportunity, for at least some roles.

The tables below show the number of banks that apply each level of discretion in respect of the determination of the amount of variable reward an individual will receive and their performance rating (as explained in Section 3.2.2.1) for Tellers and home lenders[70]. The tables show:

- The majority of banks either apply a medium or high level of discretion to both the determination of a performance rating and the size of the variable reward to be provided to each individual performing these roles.
- However, 4 banks exercise only a low level of discretion when determining the variable rewards offered to home lenders. Indeed, at an industry, level home lender schemes are more formulaic; on average there is a lower level of discretion applied in performance management and the allocation of variable rewards to home lenders compared to Tellers. This may, reflect the competitive dynamics in home lender markets, as explained in section 4.2.3.

Table 4| Level of discretion applied in performance management and VR allocation for home lenders[71]

	Level of discretion applied in VR allocation			
Level of discretion applied in performance management	L	M	H	No bonus
L	1	1	0	1
M	2	3	0	0
H	1	2	3	0

Table 5 | Level of discretion applied in performance management and VR allocation for Tellers[72]

	Level of discretion applied in VR allocation			
Level of discretion applied in performance management	L	M	H	No bonus
L	0	0	0	1
M	1	2	0	0
H	0	2	1	4

4.2.4.2 *Managers need support to exercise discretion consistently and well*

Manager discretion has several advantages. A manager can more readily consider the 'how' as well as the 'what' of an individual's achievements when discretion is exercised. Discretionary systems are less open to gaming than formulaic ones, which, amongst other things, can encourage sales banking or overzealous seller behaviour to boost bonus payments. Discretionary systems reduce the perception that there is a predictable link between sales activity and the value of variable reward achievable. Discretionary systems more readily enable a manager to consider the 'degree of difficulty' staff experience in addressing the KPIs

[70] Other roles are discussed in Appendix C.
[71] The role of home lenders is not applicable to all banks. Only 14 banks have in-scope home lenders.
[72] The Teller role is not applicable to all banks. Only 11 banks have in-scope Tellers.

embedded in their scorecard or in otherwise addressing performance expectations[73]. Discretion can give appropriate weight to qualitative indicators or elements of performance that are difficult to measure reliably and more readily lends itself to a holistic assessment than a formulaic one, especially as conditions change.

However, discretion also poses challenges. Ensuring consistency between managers and equitable treatment of individuals is key. Most banks are clearly signalling they understand the need to provide training, coaching and other support to managers. They also have strong measures in place to provide clear communication with affected staff about how the process should work and their rights to 'speak up' if what they experience is inconsistent with the preferred norms. Most, though not all, have also established formal calibration / moderation arrangements intended to ensure consistency and equitable treatment. The effectiveness of these arrangements depends on the insightfulness of managers, the quality of their judgements and the documentation they provide to support them, and the creation by leaders of a 'psychologically safe' environment that both permits and requires respectful challenge to minimise the risk of 'group think' or an unconscious bias towards sales.

The involvement of parties not directly in line roles can provide an important challenge perspective. Human Resources (HR) and the risk functions have important roles to play in challenging the status quo, including in respect of such risks. Internal audit could usefully review the operations of the challenge role, from time to time, to ensure its integrity. Both initiatives (viz. training / communication and calibration / moderation) are expensive and time consuming. They need to be pursued consistently, over time. It is far from clear to me why participation in well-designed calibration / moderation processes would not be mandatory at all banks that rely on manager discretion as a significant component of performance appraisal and / or the assignment of variable remuneration.

Manager discretion is not inconsistent with the intent of the 2017 Recommendations if it is exercised in line with the objectives of the 2017 Review. It is not a simple matter to establish, however, whether that condition has been met in practice. Boards and leaders need to remain vigilant and ensure that managers exercise their discretion consistently and in line with the spirit and intent of the 2017 Recommendations, even when the community, media and others stop watching, as eventually they well might. Regulators may also have a role to play in ensuring that internal challenge functions are effective. This is further discussed in sections 3.2.2.1 and 4.2.4.

4.2.5 Banks need to consider the behaviour driven by performance measures in executive scorecards

Executive scorecards for Short Term Incentives (STIs) typically balance financial measures with customer, people and risk management measures. However, the performance measures for executives across the industry for almost all banks include targets on mortgage growth relative to 'system' and NPS performance relative to peers. It is impossible for all banks to simultaneously improve their position relative to other banks. At least some banks will not achieve their preferred outcome. Scorecards designed to focus on the relative position rather than the absolute outcome, risk placing undue pressure on frontline staff to make sales when executives are not meeting their targets.

[73] During interviews, several banks cited recourse to such discretion exercised during various COVID-19 events as an illustration that the achievement of sales or other targets were no longer an overriding consideration in the assessment of performance and eligibility for rewards, whether financial rewards or otherwise.

4.2.6 Remuneration practices of third parties remain largely commission based

Remuneration arrangements that apply to mortgage brokers are not in-scope for this review. Most introducers and referrers receive upfront commissions with no trail commissions. Most banks have reviewed these arrangements, consistent with the 2017 Recommendations. Some additional volume-related payments previously available to introducers and referrers have been removed. However, only one bank has removed all commissions as a consequence of their review.

4.3 Future directions

Substantial reforms have occurred in the arrangements whereby eligibility of in-scope retail staff to access variable reward payments is determined. However, there is one significant bank that currently offers maximum incentive payments to home lenders in excess of 50 percent. They have committed to reducing this to 50 percent or less of fixed pay over a brief transition period. I strongly encourage this bank to keep this transition period as brief as feasible. I'd also encourage the very few banks that currently link recognition programs to sales also desist. Moreover, leaders and regulators need to ensure that vigilance about such matters is maintained as time passes.

4.3.1 The future is fragile and requires vigilance by Boards and bank leaders

It is inevitable that attention (both internal and, also, externally driven) will be diverted elsewhere as time passes and conditions change. Boards and leaders would be wise to adopt and promulgate an attitude similar to 'lest we forget' by frequently telling stories that remind staff of the consequences for the bank and for customers of poor practices in the past. Reputational and remediation costs are not small when things go wrong. Moreover, community trust is difficult to restore, once lost.

There are credible scenarios in which Boards and senior management come under pressure in the future to wind back reforms to culture and practice implemented in recent years in order to secure strategic goals that appear to be under threat (see, for example, the discussion in section 2.3.3). Boards, leaders and remuneration teams would be wise to establish arrangements that check regularly that the letter and intent of the 2017 Recommendations continue to be adhered to within the bank as time passes. For example, HR and the internal risk function should be actively involved in providing regular assurance to the CEO and the Board regarding their continued adherence to the letter and spirit of the 2017 Recommendations, including that:

- The maximum achievable variable remuneration payments are always no more than 50 percent of fixed pay, and preferably considerably less (especially for non-specialist roles);
- The proportion of variation in variable reward outcomes within a role explained by sales and financial performance is less than 33 percent, with no direct, quantifiable link between sales / financial performance and personal variable reward;
- Assessments leading to variable reward outcomes are truly balanced between the 'what' and the 'how'; and
- Leaders and managers possess the requisite skills to administer discretionary schemes leading to the allocation of variable remuneration payments consistently and well and in support of customer-centric norms, supported by effective calibration and challenge processes.

The last three of these comments apply also to performance management.

4.3.2 The future is fragile and requires vigilance by regulators

From the regulators' perspective, the systemic risks associated with retail banking are typically perceived to be an order of magnitude smaller than those posed elsewhere in the financial services sector. Much of the regulatory framework in respect of conduct risk is aimed at senior managers and those who manage significant risks that could imperil the bank (and, in an exceptional case, the financial system). The consequence of mis-selling is more likely to be felt by consumers than the bank, except in the case of systemic compliance breaches or systemic mis-selling that requires wide-scale remediation. However, relatively recent history shows that the retail sector can be a source of substantial systemic risk - the GFC was triggered in part because of poor mortgage lending practices in the subprime market!

External oversight bodies such as APRA and ASIC should pay attention to how banks are responding to the need to ensure their performance management arrangements, variable remuneration practices and lived culture provide incentives in favour of ethical conduct and a focus of the customer, not simply sales, including in retail banking. Their roles vary and, in resource constrained environments, their attention can instinctively be directed towards monitoring the biggest risks. However, there are options available to the key regulators that are worthy of consideration. One area of examination, for example in the context of ASIC's Close and Continuous Monitoring Program, could be to establish whether challenge roles are discharged effectively within the calibration / moderation arrangements that provide checks and balances when discretion is exercised in the context of retail banking performance rating or variable remuneration decisions. See also sections 2.4 and 5.3. Regulators such as APRA and ASIC could also usefully introduce periodic oversight arrangements to ensure on going adherence to the letter and spirit of the 2017 Recommendations.

5 Workplace culture

5.1 Context of this section

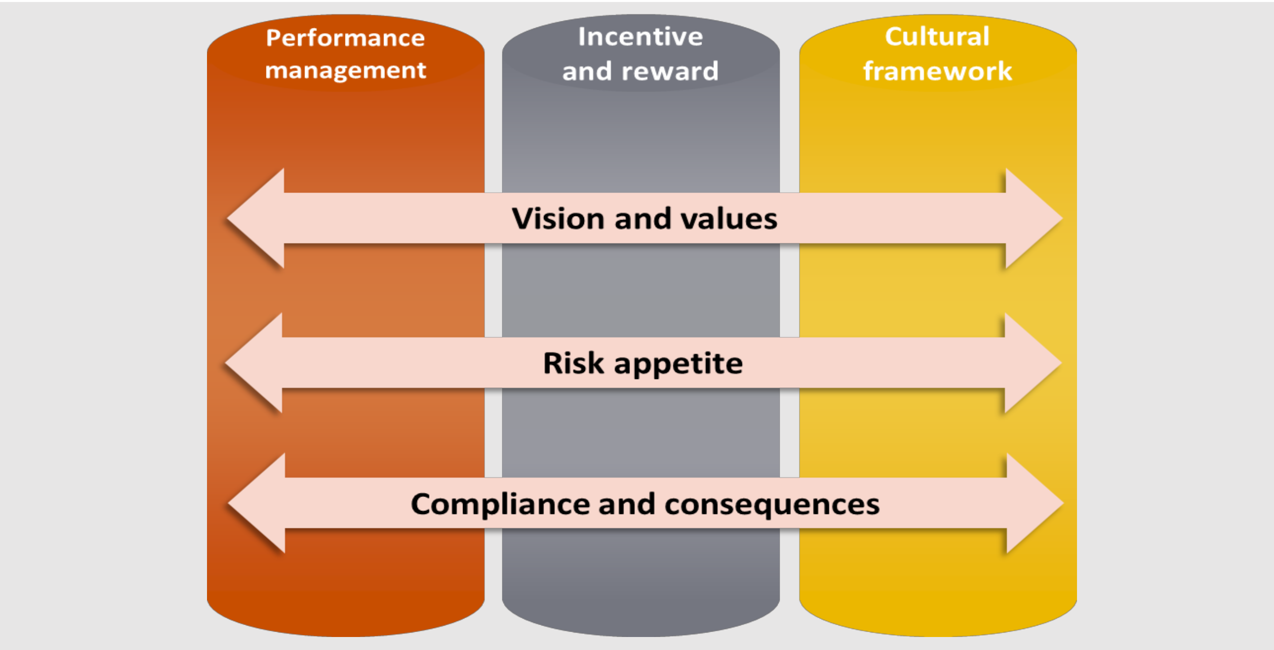
The incentives built into remuneration arrangements may be magnified or moderated by the way in which performance is managed and by the established mores or practices of the workplace (that is, its culture). A heavily sales-oriented management, for example, may instinctively value and rate more highly successful salespeople when assessing their performance and more readily award them discretionary rewards. This may be fully consistent with the objectives of the organisation. Alternatively, it may work against attempts to establish a more service-oriented approach, if that is the organisation's objective.

Other aspects of governance may similarly moderate or magnify the incentives built into remuneration arrangements. These include:

- The values of the organisation and its stated purpose or vision;
- The appetite for risk;
- Systems to test compliance with regulatory obligations or the organisation's policies and procedures; and
- The consequences (actual or perceived) of non-compliance.

Behaviour of individuals within an organisation will be affected by their understanding of or their belief about matters such as these. The figure below, which is reproduced from the 2017 Issues Paper, illustrates the linkages.

Figure 4 | Systems that direct, influence and hold accountable the activities within an organisation



My successive reviews have taken a holistic approach in assessing the approaches banks have adopted to better manage the risk of mis-selling and poor outcomes for customers. The 2017 Report noted:

In many banks the cultural orientation towards sales is deep seated. This orientation has been built over many years, in some instances exacerbated by incentives arrangements. Winding back the associated risks *of mis-selling and poor outcomes for customers will require a coordinated effort across all aspects of the governance framework and will take time.*[74]

The 2017 Recommendations therefore addressed not just remuneration but also other aspects of an organisation's governance such as those discussed above. These included aspects of leader development, management skill, efforts to articulate and embed a desirable culture, and governance. The 2017 Report acknowledged that the scale of the task varied considerably between banks. Some, for example, had already begun to move in the required direction or had a culture they believed was already sufficiently customer focused. For others, however, the changes required were substantial for at least some retail staff roles, and it was expected that their journey of cultural renewal would prove challenging.

The following sections examine the steps that banks have taken to ensure that their culture and leadership capabilities are 'fit for purpose', having regard to the 2017 Recommendations. Section 5.2.3 reports the perceptions of in-scope staff about the customer focus of their organisation.

5.2 Assessment of implementation of recommendations by 2021

5.2.1 Most banks have invested significantly in culture change

Most banks have invested significantly in key drivers that reinforce a shift of culture and practice away from an excessive focus on sales to a more balanced, more customer- centric approach. Banks that have embarked on such culture change have directed investment to:

- Define the bank's values;
- Increase leadership capability;
- Ensure staff alignment to values;
- Establish the underpinning structures and processes that support the desired culture; and
- Monitor lived culture against the desired one.

These areas are explored in more detail in the sections below.

However, some banks, specifically some of the smaller and more community focused banks, have made significantly less additional investment than others. They believe that, from the beginning of this exercise, they have maintained a customer-centric culture and that their bank's operations have continued to be grounded in complementary values[75]. Their focus has been principally on maintenance of culture rather than wholesale reform[76].

Section 5.2.3 provides evidence distilled from responses to the survey conducted earlier this year to establish staff perceptions of the extent to which industry culture is currently more customer or sales-centric.

5.2.1.1 *Some banks have refreshed their values*

Several banks have refined and simplified their values and desired behaviours to clearly articulate what is expected of staff and to hold bankers accountable. Some have defined new values and behaviours and are in the process of embedding them. In some cases, external organisations were engaged to conduct focus

[74] 2017 Report, p5.
[75] With one or two exceptions, perceptions reported in the Survey by staff of these banks generally support this view.
[76] Although one or two such banks have also introduced programs intended to strengthen the commercial focus of their organisation, without compromising its customer-centric ethos.

groups amongst staff at different levels to co-create and clearly define the behaviours and values needed to underpin the bank's vision and align banker behaviour to its strategic direction. More banks are also focusing on encouraging decision makers to ask, 'should we' rather than just 'can we', to inform well-based judgements and to imbue ethical behaviour. Some banks have pursued this objective by refreshing their Code of Conduct.

Banks that refreshed their behaviours typically increased their focus on improving risk behaviours, acting with integrity and acting in the best interest of the customer. This has been supported with internal communications and provision of learning resources to promote and embed a shared understanding of desired behaviours. However, frontline staff interviewed in the FSU roundtables mostly believe the change in values and other language is more a veneer than a reality. It is difficult to judge how pervasive such a sentiment is amongst in-scope staff. However, the fact that a significant minority of respondents to the staff survey believe their bank still to be more sales than customer-centric reinforces the need for banks to continue to hone their practice to their intent.

5.2.1.2 *There is a focus on uplifting leadership capability to model the desired culture*

Banks also report significant investment in training leaders to lead culture change, set the 'tone from the top', and model desired behaviours, expecting correct behaviours to then cascade throughout the organisation. Many have documented the changes they want to see in leadership to drive the changes required to achieve their desired culture, with several banks specifically targeting building capability in areas such as ethical leadership, effective risk management, performance management and customer innovation.

Additionally, banks have run leadership forums to collectively and openly discuss barriers to achieving their desired culture and embedding the expected behaviours. Most banks also run regular staff forums to update bankers on the culture landscape and encourage ethical behaviour, with a focus on customer service. These forums help to reinforce the desired culture. They also provide leaders an opportunity to discover and respond to staff questions. Most banks also report a concerted effort to encourage staff to 'speak up' and report activities that fall short of the expected standards. Some also encourage leaders and staff to ask, 'should we', not just 'can we'.

5.2.1.3 *Banks continue to ensure staff are equipped with skills to achieve the desired culture*

Many banks have made (and remain committed to making) a substantial investment in training in areas such as ethical decision making and banking fundamentals to promote regulatory compliance and deliver better risk outcomes. Given the impact of COVID-19, several banks provided training to equip staff with the skills to have effective conversations with vulnerable customers. During consultations, many senior executives expressed clear pride in how their staff had responded to the needs of vulnerable customers and others during the COVID-19 pandemic, which they cited as evidence that culture in their bank has shifted substantially towards putting the customer first in the last 5 years.

Almost all banks require staff to undertake mandatory training on regulatory compliance and risk management. Some banks run regular refresher training programs on how to demonstrate the behaviours that underpin the bank's values and what constitutes undesired behaviours.

There has been considerable investment across almost all banks in coaching and other approaches intended to improve frontline capability to have effective conversations with customers. Some banks have supported this through the creation or refreshment of customer conversation frameworks to support staff to deliver intended outcomes. Banks must ensure that the intent of such training is not confused with language or feedback during performance discussions that are more akin to an objective of driving sales.

5.2.1.4 *Banks have redesigned operational elements to support a customer – centric culture*

Almost all banks report they have undertaken a range of interventions designed to support building (or, in some cases, maintaining) a strong customer-centric culture. These include:

- Strengthened onboarding and offboarding processes to recruit and retain staff that embody the bank's desired, customer-centric / ethical values;
- Refreshed performance management systems which seek to secure greater alignment to (in some cases, refreshed) bank values;
- Reorientation of calibration / moderation sessions towards performance against risk and behavioural measures (the 'how') and not just the 'what';
- Updated recognition programs that typically (not always) celebrate individuals who demonstrate the bank's values. Consultation with banks suggest that these immediate recognition schemes create momentum and can send a powerful message about tangible behaviours that are valued;
- (In some cases) refreshed consequence management frameworks and codes of conduct to ensure there is a consistent approach to manage misconduct and breaches in policy, which is supported by appropriate governance; and
- Strengthening, then promoting and supporting, whistle-blower policies that promote safe ways to speak up and raise concerns.

5.2.1.5 *There has been considerable investment to measure cultural change*

All banks have stated they run internal employee surveys to create a safe channel for staff to provide feedback. These surveys inform the leadership team of any emerging employee perceptions and identify key areas that need focus. They are typically supported by programs that allow and encourage staff to 'speak up' and, in some cases, to ask 'should we', not just 'can we'.

Some banks have invested in more sophisticated approaches to measure cultural change, for example through culture dashboards, to create awareness of the current cultural landscape and to track progress against the desired culture. These banks have defined target metrics and track trends over time to iteratively test and, desirably, continuously improve their culture.

Whilst there has been considerable investment to monitor culture there has been little progress as an industry to monitor customer outcomes. As such, banks should carefully consider how they can monitor culture to draw out any themes relating to a bias towards sales in preference to ethical behaviour and customer service, what measures should be tracked to monitor customer outcomes and what are the desired outcomes required to achieve a more customer-centric culture.

5.2.2 Continued focus is required by most banks to achieve their desired culture

Despite having committed substantial resources, most banks that are seeking to achieve significant change acknowledge the transition is incomplete and 'it is a journey' to achieve their desired culture. Even banks that believe their culture is close to their preferred state acknowledge that preserving the status quo requires vigilance and effort. Most banks acknowledge that consistent effort will be required into the future.

Most banks report that they have embarked on a sustained drive to simplify internal processes and product lines with a view to improving their customer experience. Several banks report that their efforts to improve customer service is hampered currently by legacy systems, which can be perceived as leading to a poor customer experience. They acknowledge that continued investment to support simplification is a strategic imperative.

The 'ongoing journey' the industry generally has embarked upon to achieve a customer-centric culture was supported by findings of the staff survey. Staff perception are that the industry is broadly more customer focused than sales-focused, but there remains room for meaningful improvement. These perceptions are explored further in section 5.2.3 below.

5.2.3 Consolidated findings of retail banking staff perceptions of remuneration practices

Following a recommendation of the Interim Review in 2019, a Survey was designed and administered across 18 banks to gather perceptions of frontline staff about the extent to which they perceive the culture of their retail bank is sales-centric or customer-centric. Around 37,000 staff are estimated to be in-scope. Some 13,760 effective responses were received, a respectable response rate of 37 percent, enabling statistically valid estimates to be provided at a population level.

Survey respondents were asked to indicate their level of agreement to 16 statements relating to 'what is valued at your workplace'. These statements were framed to be either sales-centric or customer-centric. An average customer-centricity score was allocated to each statement, on a scale from 2 to -2, where:

- 2 means I strongly agree on customer-centric statements or strongly disagree on sales-centric statements;
- 1 means I agree on customer-centric statements or disagree on sales-centric statements;
- 0 means I neither agree nor disagree on the statements;
- -1 means I disagree on customer-centric statements or agree on sales-centric statements; and
- -2 means I strongly disagree on customer-centric statements or strongly agree on sales-centric statements.

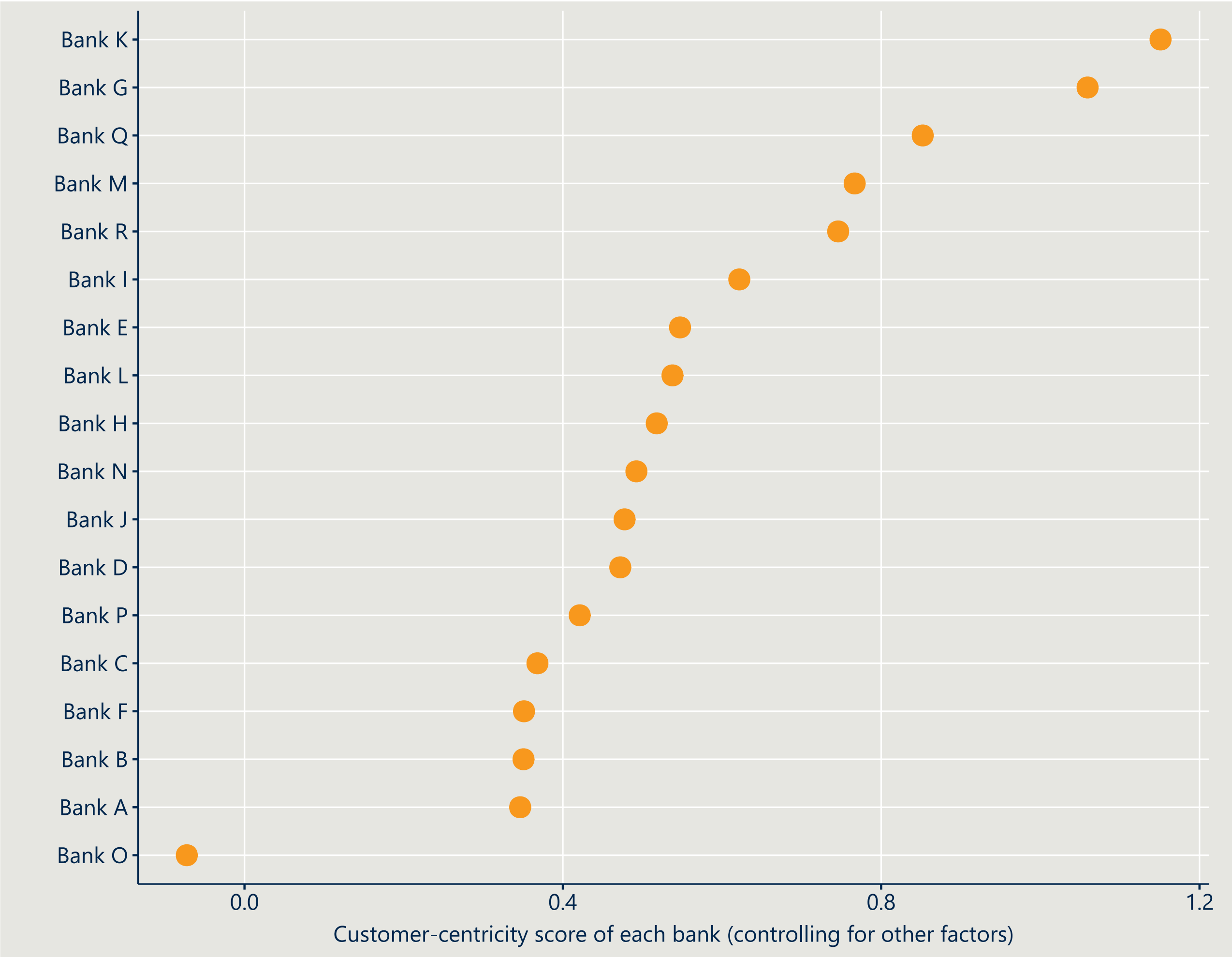
The Survey results indicate that at an industry level, staff perceive that on average banks are more customer-centric than sales-centric. The average perceived level of customer-centricity achieved by the industry was equal to 0.6, on a scale from -2 to +2, where +2 indicates the highest level of customer centricity and -2 indicates the lowest level of customer centricity. This is a creditable result. As an averaged result, however, it implies there is room for improvement. Examination of the range of results reported for each bank suggests this is true both in respect of the industry overall and for almost all banks.

As Figure 5 shows[77], perceived customer-centricity varied considerably between banks. It was not correlated to the size of bank, with statistically significant differences in the customer-centricity scores between the major banks, for example. However, on average, after controlling for factors that are

[77] The figure shows the average score for perceived customer-centricity in each bank, after controlling for factors such as the product, role and age mix of respondents in the bank. Confidence intervals are not shown to avoid identification of individual banks.

significant independent influences, managers are on average somewhat more willing to agree that their bank is customer-centric than Tellers or Sellers[78].

Figure 5| Regression of perception of customer-centric workplace on various factors



All but one bank achieved an average customer-centricity score above zero, which is encouraging. Indeed, for most banks, three quarters of their staff have positive perceptions of customer-centricity (their responses were higher than zero). However, the average score across the industry indicates there is an opportunity to improve customer-centricity in retail banking. Moreover, most banks have some staff who clearly do not see the workplace as customer-centric, suggesting room for improvement in one or more of processes, systems, behaviours, or communication.

Some banks were surprised by their staff's assessment of their level of customer-centricity, implying a disconnect between the intentions of senior executives and the perceptions of frontline staff. Pleasingly, the typical reaction of senior managers when discussing these results during consultations was not to challenge the validity of the results but to want to look further into the underlying causes of these perceptions. Indeed, virtually all banks acknowledged there is work to be done at their organisation to shift the culture to achieve a greater focus on the customer, albeit some banks (usually smaller community

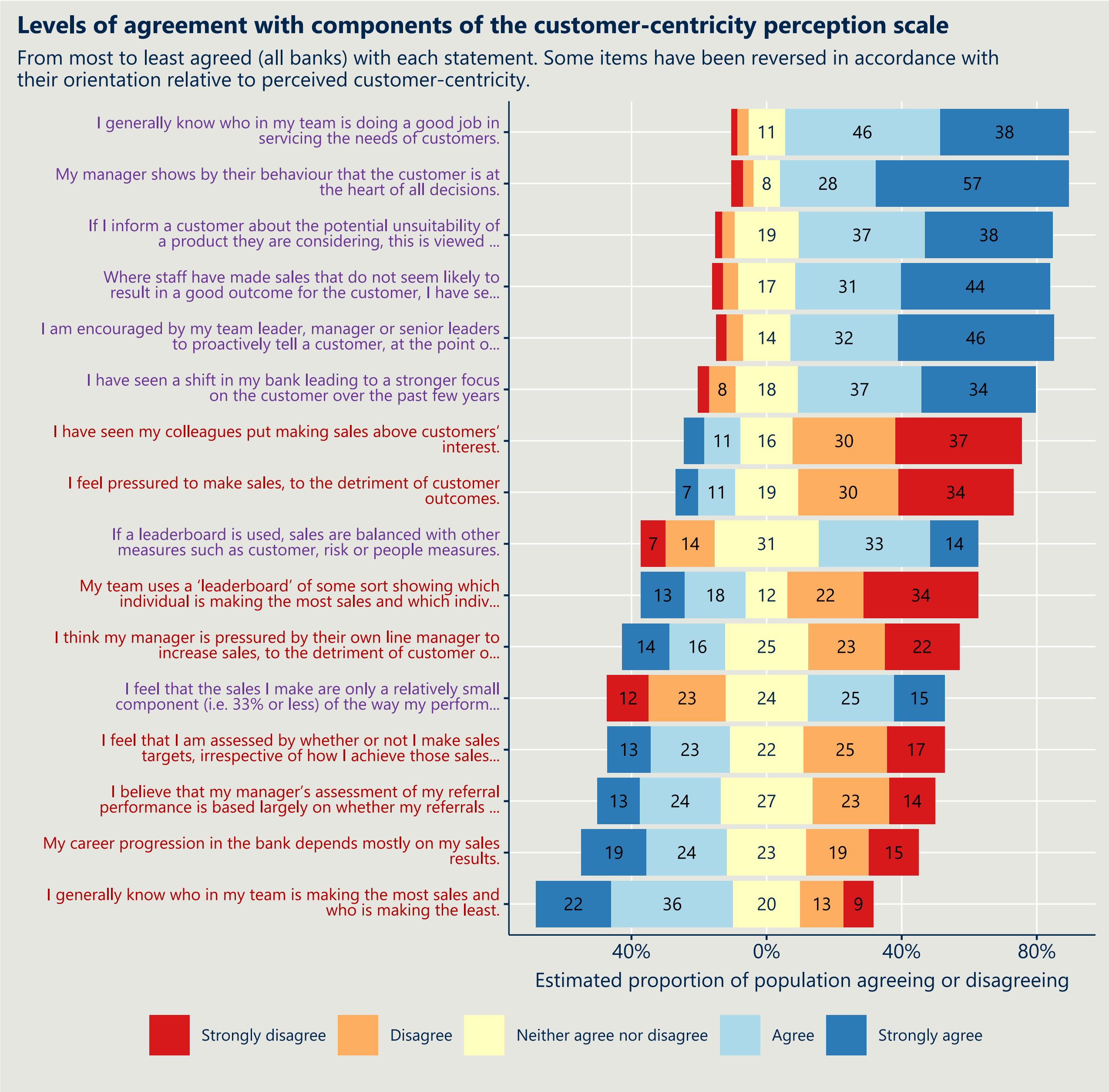
[78] See
Figure 19, Appendix A.

banks) believe they are very close to where they need to be and are principally in maintenance mode rather than change mode. One or two banks observed with wry amusement that the industry level convergence towards a more customer-centric culture could put an element of their competitive advantage at risk.

All in-scope staff, irrespective of whether or not they were eligible for variable pay, were invited to participate in the Survey. The results imply that staff who are eligible for variable remuneration perceive their workplace to be slightly more customer-centric than staff who are not eligible for variable pay. However, this result was only evident when access to such remuneration was not perceived to be linked to achieving revenue targets, customer acquisition or meeting business targets.

Figure 6, below depicts the average results achieved for each of 16 questions that were designed to test the relative customer centricity of their bank's practices and culture. Across all 16 statements, staff demonstrated stronger agreement than disagreement on all perceived customer-centric practices and stronger disagreement than agreement on most sales-centric practices, which is encouraging.

Figure 6 | Levels of agreement with each of the 'what is valued in your workplace' statements



The chart above shows that seventy percent or more of staff either agree or strongly agree with the following 6 customer-oriented statements, with staff usually recording slightly lower scores than their near managers[79]. These statements are arranged in descending order of the customer-centricity score:

- I generally know who in my team is doing a good job in servicing the needs of customers;
- My manager shows by their behaviour that the customer is at the heart of all decisions;
- If I inform a customer about the potential unsuitability of a product they are considering, this is viewed positively by my team leader or manager;

[79] The biggest difference in the level of agreement was for the statement "If I inform a customer about the potential unsuitability of a product they are considering, this is viewed positively by my team leader or manager" where 75 percent of staff agreed/strongly agreed and 84 percent of their near managers agreed or strongly agreed.

- Where staff have made sales that do not seem likely to result in a good outcome for the customer, I have seen my manager respond with appropriate actions e.g. managing the performance or behaviour of the staff member, teaching the staff member how to better serve the customer or implementing appropriate training;
- I am encouraged by my team leader, manager or senior leaders to proactively tell a customer, at the point of sale, if a product is unsuitable; and
- I have seen a shift in my bank leading to a stronger focus on the customer over the past few years.

The statements that implied the lowest level of customer-centricity are:

- I generally know who in my team is making the most sales and who is making the least, which had a score of -0.5 as 58 percent of staff agreed or strongly agreed with the statement; and
- My career progression in the bank depends mostly on my sales results, which had a score of -0.1 as 43 percent of staff agreed or strongly agreed with the statement.

A result that surprised most banks was that over 30 percent of staff across the industry agreed with the statement 'my team uses a "leaderboard" of some sort showing which individual is making the most sales and which individual is making the least'. Indeed, at least 15 percent of staff in every bank agreed with that statement or 'I generally know who in my team is making the most sales and who is making the least'. This is particularly surprising because only one bank reported to the review that they still used leaderboards. Over 20 percent of staff disagreed with the statement that 'if a leaderboard is used, sales are balanced with other measures such as customer, risk or people measures'. However, frontline staff in some of the organisations with the highest levels of customer-centricity also reported that leaderboards exist, which demonstrates the importance of culture and setting the 'tone from the top' to establish workplace behaviours and expectations that are grounded in acting in the best interest of the customer.

5.3 Future directions

A bank's culture is an important pillar to support behaviour that is ethical and is in the best interest of the customer (and, indeed, to deeply embed expectations within a workplace that require such behaviours as 'the way we do things around here'). While changing policies can shift the bank's variable remuneration structures and performance management systems, shifting culture requires a considerable and sustained level of investment and visible leader commitment to embed the desired culture in practice. Vigilance is required to achieve and maintain a sustainable customer-centric culture, whereby appropriate behaviours, focused on the customer, are instinctive. Culture is influenced by the hard and soft wiring of an organisation. Delivering a sustainable culture requires a holistic approach that is integrated across the whole organisation.

5.3.1 Culture is key and needs constant vigilance and transparency

While there has been considerable investment in culture, especially by some banks, the variability of the results recorded in the staff survey by individual banks suggest that there is an opportunity still for the industry to improve customer-centricity. Each bank has the option to access a report of their own Survey outcomes, which is directly targeted at providing insights into bank culture. Each bank can thus identify the nature of the opportunity before it.

However, I believe it is in the interests of the industry that it undertakes and publishes the results of regular reviews of culture to specifically draw out issues relating to customer service or ethical behaviour, and develop measures to assess, progress and monitor contemporary culture. This could be done by complementing internal surveys conducted by each bank with a specific and common survey of remuneration and incentive practices along similar lines to the one developed for this review, on an annual basis. The ABA may have a role to play in facilitating such a development. Alternatively (or, as well), such an issue may be addressed through the risk culture survey currently under development at APRA. APRA's role is typically characterised in terms of securing the stability of the financial system, in which case retail banking may be thought to be of low risk. However, arguably, the GFC illustrates the potency of inadequate oversight of retail banking culture. Arguably, periodic, common, transparent, pro-customer culture reviews would help to preserve and extend the benefits of the substantial work the industry has undertaken in recent years to build public trust. In addition, regulators such as APRA and ASIC could also usefully introduce periodic oversight arrangements to ensure on going adherence to the letter and spirit of the 2017 Recommendations.

Appendix A - Retail banking staff perceptions of remuneration practices

Glossary of terms used in Appendix A

Term	Definition
Correlation, and correlation matrix	The degree to which two variables “move” in relation to one another. Positive values mean they move in the same direction. A value of 1 or -1 means each variable could be completely predicted from the other; 0 means no relationship. A correlation matrix is a visual representation of all the pairwise correlations of a set of variables, allowing the reader to see at a glance which ones are strongly related to each-other.
In-scope staff	Staff of retail banks comprise Tellers, Sellers and their supervisors, near managers (Managers) and their equivalents in call centres.
N	Population size
n	Sample size
Non-financial rewards	Any tangible or intangible non-financial rewards. These include but are not limited to movie tickets, bottles of wine, time off or being shown at the top of a leaderboard or public recognition of your contribution; or they could be for your team, such as team lunches or not paying for drinks after work.
Regression	A statistical modelling and inference method that allows one variable (“the response”) to be explained by a combination of others (“explanatory variables”). The relationship of each explanatory variable with the response can be interpreted as “after adjusting for the other variables”.
Remuneration review working group	A working group consisting of ABA staff and representatives from the 18 banks participating in the review. The banks are; CBA, Westpac Group, NAB, ANZ, Bendigo and Adelaide Bank, BOQ, Suncorp, Rabobank Australia, HSBC, Bank Australia, MyState Bank, Macquarie Bank, Citibank Australia, Bank of Sydney, ME Bank, ING Bank Australia, AMP and Arab Bank Australia.
Variable remuneration	A proportion of staff’s pay which changes depending on the staff, or the staff’s group’s, performance. This is usually referred to as a bonus, short-term incentive, group performance dividend, profit share or commission.
Weights, or grossing-up weights	Weighting given to each respondent in a survey such that total weights match total numbers in a population by different variables e.g. gender and age group. The weights indicate how many people in the population each sample respondent represents and allow inference to focus on the overall population (controlling for non-response and other sampling bias) rather than just the sample.

Overview

In late February and early March 2021[80], the employees, contractors and franchisees of 18 Australian banks with retail operations were invited to complete a survey of remuneration and incentive practices in their workplace. The purpose of the survey was to inform the effectiveness of the implementation of the 2017 recommendations by determining the extent to which a culture of 'sales' existed in the banks. The survey was developed by the Remuneration Review working group with input on drafts and sign off from Steve Sedgwick. The population for the survey was defined as customer-facing sellers and their line of management.

Around 37,000 staff are estimated to be in-scope, and 13,760 effective[81] responses were received, a respectable response rate of 37 percent. Responses were weighted by age, gender and bank to adjust for any non-response bias and ensure inferences and estimates in this report can relate to the in-scope population as a whole, not just the sample.

Most (69 percent) in-scope employees and contractors have a potential variable pay component. Managers are more likely to have variable remuneration than other staff. The largest role-group, "Teller or Customer Service", has the lowest proportion receiving variable remuneration. Of the staff with a potential variable pay component, **64 percent are estimated to see at least one of sales, revenue or customer acquisition as driving variable remuneration.**

An indicator of the perceived customer-centricity of the workplace was estimated for each respondent, drawing on their agreement or disagreement with a range of questions about process, behaviour and systems in the bank in which they work (details in the section *What is valued in your workplace*). **The industry has an average perceived customer-centricity score of 0.6, from a possible range of -2 to +2. The score indicates the industry is perceived to be more customer-centric than sales-centric. All banks except one achieved an average positive perception by their own staff of perceived customer-centricity**. While positive, all banks also have room to improve their customer-centricity in the eyes of their staff.

A higher perception of customer-centricity is held by managers; relatively new staff; those who received variable remuneration; and those who work in transactions and deposits. Staff who perceive their workplace as not customer-centric are more likely to be those who see variable remuneration as driven by sales, revenue or customer acquisition; those in workplaces with no variable remuneration or who did not receive such remuneration themselves; and those in selling roles.

A key interpretation of the above is that **being in a workplace that offers variable remuneration is a positive for staff's perception of their bank's customer-centricity, but only if the variable remuneration is not seen to be driven by sales, revenue, customer acquisition or arbitrary discretion.**

The aspects of customer-centricity on which bank staff rated lowest are "I generally know who in my team is making the most sales and who is making the least" which has a score of -0.5 and "My career progression in the bank depends mostly on my sales results" which has a score of -0.1. High levels of agreement with

[80] Survey was open between 15th February and 5th March 2021. Survey launching time for the banks varied but each bank had approximately two weeks to complete the survey.
[81] Effective responses exclude responses from staff who are not in-scope, i.e. staff who do not work with customers and they do not manage – or manage someone who manages – staff who work with customers. Responses that were so incomplete that these questions about customers were not answered are also excluded.

these statements suggests an orientation towards sales as a constant benchmark in employee and contractor experience.

The aspects of customer-centricity which bank staff rated most positively were “My manager shows by their behaviour that the customer is at the heart of all decisions” which has a score of 1.3 and “Where staff have made sales that do not seem likely to result in a good outcome for the customer, I have seen my manager respond with appropriate actions” which has a score of 1.1. “I generally know who in my team is doing a good job in servicing the needs of customers” had a high score of 1.2 but was not well correlated with other statements and so was excluded from the constructed customer-centricity variable.

Overall, the survey offers a useful insight into the state of remuneration practices and their relationship to employee and contractor perceptions of the customer-centricity of their workplace. The findings are essentially positive, while identifying some areas for potential improvement, that can be considered as part of the broader effort of reviewing the implementation of the 2017 Review.

Survey demographics

A total of 13,760 staff have responded to the survey, averaging a 37 percent response rate. This section focuses on aggregated analysis of the demographics. This includes:

- Comparison of banks' number of relevant staff to sample size - Figure 7; and
- Response rates by age and gender - Figure 8.

Figure 7 | Response rates were good, averaging over 35 percent across the sector.

Key insights

- The larger the number of in-scope employees and contractors, the larger the effective sample (shown by the positive slope of the dots).

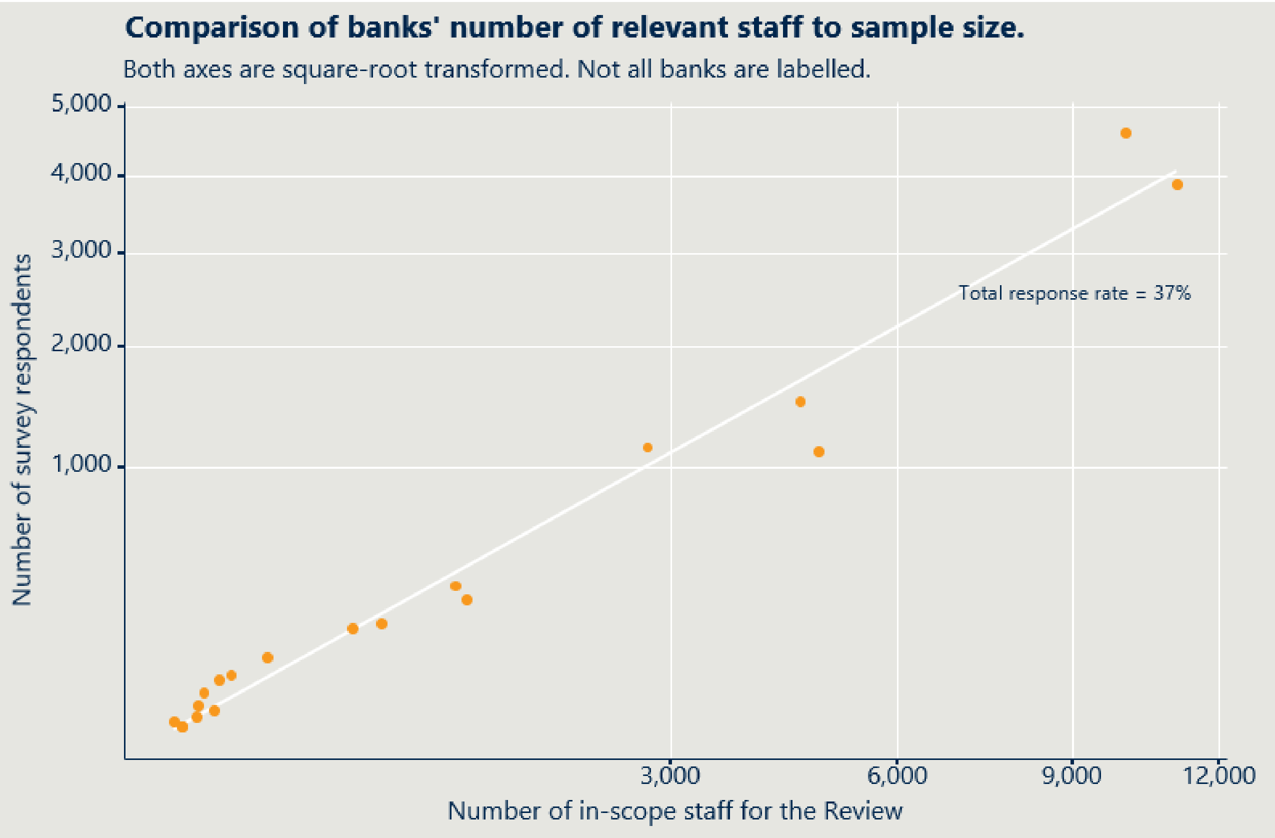
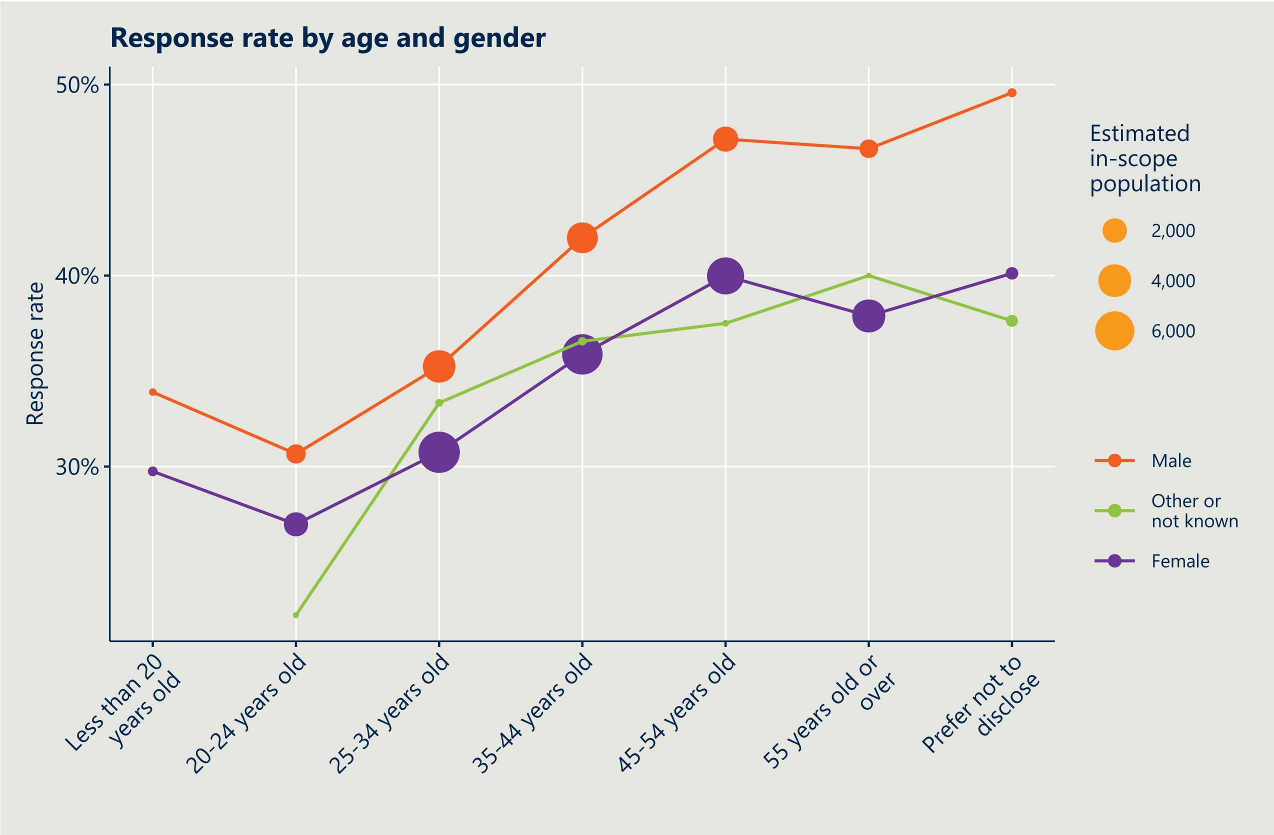


Figure 8 | A higher proportion of men responded than women, at all ages.

Key insights:

- More women (purple dots) than men (orange dots) are in-scope for the survey – approximately two thirds of in-scope staff are female;
- Response rates are generally higher for older people, and lowest for those under 25 years old;
- Response rates were higher for men than women – which is unusual in surveys in general; and
- Overall, the response rate of 37 percent was satisfactory for a survey of this sort.



Staff perception of what is valued in the workplace

This section includes analysis of staff perception of what is valued in the workplace in the below three sub-sections.

- Summary of perceived customer-centricity;
- Regression analysis to determine which factors matter and how much; and
- The components of perceived customer-centricity.

Summary of perceived customer-centricity

The perceived customer-centricity value is a simplified representation of the responses to 'what is valued at your workplace' statements. The value is an arithmetic average[82] of scores assigned to each response, accounting for the type of questions – whether they are sales-centric or customer-centric statements:

- **2** Strongly agree on customer-centric questions or strongly disagree on sales-centric questions;
- **1** Agree on customer-centric questions or disagree on sales-centric questions;
- **0** Neither agree nor disagree on any questions;
- **-1** Disagree on customer-centric questions or agree on sales-centric questions; and
- **-2** Strongly disagree on customer-centric questions or strongly agree on sales-centric questions.

The higher the score, the stronger indication that the staff perceive the workplace to be customer-centric. The method is reliable according to statistical checks which are described further in the section *Explanation of the single numeric summary.*

The average value of the aggregated responses is approximately 0.6 which indicates the banks are more customer-centric than sales-centric. This sub-section examines customer-centricity by looking at various factors that are likely to influence it. These factors are:

- Key demographics, i.e. gender and age – Figure 9;
- Roles - Figure 10;
- Time with the bank - Figure 11;
- Primary products that the staff work with - Figure 12;
- Type of customers that the staff work with - Figure 13;
- Mode of engagement between staff and customers - Figure 14;
- Whether the staff receive variable remuneration - Figure 15;
- What factors determine variable remuneration - Figure 16;
- Whether the staff receive non-financial rewards - Figure 17; and
- Individual banks - Figure 18.

[82] There are a total of 16 statements in the survey. However, one statement - I generally know who in my team is doing a good job in servicing the needs of customers - is dropped from the calculation based on the correlation and reliability analysis. More details on the method are included in Appendix C – Explanation of the single numeric summary.

What the figures mean:

The figures in this section are boxplots that present the perceived customer-centricity (x-axis) by the factors (y-axis) listed above. The higher the score, the stronger indication that the staff perceive the workplace to be customer-centric. The next section examines the statistical significance of select factors – which matters most and how much. When the commentary in in this section observes a difference between different groups' ratings of customer-centricity, this is because the analysis outlined in the next section had found statistically significant evidence in this case.

How to read the figures in this sub-section

- Percentages in the vertical axis labels (e.g. "20-24 years old (8 percent)") are estimates of the proportion of the population in each category;
- The vertical lines in the boxes are the median value;
- The white boxes are bounded by the first and third quartiles (the 25th and 75th percentiles). The middle 50 percent of the data are within that box. The sizes of the boxes are determined by the range of values in the relevant subset of the population; smaller boxes mean the population is more tightly clustered around a set of values; and
- The dots at the left-hand side of the chart area are outliers which are defined as individual respondents who gave values outside 1.5 x the inter-quartile range. There are no outliers to the right because enough respondents scored a perfect '2' that these values are considered unremarkable within the distribution of the data, rather than outliers.

Figure 9 | There is no material variation in perceived customer-centricity by gender and age.

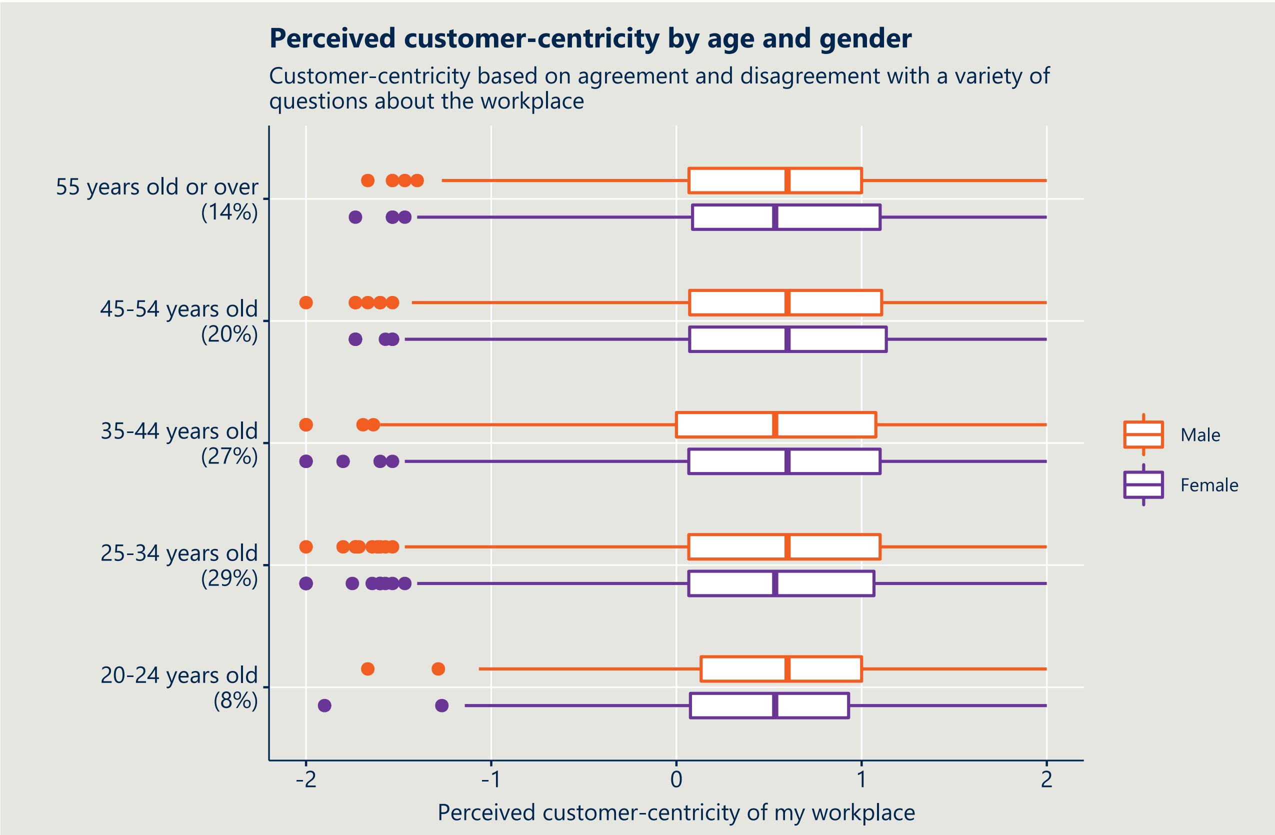


Figure 10 | There is variation in perceived customer-centricity between roles; managers tend to see the workplace as more customer-centric than those in other roles.

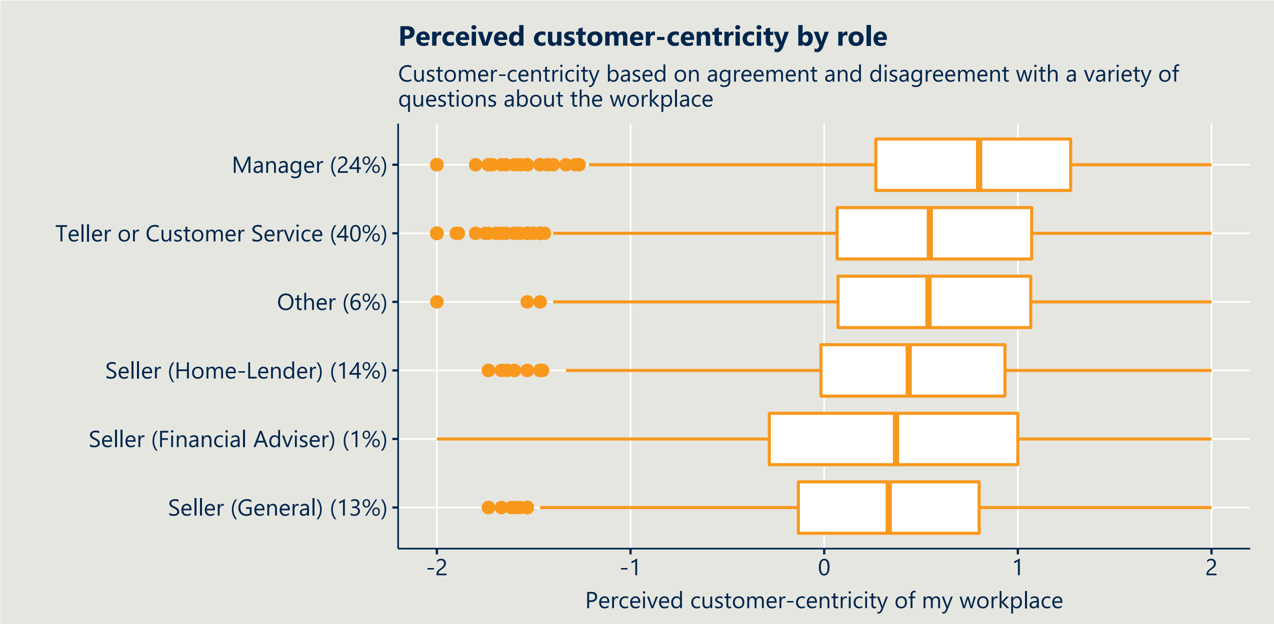


Figure 11 | Recent starters are more positive about customer-centricity in their workplace than those who have been longer at the bank.

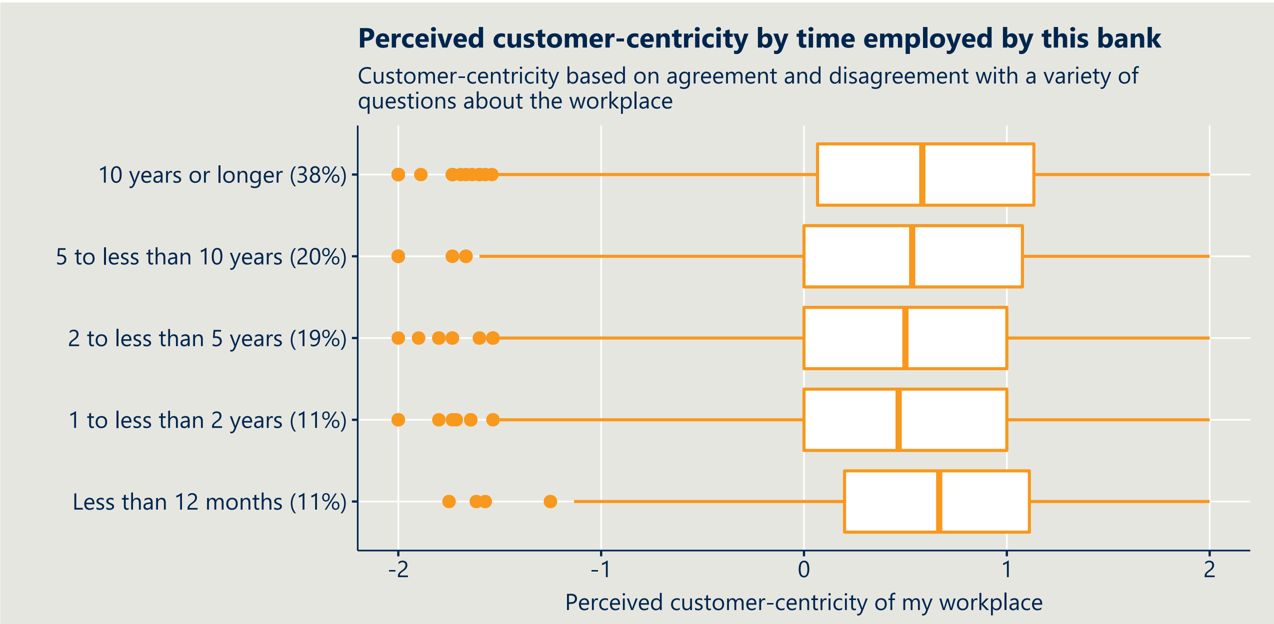


Figure 12 | There is some variation in perception of customer-centricity across the primary products staff work with (Multiple responses question).

Key insights:

- In-scope employees and contractors who work with superannuation, investment, wealth and financial planning related products have the lowest perception of customer-centricity in their workplace. This is consistent with the Seller (Financial Adviser) value in Figure 10; and
- 'Transactions and deposits' is the most common product grouping that in-scope staff work with, with 29,200 such staff, 78 percent of the population.

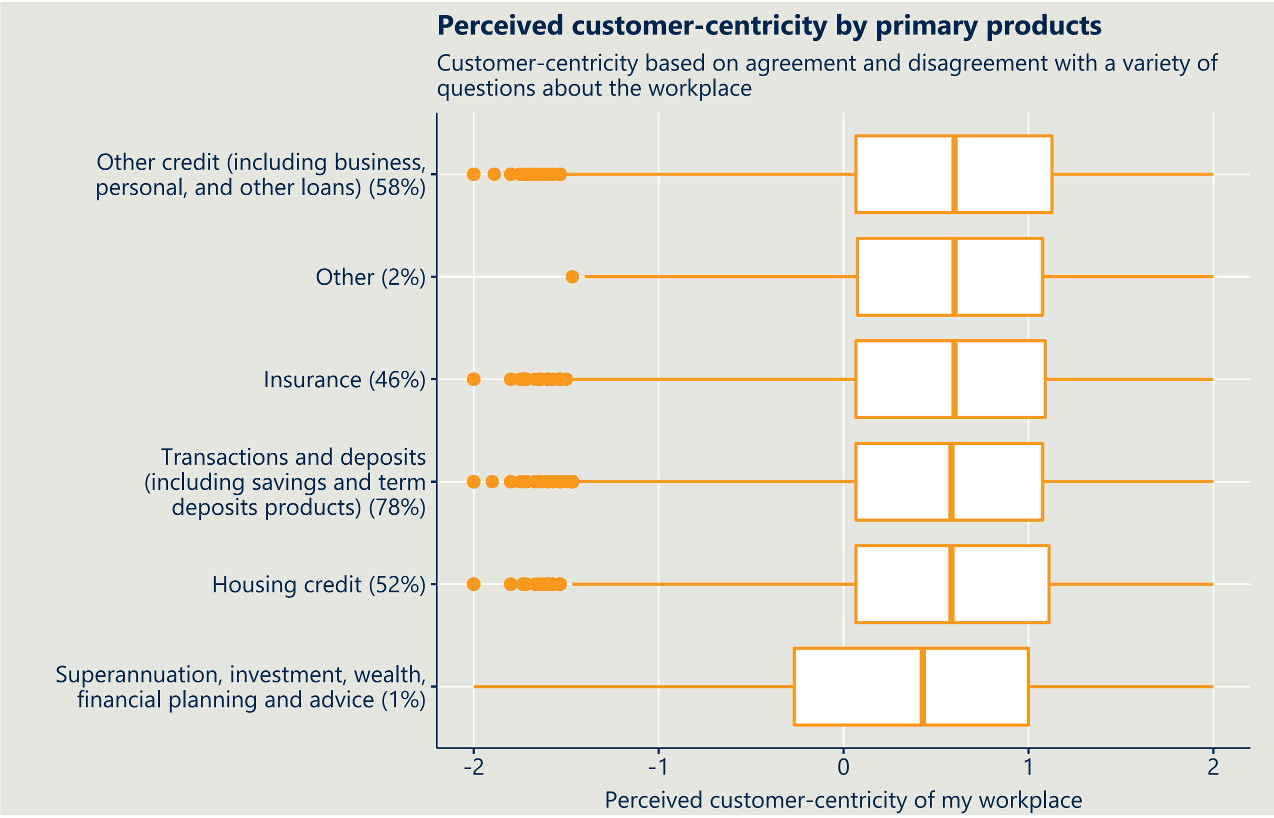


Figure 13 | The evidence that perceptions of customer-centricity vary by customer type is not statistically significant (multiple responses question).

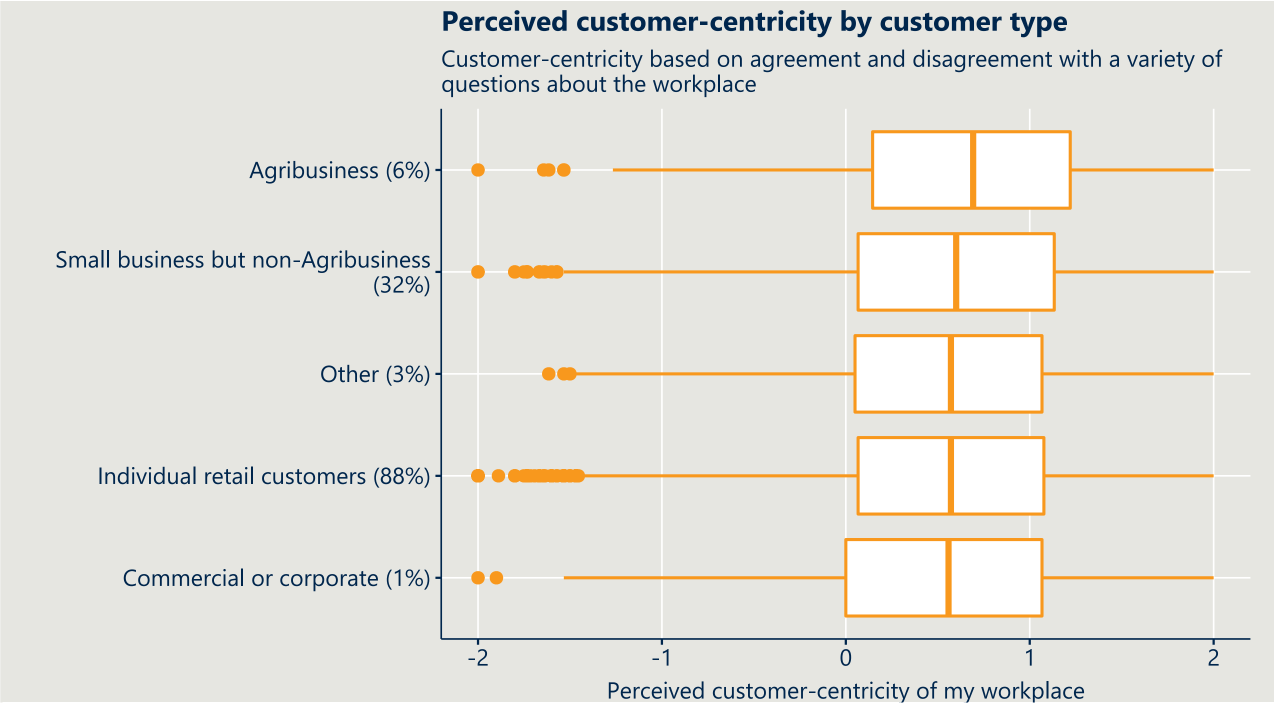


Figure 14 | There is little or no apparent variation in perceived customer-centricity between modes of engagement (multiple responses question).

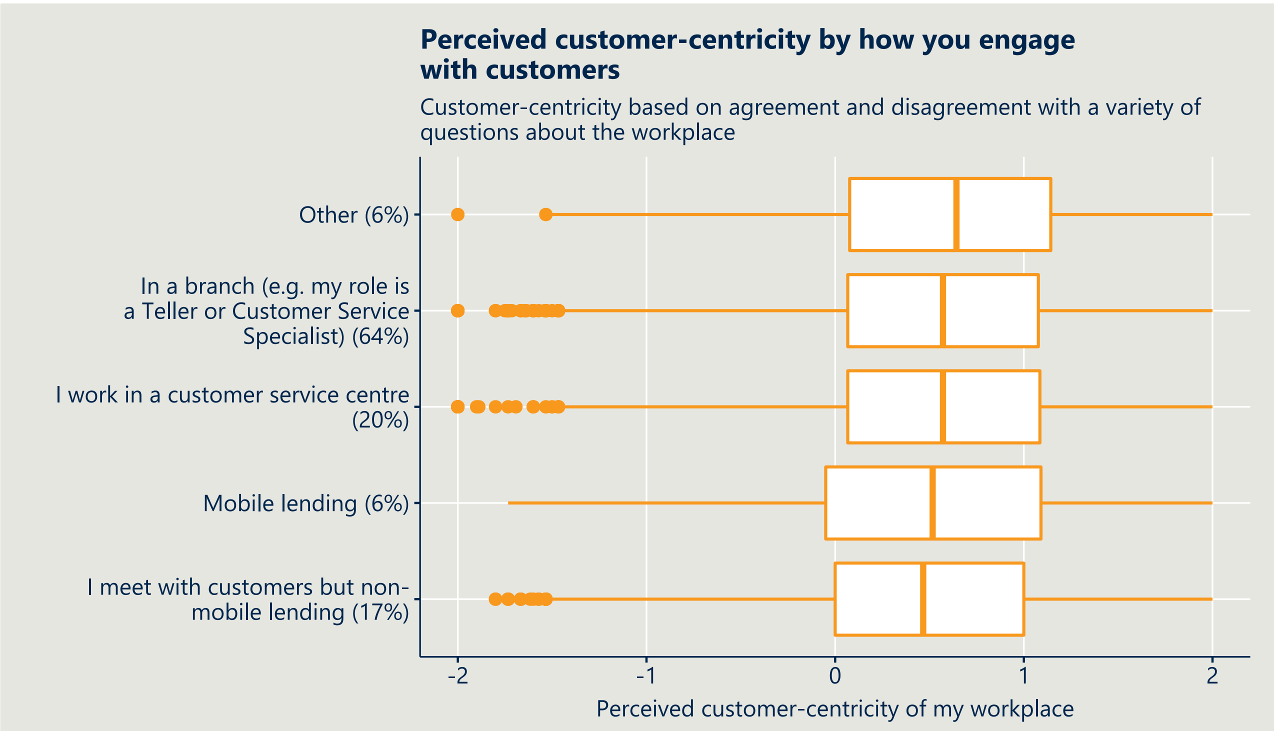
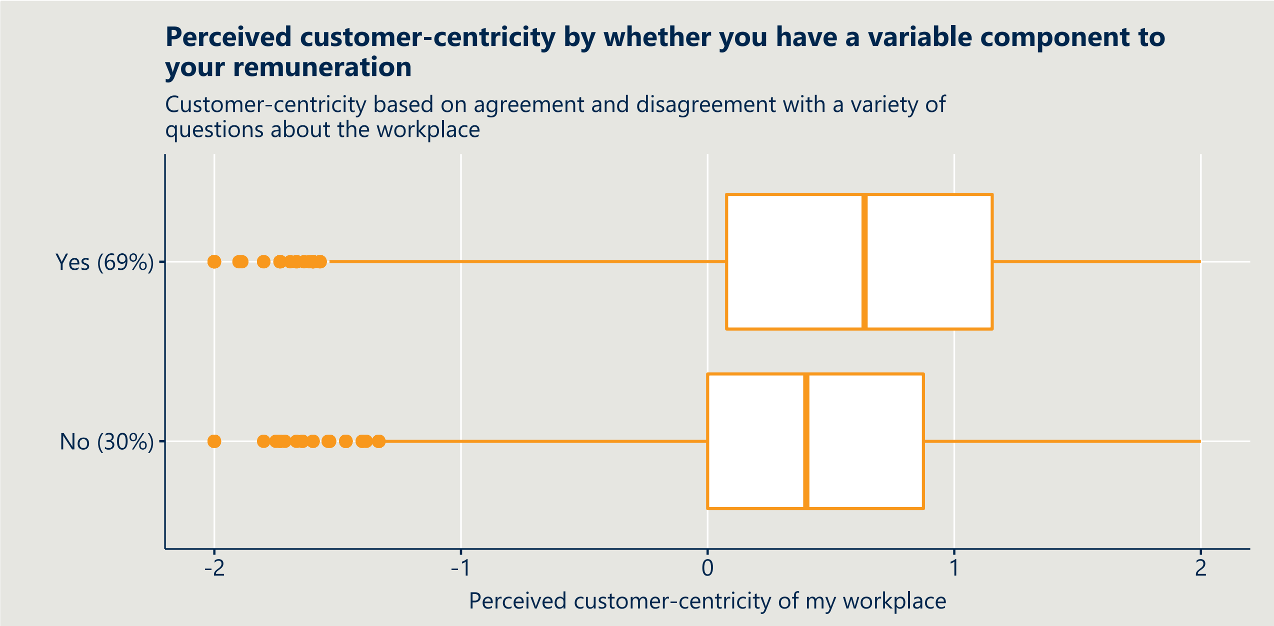


Figure 15 | Staff who are eligible for variable remuneration are slightly more positive about customer-centricity in their workplace[83]

Key insights:

- 69 percent of the in-scope staff have a variable component (such as a bonus scheme) as part of their remuneration (noting that this number includes some who are eligible for variable remuneration but did not receive it); and
- Employees and contractors with a variable component to their pay package are more positive in their perception of the workplace's customer-centricity than are those who do not. The difference is statistically significant according to the analysis in Figure 19.



[83] Noting in the chart the percentages do not add up to 100 percent due to rounding.

Figure 16 | Among staff who are eligible for variable remuneration, there is some variation in perception of customer-centricity related to factors – that the staff think – determining it (Multiple responses question).

Key insights:

- Seeing variable remuneration as driven by meeting customer targets, business targets and customer acquisition correlates with lower perceived customer-centricity, as does being in a workplace that does not offer variable remuneration;
- In total (removing duplicates), 16,700 staff are estimated to see variable remuneration as driven by at least one of customer acquisition, revenue targets or sales targets. This is 44 percent of all in-scope staff, and 64 percent of staff eligible for variable remuneration; and
- Staff who see people leadership, risk management, customer service and values as driving variable remuneration are more likely to perceive their workplace as customer-centric.

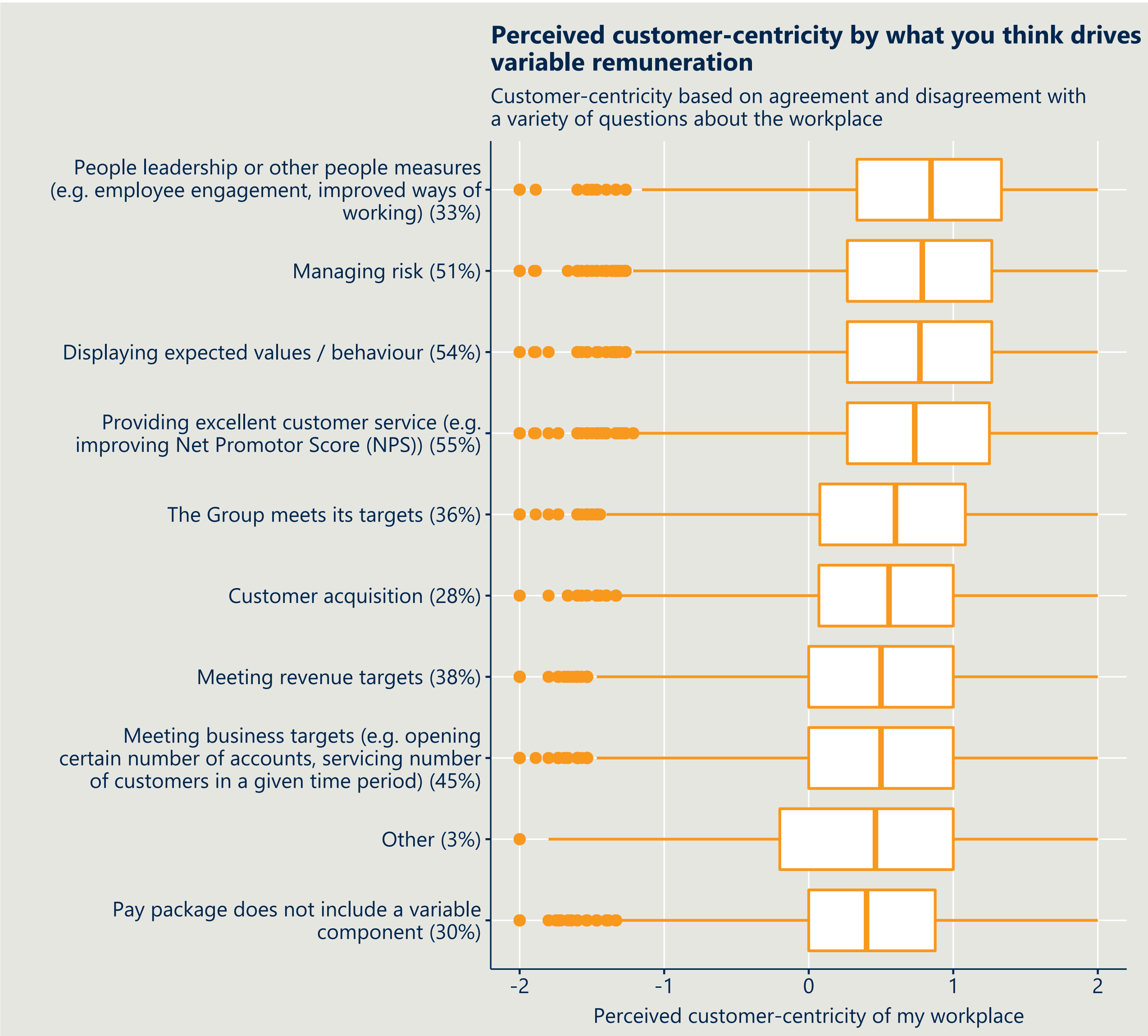


Figure 17 | There is some variation in perception of customer-centricity based on whether and how often staff receive non-financial rewards

Key insights:

- Among staff whose workplace provides non-financial rewards, those who receive non-financial rewards have higher perceptions of customer-centricity in their workplace than those who do not; and
- Based on the survey, a significant majority (60 percent) is estimated to think their workplace does not provide those non-financial rewards.

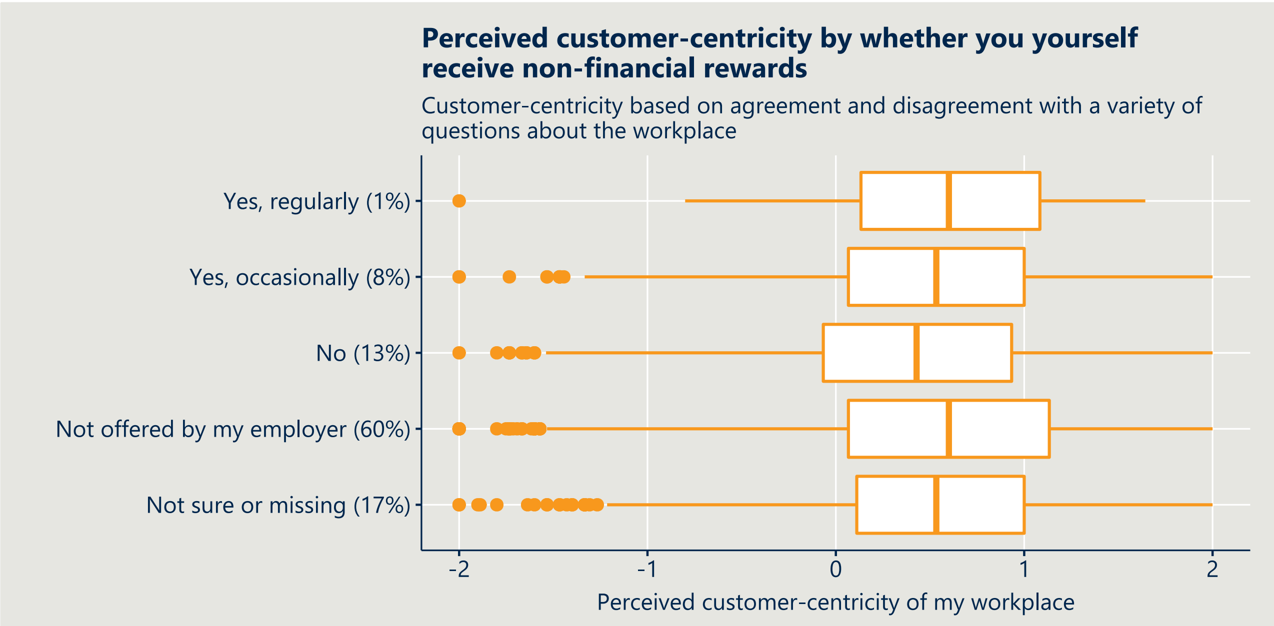


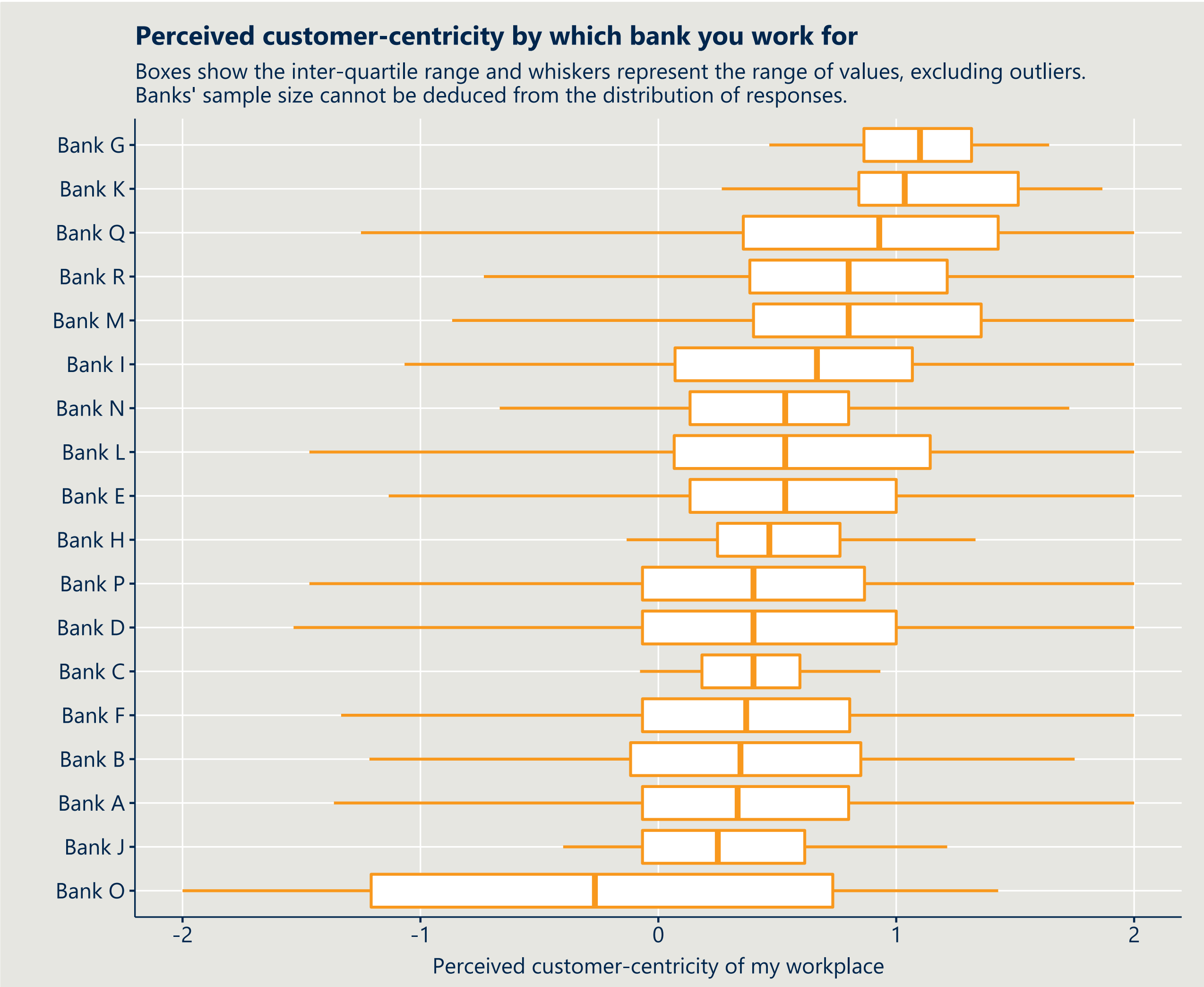
Figure 18 | Staff perception of customer-centricity varies materially across banks.

Key insights:

- All banks except one have a median staff perception of customer-centricity that is positive (vertical line in the white box is to the right of the "0" line);
- For most banks, three quarters of their staff have positive perceptions of customer-centricity (the white box with the central 50 percent of staff is to the right of the "0" line); and
- Most banks have a number of staff who clearly do not see the workplace as customer-centric, suggesting room for improvement in one or more of processes, systems, behaviours or communication.

Interpretive notes

18 random letters (A-R) are assigned to the 18 banks that participated the survey. The assignment is consistent across the diagrams in this report.



Regression analysis to determine which factors matter and how much

Regression analysis can help identify which factors are related to perceived customer-centricity and to what extent. The analysis answers the questions: Which factors matter most when we adjust for the presence of the others? Which matter less? And how uncertain are we about these effects – is there good evidence that they would reproduce if we repeated the survey, or could the apparent relationships be statistical noise and the luck of the sampling process? The analysis has two purposes in this report: first is to confirm the variables we looked at in the previous section have solid statistical evidence of a relationship; and second is to look at all the factors and their impact at a glance while controlling for each-other.

Results are presented in two figures – effect of individual factors (Figure 19) separately from the bank's individual effects (Figure 20).

The factors that matter most are: **what you think determines variable remuneration, whether you get a variable component, time worked for the bank, your role, and the bank you are in.** They all have significant evidence of a relationship with perceived customer-centricity.

The factors that matter less are: **age, gender, products, whether staff received non-financial rewards, employment type (permanent, casual or fixed), relationship to the bank (employee, contractor or work in a franchise).** They have no significant evidence of a relationship with perceived customer-centricity.

Two alternative specifications of this model are explored in the section *Alternative specifications of regression*. Overall, the analysis supports the conclusion that **variable remuneration can actually help perceptions of customer centricity of the workplace, but only if the right things are seen to drive variable remuneration: displaying the expected values, providing excellent customer service, managing risk, and people leadership.**

What the figures mean:

The figures in this section look at impact of various factors on perception of customer-centricity in the workplace. The figures use a 'typical' employee from the survey (described in the subtitle of the figure) as a reference. Generally, the further a value deviates from the contrast, the larger impact the factor has. If a bar (95 percent confidence interval) does not overlap with the reference line then there is statistically significant evidence of a relationship between a factor and perceived customer-centricity.

How to read the figures in this section:

1. The vertical grey line represents the reference level of the 'typical' employee or contractor; and
2. Width of the horizontal bars represents the 95 percent confidence interval, i.e. repeating this approach to data collection and analysis many times, 95 percent of the time the bar range would include the true effect size. The narrower the bar is the more confidence we have in the precision of the results. The most material driver of this is sample size; for example, the bar for the effect of being "under 20 years old" is relatively wide because relatively few of the population and sample are that young.

Figure 19 | Various factors correlate (positively or negatively in contrast with an 'average' employee) with perceived customer-centricity of the workplace.

Key insights:

- The factors that matter most are: 'what you think determines variable remuneration', 'whether you get a variable component', 'time worked for the bank', and your role; and
- Staff who worked more than 1 year with the bank perceive their workplace as less customer-centric than staff who worked less than 12 months (the contrast line).

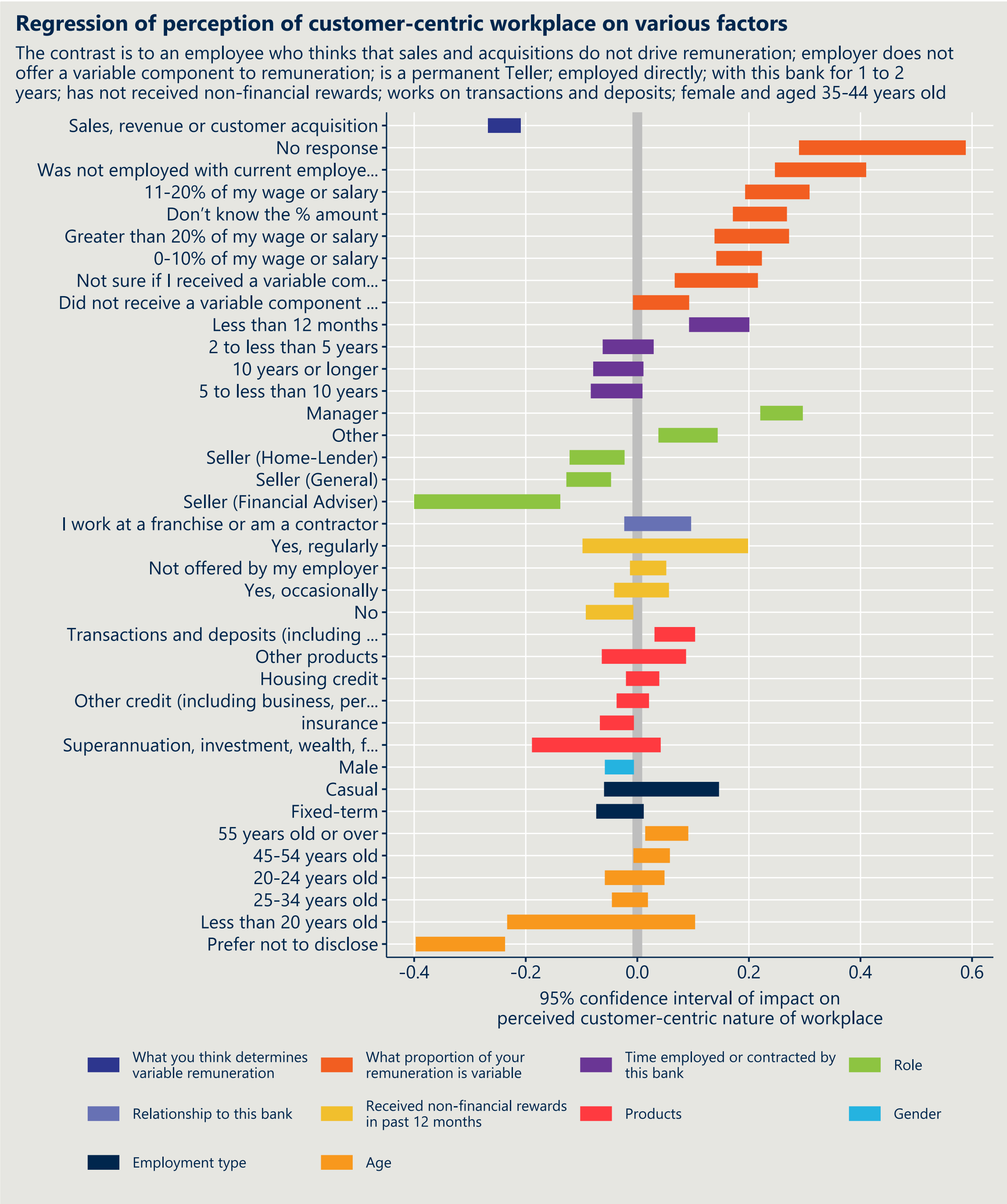
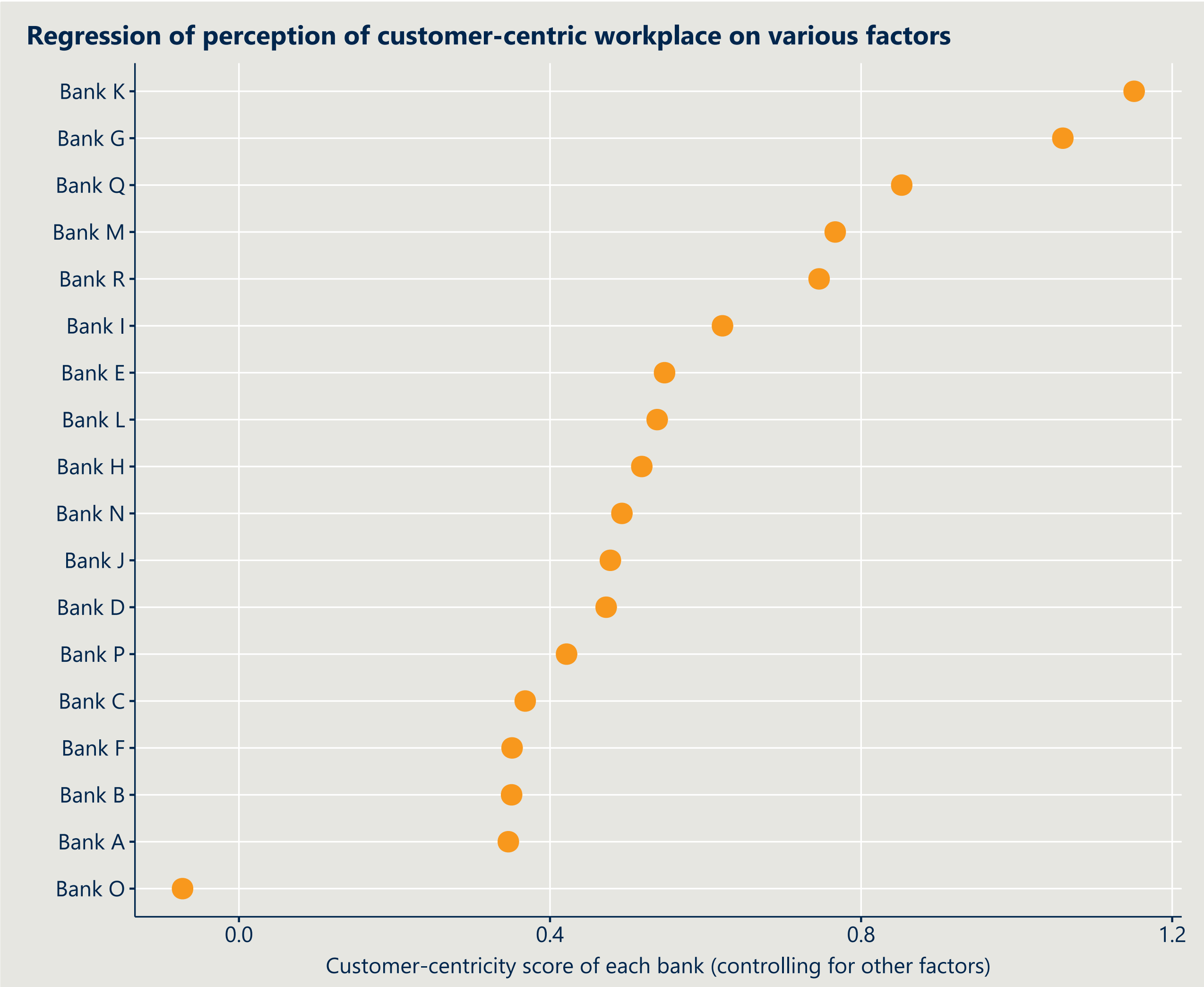


Figure 20 | There is variation and some uncertainty in perceived customer-centricity in each bank, but nearly all banks have a positive score on average.

Key insights:

The ordering of the banks is similar to that in Figure 18, but where that earlier figure showed the distribution of individual employee and contractor scores within the banks, the figure below shows the average score for perceived customer-centricity in each bank, after controlling for factors such as the product, role and age mix in the bank. Confidence intervals are not shown to avoid re-identification of individual banks.



The components of perceived customer-centricity

This sub-section goes beyond the single numeric summary of perceived customer-centricity to the original individual statements about the workplace survey respondents were asked to agree or disagree with. It provides analysis of the original questions using diverging stacked bar charts. These show responses for each of the 'what is valued at your workplace' statements in part 2 of the survey. The analysis includes:

- Aggregated responses from all banks – Figure 21;

- Breakdown of responses by roles -

- Figure 22;
- Breakdown of responses by whether staff is eligible for variable renumeration - Figure 23;
- Breakdown of responses by whether variable renumeration includes revenue, sales or customer; and acquisition targets – Figure 24.

What do the diverging stacked bar charts mean:

The charts illustrate the level of agreement on each of the 'what is valued at your workplace' statements, ranked by how positive the responses are, i.e. questions showing more positive agreement on customer-centricity are ranked higher.

How to read the charts:

There are total of 16 questions ranked below. Questions that are framed in a positive way towards customer-centricity are coloured purple in the figures in this section; the questions in red are those that are framed in a sales-centric way. 'Neutral' or 'Neither agree or disagree' responses are plotted at the centre which represents 0 percent agreement or disagreement.

The full questions are listed below– questions are also repeated in the charts but some of them are shortened for readability.

1. I generally know who in my team is doing a good job in servicing the needs of customers;
2. My manager shows by their behaviour that the customer is at the heart of all decisions;
3. If I inform a customer about the potential unsuitability of a product they are considering, this is viewed positively by my team leader or manager;
4. Where staff have made sales that do not seem likely to result in a good outcome for the customer, I have seen my manager respond with appropriate actions e.g. managing the performance or behaviour of the staff member, teaching the staff member how to better serve the customer or implementing appropriate training;
5. I am encouraged by my team leader, manager or senior leaders to proactively tell a customer, at the point of sale, if a product is unsuitable;
6. I have seen a shift in my bank leading to a stronger focus on the customer over the past few years;
7. I have seen my colleagues put making sales above customers' interest;
8. I feel pressured to make sales, to the detriment of customer outcomes;
9. If a leaderboard is used, sales are balanced with other measures such as customer, risk or people measures;
10. My team uses a 'leaderboard' of some sort showing which individual is making the most sales and which individual is making the least;
11. I think my manager is pressured by their own line manager to increase sales, to the detriment of customer outcomes;
12. I feel that the sales I make are only a relatively small component (i.e. 33 percent or less) of the way my performance is assessed;

13. I feel that I am assessed by whether or not I make sales targets, irrespective of how I achieve those sales target;
14. I believe that my manager's assessment of my referral performance is based largely on whether my referrals result in sales;
15. My career progression in the bank depends mostly on my sales results; and
16. I generally know who in my team is making the most sales and who is making the least.

Figure 21 | Levels of agreement vary across the questions at the industry level.

Key insights:

- Staff respond with stronger agreement than disagreement on all perceived customer-centric practices in their workplace and stronger disagreement than agreement on most sales-centric practices;
- Some sales-centric practices, e.g. leaderboards are used, sales are often balanced with other measures such as customer, risk or people measures;
- Responses to the last four questions in the figure show that staff perceive sales pressure. The aspects of perceived customer-centricity on which bank staff felt most questionable are "I generally know who in my team is making the most sales and who is making the least" and "My career progression in the bank depends mostly on my sales results"; and
- The aspects of perceived customer-centricity on which bank staff felt most positive were "I generally know who in my team is doing a good job in servicing the needs of customers", "My manager shows by their behaviour that the customer is at the heart of all decisions" and "If I inform a customer about the potential unsuitability of a product they are considering, this is viewed positively by my team leader or manager".

Levels of agreement with components of the customer-centricity perception scale

From most to least agreed (all banks) with each statement. Some items have been reversed in accordance with their orientation relative to perceived customer-centricity.

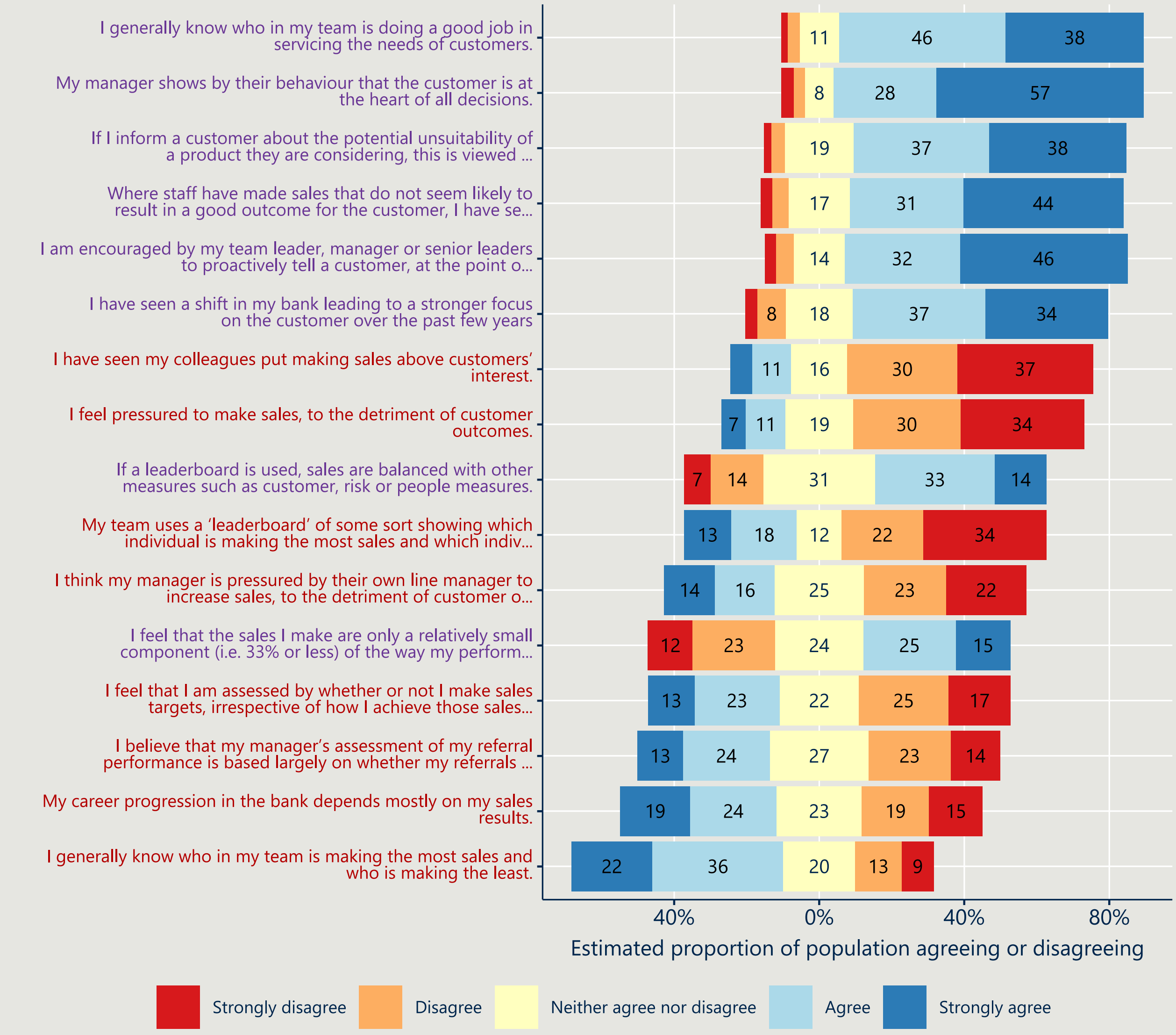


Figure 22 | The 'shape' of responses by roles generally aligns with the aggregated responses (Figure 15).

Key insights:

- There is little visually apparent difference in the shape among the roles – even though the perceived customer-centricity value (Figure 10) for them did show a difference when summarised as a single number; and
- Sellers report higher disagreement than other roles with the statement about sales forming a small component of performance assessment.

Figure 23 | Comparison of components of the customer-centricity perception scale between staff who are eligible for variable remuneration and staff who are not.

Key insights:

Staff who have a variable pay component report more positively on perceived customer-centric practices - in general, a higher level of agreement on perceived customer-centric statement and higher level of disagreement on sales-centric statement - than staff without.

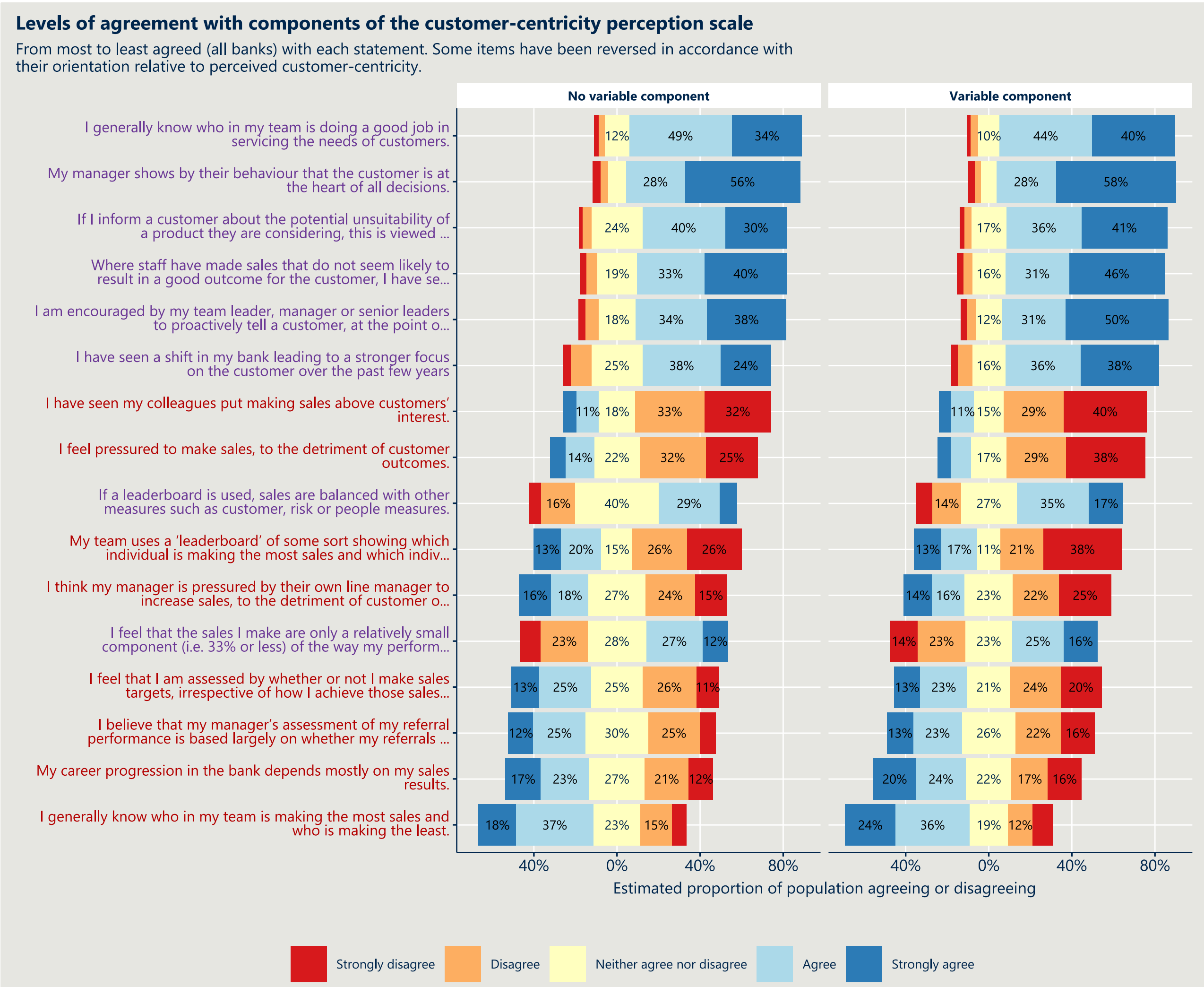
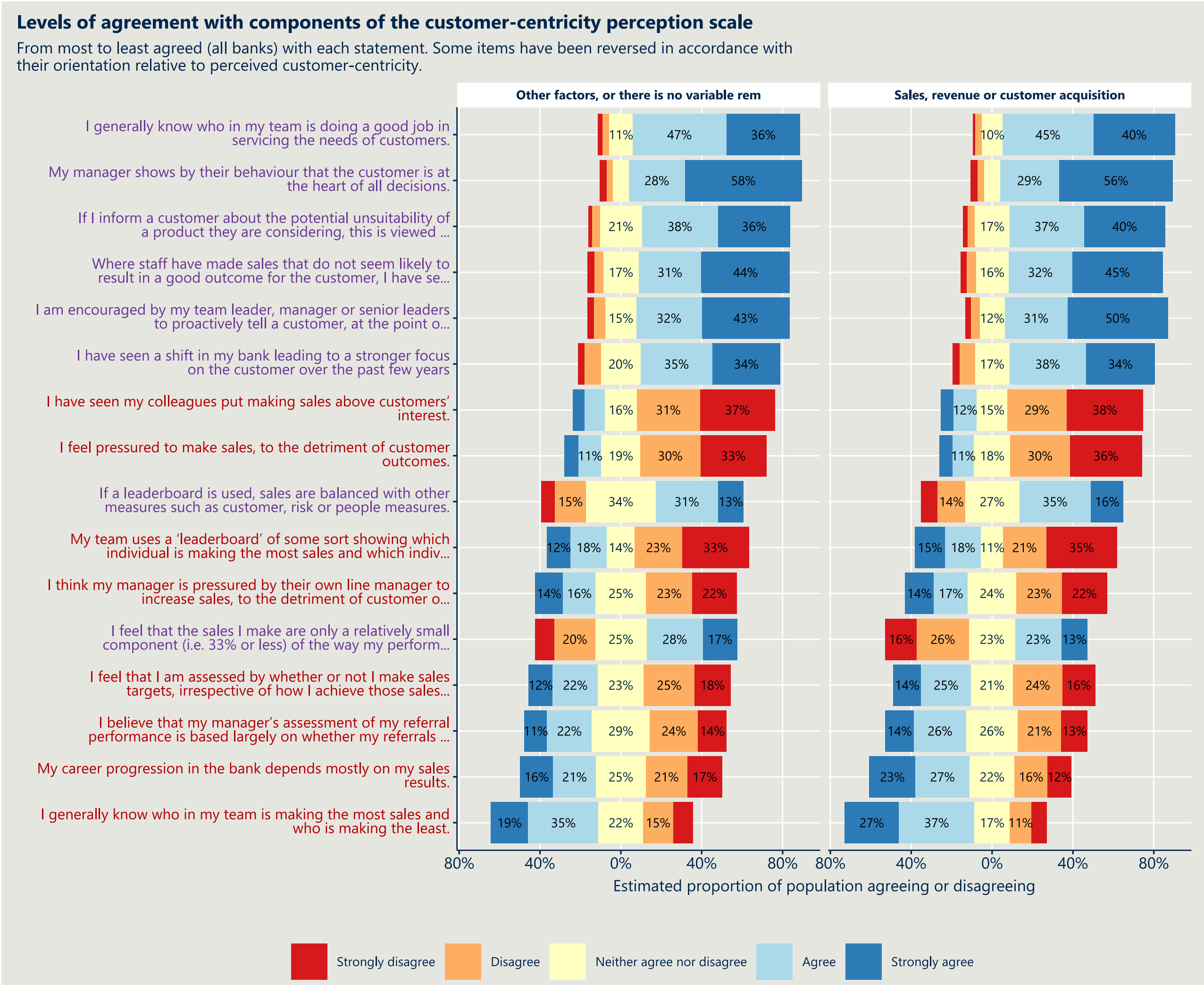


Figure 24 | Comparison of components of the customer-centricity perception scale between staff whose variable remuneration includes revenue or customer acquisition and staff whose variable remuneration does not include these or does not have variable remuneration.

Key insights:

There is no material variation in responses between the two groups.



Staff perceptions of how they are rewarded

This section analyses how employees and contractors report they are rewarded in terms of variable remuneration and non-financial rewards. The analysis intends to show the prevalence of variable remuneration and non-financial reward.

This section includes the following analysis:

- Prevalence of variable remuneration and how much is it as a proportion of total pay - Figure 25;
- Comparison of variable remuneration by managers and others - Figure 26;
- Variable remuneration for staff who could not provide the percentage amount - Figure 27;

- Proportion of staff receiving variable remuneration by roles - Figure 28;
- Factors determining variable remuneration - Figure 29; and
- Proportion of staff who report receiving non-financial rewards - Figure 30.

Figure 25 | Most of the in-scope staff surveyed have a variable pay component.

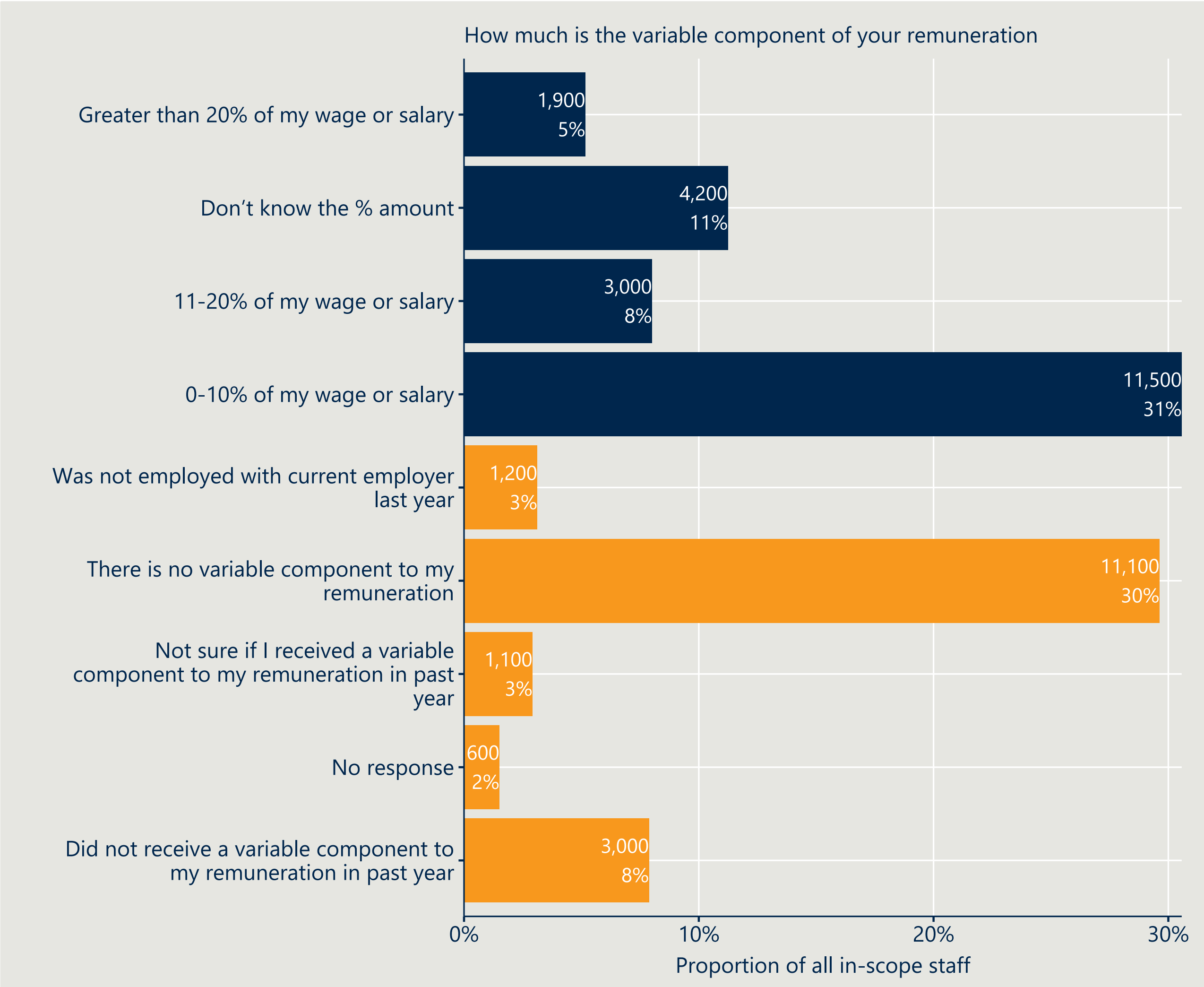


Figure 26 | Managers are more likely to have a variable component to their remuneration.

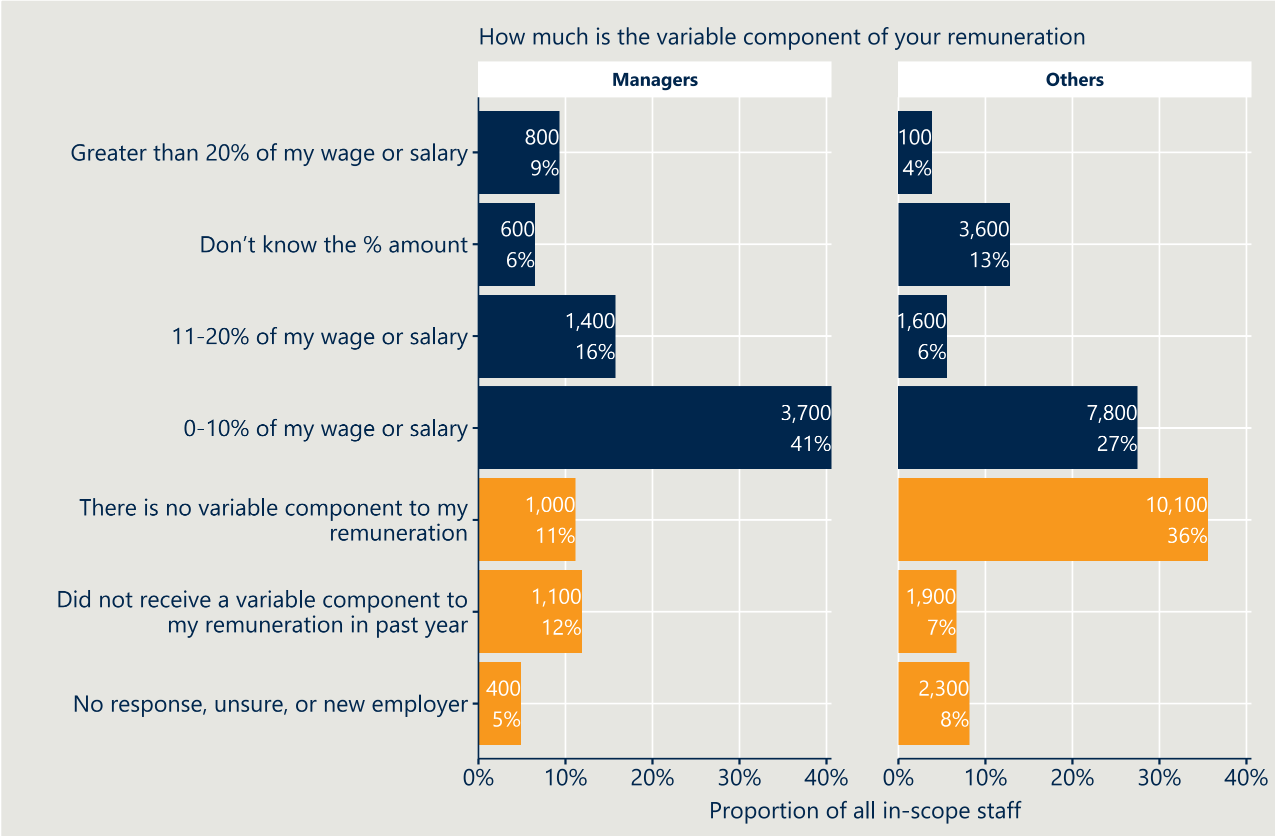


Figure 27 | Further analysis on staff who have variable pay but didn't provide a percentage amount.

Key insights

- Among those who could not provide a proportion of variable pay but could provide an absolute number, managers receive higher average variable pay than others; and
- Sample sizes (n) for manager and others who could not provide a proportion but could provide a number are small.

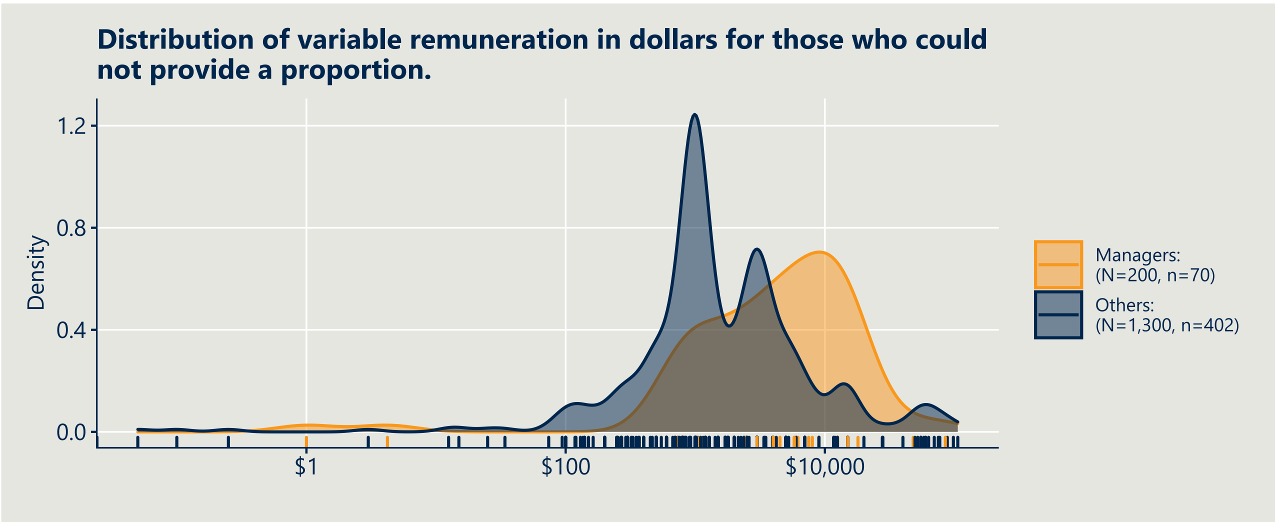


Figure 28 | More than 50 percent of staff in each of the roles have received a variable component in their last annual performance review.

Key insights:

- Tellers are the biggest group, but least likely to have variable remuneration; and
- Other than managers, home lenders are the most likely group to have variable remuneration.

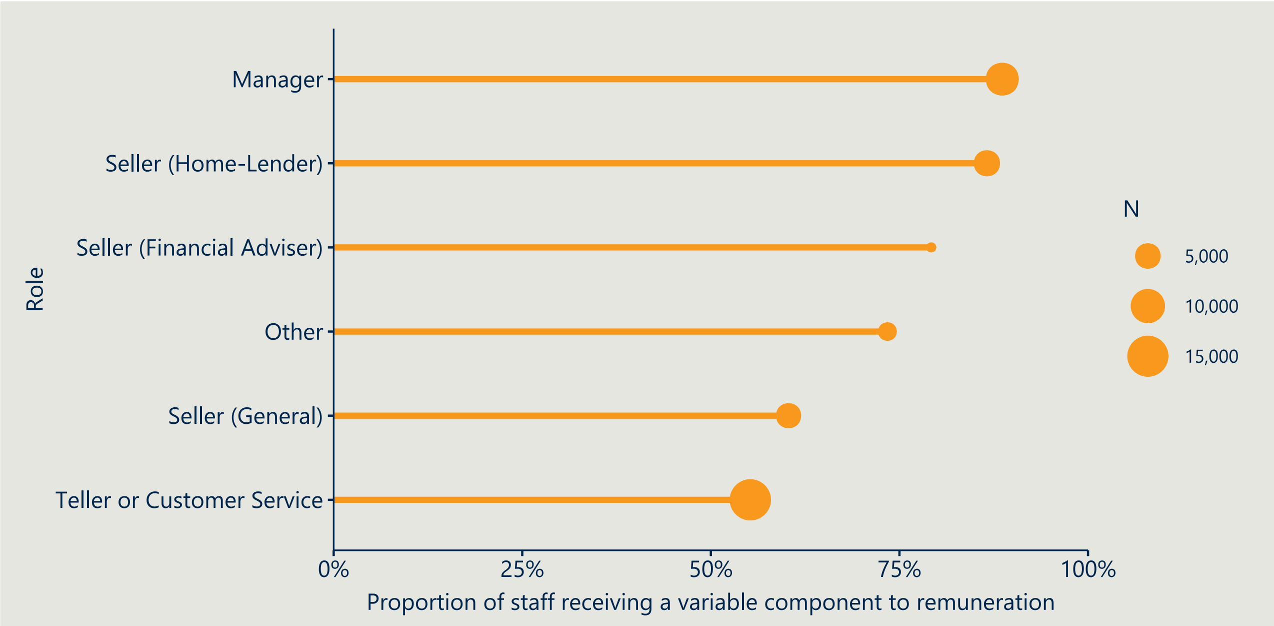


Figure 29 | Staff who are eligible for variable remuneration primarily see factors that aren't sales-oriented as determining (Multiple responses question).

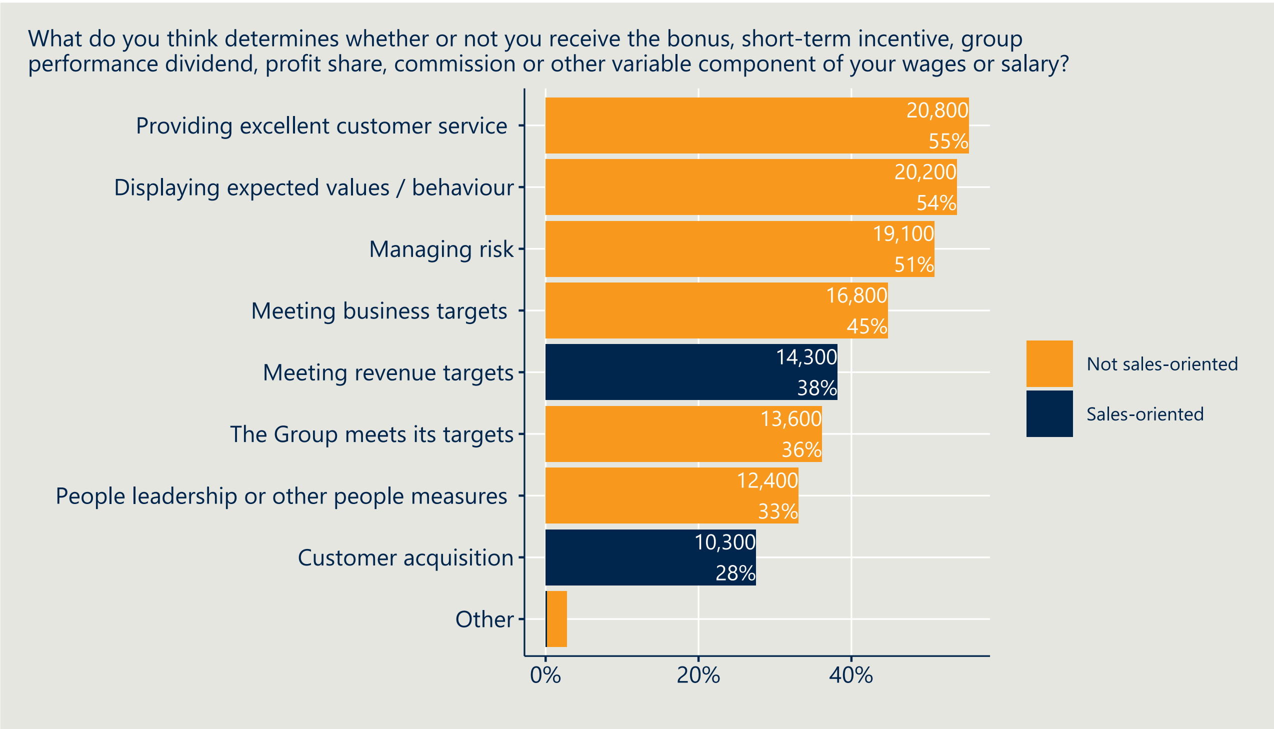
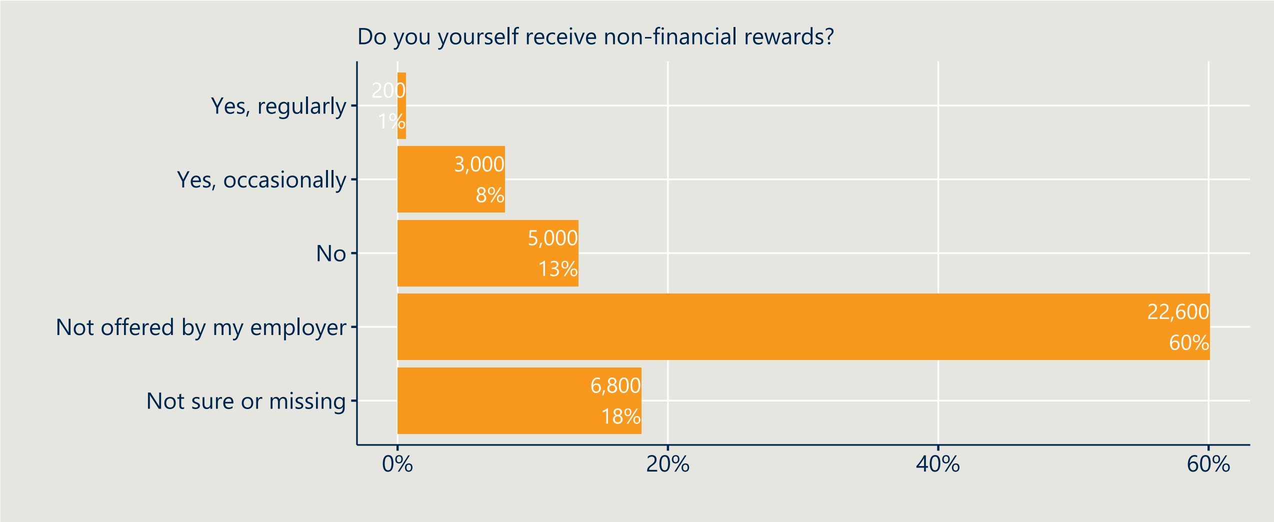


Figure 30 | Very few in-scope staff report receiving non-financial rewards.



Explanation of the single numeric summary

In the previous section, we introduced a one-dimensional numerical measure of the perceived 'customer-centricity' of respondents' workplaces. This steps to calculate the measure, for each respondent, are:

- Assign values of -2, -1, 0, 1 and 2 to "strongly disagree" through to "strongly agree" for each individual's response to each of 15 agree/disagree questions (all 16 original statements, other than "I generally know who in my team is doing a good job in servicing the needs of customers");
- Values are then reversed for some statements, so higher values always indicate "most customer-centric". The statements for which values were reversed are those coloured red in the diverging Likert scale charts in the previous section; and
- Each respondent is then given a simple unweighted average of the 15 statements, excluding any missing values. This average becomes their customer-centricity perception score and is the value used in the boxplots and the regression in the previous section.

We carefully considered three questions in the development of this measure:

- **Is it appropriate to convert original categories ("agree", "disagree", etc) to numbers (-1, 1, etc)?** Our experience shows that in batteries of questions of this sort where there is a natural symmetry and spacing to the response options, there is minimal if any distortion in converting the categories into numbers. A more sophisticated approach to analysis designed for use with ordinal categories – use of polychoric correlations – nearly always returns identical substantive conclusions, but loses significantly in explainability.
- **Is it appropriate to simply exclude unanswered questions from the scale, or should values be imputed, or cases excluded completely?** This matters most for statements such as the follow up on leaderboards ("If a leaderboard is used…") that was legitimately missing (as not relevant) for many respondents, and "neither agree nor disagree" (hence 0, contributing to the denominator but not the numerator of the simple average) for others. Further analysis of this point would be interesting, but time prevented a completely thorough investigation. On balance, leaving all cases in, not imputing values, and taking a simple average was judged to be an appropriate pragmatic approach.
- **Which if any variables should be omitted?** This is answered below.

- To help answer these questions, the next two figures investigate which of the statements relate to each other.

The analysis in Figure 31 is based upon examining the “distances” between questions (treating each question as a point in n-dimensional space, with the same numerical ratings used for each question that were used to create the perceived customer-centricity measure). A technique called “Divisive Analysis Clustering” (or DIANA)[84] is then used to create a “tree”, such that questions which are closely related to each other tend to be twigs at the endpoint of a common branch. The purpose is to visualise groupings between the questions to better understand which questions generate similar answering patterns to each-other.

The analysis in Figure 32 is a pairwise correlation matrix. It shows the correlation coefficient for each question with each other question. The purpose is an alternative, simpler visualisation of which questions have similar or different answering patterns.

The findings from this analysis are suggestive rather than conclusive.

[84] Maechler, M., Rousseeuw, P., Struyf, A., Hubert, M., Hornik, K.(2019). *cluster: Cluster Analysis Basics and Extensions*. R package version 2.1.0.

Figure 31 | Some of the 'what is valued at your workplace' statements are particularly closely related to each other.

Key insights

- The seven statements at the top of the chart (from "My team uses a leaderboard…" to "I believe that my managers assessment…") form a cluster of related questions that have similar answering patterns;
- The "If a leaderboard is used…" question does not closely relate to other groups, reflecting that many answers were "not applicable" or blank, and that this question provides additional nuance to the other leaderboard question;
- The bottom four questions about managers form another cluster of related statements; and
- The clustering's suggested by this analysis differ from those in Figure 32, suggesting these particular results (i.e. about clustering of statements together) should be interpreted with caution.

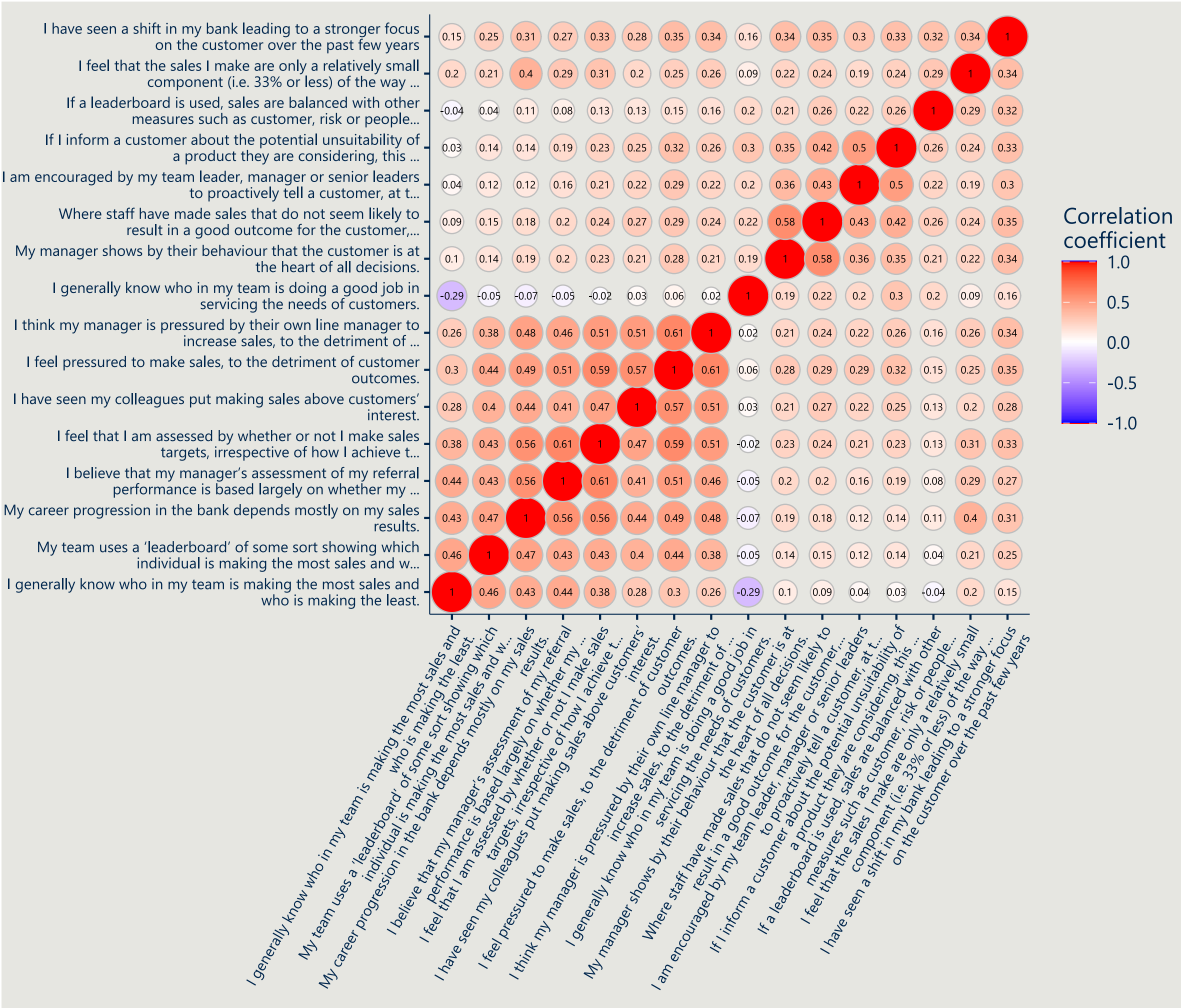
Figure 32 | Some questions are more closely related to each other than the others.

Key insights

- One statement – "I generally know who in my team is doing a good job in servicing the needs of customers" – stands out as having low correlation (sometimes even negative) with the other questions. This statement is probably measuring a different underlying dimension from the others, and because of this it was excluded from the 'perceived customer-centricity' construct. See section Explanation of the single numeric summary; and
- The statements fall into two broad clustering's, with those in the bottom left corner a tighter grouping than the other. The statements within each cluster have more correlation with other statements in that cluster than those that are not. The clusters are different from those in Figure 31, suggesting that these particular results should be interpreted with caution.

Interpretive notes

- Higher values (red) mean a positive correlation i.e. customer-centric answers on one question predict customer-centric answers on the other; and lower values (blue) mean negative i.e. customer-centric answers on one question predict sales-centric answers on the other; and
- Some variables have been switched so they all "point in the same direction" i.e. positive values mean a higher perception of customer-centricity. The expected correlation coefficients are all positive.



In our view, one statement stands out in the correlation matrix as having low correlations with all the other statements – from -0.29 to 0.30 (whereas all other statements have at least one correlation with another statement higher than 0.30, and many have correlations above 0.4 and 0.5). This leads to a suspicion that the agreement with this statement is measuring a different underlying variable from agreement with the other statements.

This suspicion is confirmed by reliability analysis, as shown in Figure 33. Cronbach's Alpha is a measure of internal consistency of a collection of measures being considered as the source data for a single-dimensional summary. Higher values indicate greater evidence that the multiple variables can be seen as measures of a single underlying dimension. Reliability analysis includes consideration of whether Alpha is improved (i.e. increased) if one of the candidate variables is removed. In this case, the overall reliability is very high by any usual social sciences standard – the common rule of thumb is that 0.70 and above is good, and higher than 0.90 means that some of the component questions are redundant. The reliability is improved noticeably by removing the "I generally know who in my team is doing a good job in servicing the needs of customers" statement. Accordingly, our 'perceived customer-centricity' measure removes that item and is based on the 15 remaining. Another candidate to drop, "If a leaderboard is used…" was judged after due consideration worth keeping as it adds important nuance to the other "leaderboard" statement, and improves the reliability only very marginally on exclusion.

Figure 33 | Reliability of the 'customer-centricity' construct is high. One variable ('I know who is doing a good job of servicing customers') was dropped, as indicating a different underlying variable from the others.

Alternative specifications of regression

Removing “what determines variable remuneration”

The regression in the previous section mostly included variables that are largely exogenous to the process of generating views on the respondent’s customer-centricity perception (whether or not they are a manager; their age and gender; their customer type; etc.). The respondent’s perception of customer-centricity of the workplace is expected to have no effect on some of these variables (age and gender) or only a small and slow-moving effect on others (e.g. whether or not you become a manager).

One variable that was arguably questionable to include is the respondent’s perception of what drives remuneration. While a separate question in the survey from the rating questions that were used to define the customer-centricity perception score, a case could be made that both the perceived customer-centricity and the perception of what drives remuneration are measuring the same underlying attitudinal concept.

If this is the case, then some of the explanatory power of the other variables – like customer type, how one engages with them, role, etc – could be masked to the “what do you think drives variable remuneration?” question being included as a dominant explanatory variable. To allow for this case, we fit an alternative version of the model (results presented overleaf in Figure 34) excluding the “what do you think drives variable remuneration” from the list of explanatory variables.

The substantive conclusions are unchanged by the alternative formulation. The results are included here only to allay any concerns from the above line of thinking.

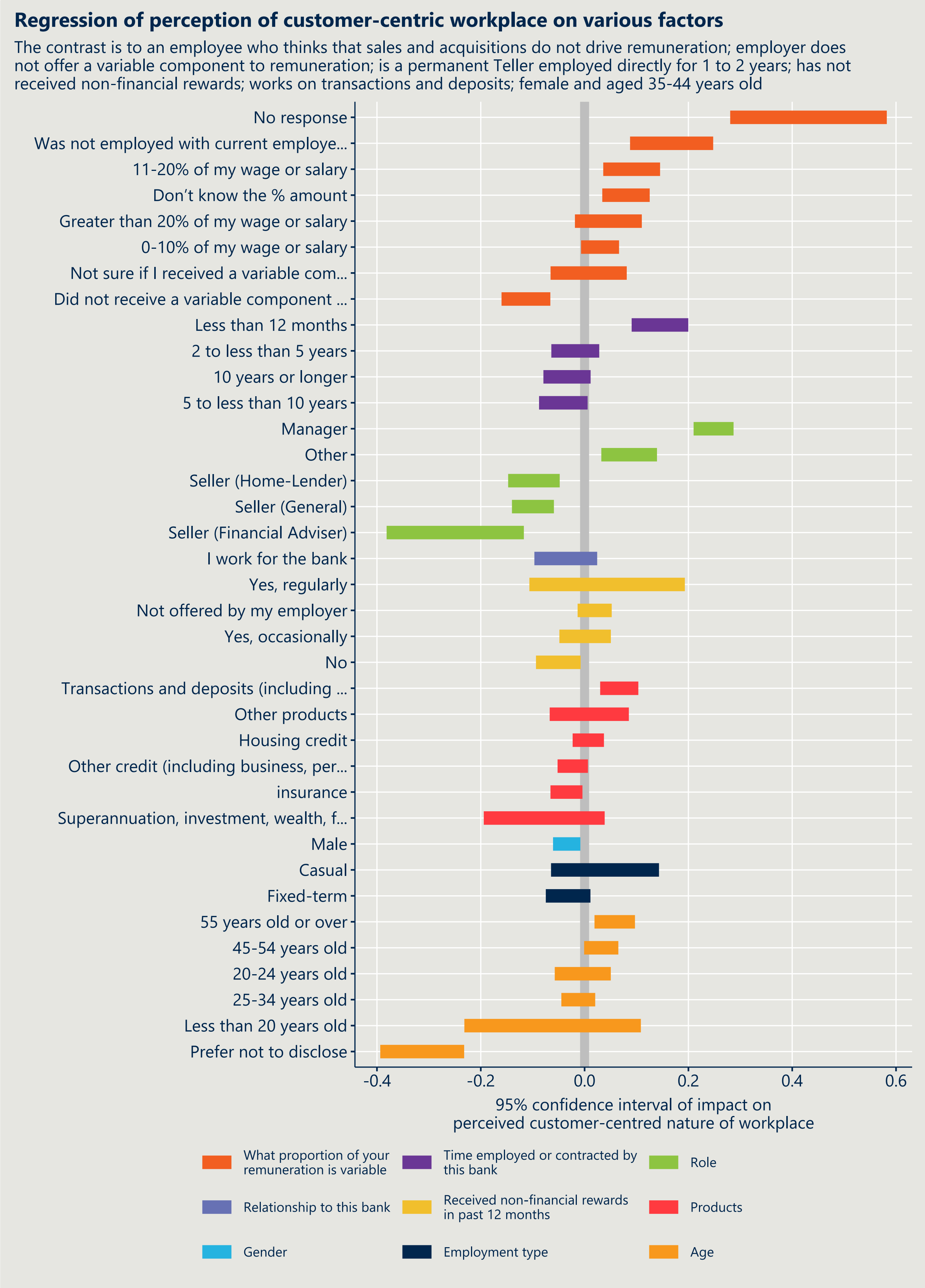
It is worth noting that there are some subtle changes in the estimated effects of the “what proportion of your remuneration is variable” factors. The baseline for comparisons is a workplace that does not offer variable remuneration. The effect of receiving variable remuneration over this baseline is less in this alternative formulation of the regression than the original. The implication of this is that whether or not variable remuneration is perceived to be based on sales, customer acquisition and revenue is a particularly important mediator of the impact (positive or negative) on perceived customer-centricity of a variable remuneration system.

Standard diagnostic plots were examined for both models fit for this paper and no problems were found with any implications for the inferences drawn.

The statistical modelling – like the data management and production of graphics – was performed in the R statistical computing environment.[85]

[85] R Core Team (2020). R: A language and environment for statistical computing. R Foundation for Statistical Computing, Vienna, Austria. URL https://www.R-project.org/

Figure 34 | Substantively unchanged results from alternative formulation of the regression model



Including all levels of “what determines variable remuneration”

A third alternative approach is in the opposite direction to leaving out “what determines variable remuneration” altogether. This approach is to instead include a more granular version of “what determines variable remuneration” as multiple explanatory variables (as respondents could choose as many as they wanted).

The results of this approach are shown in Figure 35 and Figure 36. This “very full model” also includes detail on “customer type” and “primary form of engagement” that was omitted from the model in the main text.

An important effect is observed: the answer to the “what determines variable remuneration” question is clearly very important in understanding perceived customer-centricity. In fact, the positive effect of receiving variable remuneration observed in the model in the main text is no longer present, with its explanatory power absorbed by the extra detail in perceived driver of variable remuneration. The effect of working for the bank for 12 months or less has also been greatly reduced.

Note that “other” (i.e. free text write-in) being seen to determine variable remuneration is negatively associated with perceived customer-centricity, as is meeting business targets, revenue targets and customer acquisition. The free text write-ins for this question included mentions of issues such as favouritism, discretion, and arbitrariness.

This additional model specification reinforces the conclusion in the main text that variable remuneration can help perceptions of customer-centricity, but only if it is seen as being driven by the right causes – such as displaying leadership, excellent customer service, and managing risk.

Figure 35 | Bank effects after controlling for all variables including full detail of "what determines variable remuneration"

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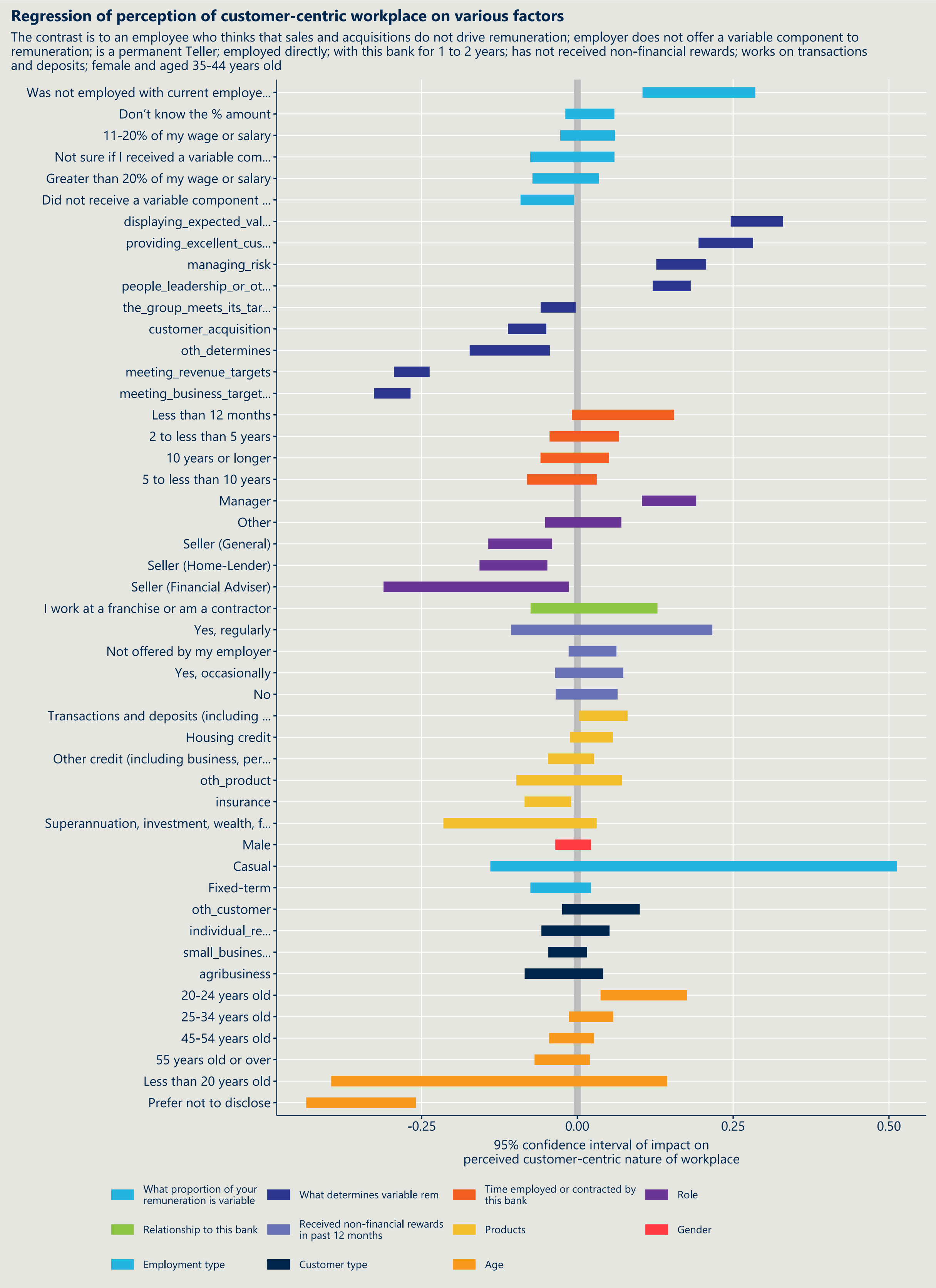
Figure 36 | "What determines variable rem" is more important for predicting customer-centric perception than other variables when included in full



Appendix B – Implementation of the 2017 recommendations

The table below is an overall assessment of compliance of the industry against implementing each of the 2017 recommendations that are relevant to this review. The assessment of compliance considers the current state of policies in place as well as any immediate changes banks have stated they will be making to their policies.

Recommendation	Assessment of compliance
1	• Some banks are not fully compliant across all recommendations. • Partial compliance is most prevalent in relation to: ○ Financial measures – With limited exceptions, banks state they have <33 percent of their scorecards weighted to financial measures. However, several have "productivity" measures that are dependent on a sale being made (e.g. number of customer needs met). These are arguably more accurately sales measures, therefore the effective weight of financial measures for these banks is greater than the recommended 33 percent. ○ Customer measures – while customer measures have evolved to capture richer data through customer complaints and verbatim feedback, there has been little progress as an industry to measure customer outcomes rather than customer satisfaction/advocacy. ○ Leaderboards – while all but one bank reported that leaderboards do not exist at their bank, over 30 percent of staff across the industry reported that leaderboards exist in the survey – demonstrating the disconnect in the perceptions of executives and perceptions of frontline staff.
2	• There are no direct links between VR and financial measures, the only exception being for home lenders of one bank. As such, almost all links are only indirect, where financial measures are considered alongside a range of other measures to determine the final VR allocation.
3	• Across all banks, eligibility to receive any variable reward payment is based on an overall assessment against a range of factors. • However, given that many banks require managers to exercise discretion to assess overall performance and VR allocation, the effective implementation of this recommendation is highly dependent on supporting the discretion process through manager training and holding robust calibration sessions.
4	• Five banks are not fully compliant with this recommendation. • One bank has financial measures that account for over 33 percent of the performance assessment for home lenders. However, the scorecard is under review and new scorecards will be released to employees. • Other banks have productivity measures classified as non-financial measures, but are arguably financial in nature, and therefore were reclassified to financial measures for the purpose of this assessment, which resulted in an effective weight over the recommended 33 percent limit, although this was typically not dramatically more than 33 percent. For example, these measures required a sale to be made to be deemed 'successful'.
5	• Three banks are not fully compliant as the scorecards include productivity measures that are classified as customer measures, but are arguably financial in nature, which are included alongside other genuinely customer centric measures. These productivity measures typically include referrals, in circumstances where a subsequent sale is required, and is therefore perceived to be a financial measure rather than a customer measure. • Across the industry there has been limited progress to measure customer outcomes.
6	• All banks are fully compliant. Banks either have behavioural or risk gateways to be eligible to access any VR, or appropriate behavioural or risk modifiers to adjust the VR

	allocation according to the severity of the breach, where severe breaches result in the individual receiving no VR and where the breach is serious enough, termination.
7	• All banks are fully compliant. There are no accelerators related to financial measures, accelerator-like modifiers related to financial measures or financial gateways.
8	• One significant bank is not compliant with this recommendation. They provide a VR opportunity that is over 50 percent of fixed pay for a substantial minority of home lenders. However, this bank has committed to reducing this maximum to no more than 50 percent of fixed pay – immediately for new hires and progressively over a relatively brief period for others currently eligible for more than 50 percent. • A few banks do not have a cap on maximum achievable variable pay but in practice do not pay variable rewards to in-scope staff that exceed the recommended limit.
9	• All banks have reviewed their culture. However, some reviews do not appear to have focused on assessing whether there is a bias towards sales in preference to ethical behaviour and customer service.
10	• All banks have reviewed, or are reviewing, their performance management system to embed signals and incentives to staff are aligned with Recommendations 2 to 8. • Almost all banks have a performance assessment that is identical to that used to determine VR, with the exception of a few roles, to streamline the process.
11	• All banks have stated that their managers reflect predominantly an ethical and customer focus when exercising any discretion while managing performance, and in allocating variable reward payments due to the calibration processes they have in place to moderate outcomes. • Many banks have also invested in leadership programs to uplift capability in coaching and performance assessments, for example, to assess to quality of customer conversations. Banks should ensure such programs do not reflect a focus on sales outcomes. • All banks state that managers reflect predominantly an ethical and customer focus when communicating with staff and this is reflected in staff perceptions where 85 percent of staff agreed or strongly agreed with the statement ‘My manager shows by their behaviour that the customer is at the heart of all decisions’.
12	• All but one bank stated that leaderboards do not exist at their bank. However, the results from the survey indicate that across the industry over 30 percent of staff believe leaderboards exist, and over 20 percent of staff disagree with the statement “if a leaderboard is used, sales are balanced with other measures such as customer, risk or people measures”. • Two banks run recognition programs for home lenders that include financial performance. However, for one of these banks financial performance is a component of a balanced scorecard approach to recognition.
13	• Most executive scorecards balance financial measures with risk, customer and people measures. However, for some banks, executive scorecards continue to mainly focus on financial measures, which account for over 50 percent of the weight. • Almost all banks have listed increasing market share in home lending as a performance objective for senior executives.
14	• All banks have reported publicly how retail staff are remunerated. • All banks state that they have effective and safe whistle-blower channels where staff can provide feedback, anonymously if required.
16	• All banks have reported that they have examined their governance arrangements with retail (non-mortgage) brokers to ensure their practices are consistent with the recommendations of this review. However, retail (non-mortgage) brokers were not relevant to most banks.
20	• All banks that pay incentives to introducers and referrers have reviewed their governance arrangements with introducers and referrers and uplifted processes and controls to ensure they meet minimum conduct and compliance standards. For

	example, some banks have mandated upfront training on compliance and strengthened their consequence management with appropriate remuneration clawbacks in case of misconduct or policy breaches.
21	• All banks with franchisee networks have examined their governance and remuneration arrangements to ensure these are consistent with the recommendations of this Review. Some of these banks have ensured that the performance management system for franchisees is the same as that in the rest of the bank.

The list of recommendations from the 2017 review that are relevant for this review are below.

Recommendation 1: *I recommend that all banks begin to implement the recommendations in this Report as quickly as systems and other changes can be introduced. If transitional arrangements are necessary, full implementation should be achieved by no later than the performance year that begins in 2020.*

Recommendation 2: *Banks remove variable reward payments and campaign related incentives that are directly linked to sales or the achievement of sales targets (including, but not limited to cross sales, referral targets, and profit and revenue targets).*

Recommendation 3: *Eligibility to receive any variable reward payment should be based on an overall assessment against a range of factors that reflect the breadth of the responsibilities of each role.*

Recommendation 4: *Any financial measures included in an overall assessment consistent with Recommendation 3 should:*

- *Be product neutral (that is, not encourage the sale of one product over another); and*
- *In the case of a scorecard, together attract a maximum effective weight of 50 percent as quickly as systems and other changes can be introduced, falling to 33 percent or less by 2020.*

Recommendation 5: *All customer measures are genuinely customer-centric and tailored to the role being assessed, and progressively reflect a focus on customer outcomes not just customer loyalty/satisfaction.*

Recommendation 6: *Credible behavioural or equivalent values gateways be applied to determine whether an individual can access any variable rewards to which they might otherwise be entitled.*

Recommendation 7: *Variable reward payments no longer include:*

- *Accelerators related to financial measures;*
- *Accelerator-like modifiers related to financial measures;*
- *Other mechanisms related to financial measures that have such an accelerator-like effect on the value of variable rewards available; and*
- *Financial gateways, including but not limited to those that relate to the number or value of cross sells.*

Recommendation 8: *Variable reward payments ultimately amount to a relatively small proportion of fixed pay, with a progressive reduction in the maximum variable reward amount payable in any schemes that require a transition period to implement this recommendation.*

Recommendation 9: *Each bank formally examine its workplace culture and institute formal processes to redress any conscious or unconscious bias towards sales in preference to ethical behaviour and customer service.*

Recommendation 10: *Each bank examine its performance management system and make changes as necessary to ensure that the embedded signals and incentives to staff are aligned with Recommendations 2 to 8.*

***Recommendation 11**: Each bank ensure Managers reflect predominantly an ethical and customer focus when communicating with staff, exercising any discretion while managing performance, and in allocating variable reward payments.*

***Recommendation 12:** Each bank reconsider what use is made, if any, of leaderboards, recognition programs and campaigns as well as any other methods that have similar effect (including informally in branches or call centres) and ensure any continuing role in using these methods is consistent with the intention to de-emphasise sales relative to ethical behaviour and customer outcomes.*

***Recommendation 13:** Consistent with the objectives of the recommendations for frontline staff, the variable reward payment and performance management arrangements of all senior and (retail bank) middle level executives be based on:*

a. Their overall performance against a number of measures that reflect the nature and breadth of their role; and

b. Customer oriented, ethical behaviour and non-financial measures accounting for the dominant factors in that assessment.

***Recommendation 14:** Boards and Chief Executives:*

a. Visibly and effectively oversee the implementation of these recommendations for at least the next five years and report publicly, in their Annual Report to shareholders, for example, on how retail staff are remunerated, and their performance assessed; and

b. Ensure that effective, safe channels are in place to obtain feedback from frontline staff about their perceptions of the effectiveness of efforts to reform the bank's culture, performance management and remuneration arrangements, including in respect of whistle-blower arrangements.

***Recommendation 15:** The ABA commission an independent reviewer to report publicly in three years about how well banks have changed their practices and implemented the recommendations and assess whether further regulatory or legislative change is required.*

***Recommendation 16:** Banks examine their governance arrangements with retail (non-mortgage) brokers to ensure their practices are consistent with the recommendations of this review.*

***Recommendation 20:** In respect of Introducers and Referrers:*

a. Banks examine their governance of these arrangements to ensure that existing practices are appropriate; and

b. ASIC, in due course, investigate whether the upfront commission paid to Introducers and Referrer is justified.

***Recommendation 21:** Banks that provide products or services through Franchisees examine their governance and, as appropriate, remuneration arrangements and seek to make changes that are consistent with the recommendations of this Review.*

Appendix C – Level of discretion applied in performance management and variable remuneration

The tables below show the distribution of banks that apply each level of discretion across the allocation VR (as explained in Section 4.2.2.1) and performance management (as explained in Section 3.2.2.1) for Sellers (General) and Managers. The tables for Tellers and home lenders are included in Section 4.2.2.1. Sellers (Financial Advisers) have not been included to avoid identifying banks due to the limited number of these roles that are in-scope across all banks.

These tables demonstrate that there is a considerably high level of discretion applied across both roles, with banks typically applying either a 'high' or 'medium' level of discretion across both performance management and VR allocation. As such, this shows that a higher level of discretion is applied across performance management and VR allocation for Managers and Sellers (General) in comparison to home lenders as shown in section 4.2.2.1.

Table 6 | Level of discretion applied in performance management and VR allocation for Sellers (General)

	Level of discretion applied in VR allocation			
Level of discretion applied in performance management	L	M	H	No bonus
L	1	0	0	1
M	1	3	0	0
H	1	4	4	2

Table 7 | Level of discretion applied in performance management and VR allocation for Managers

	Level of discretion applied in VR allocation			
Level of discretion applied in performance management	L	M	H	No bonus
L	0	0	0	2
M	2	4	0	0
H	1	3	5	1

Appendix D – Terms of Reference

Aims

1. Assess the implementation of the recommendations in the final report of the 2017 Retail Banking Remuneration Review (Sedgwick Review);
2. Ensure the intent, integrity and spirit of the Recommendations are being implemented; and
3. Prepare a report on the implementation of the recommendations at participating banks.

Scope of the 2021 assessment

The scope of this assessment will be limited to bank staff, introducers, referrers, and franchisees and will not include a review of the mortgage broker channel. The exclusion of broker remuneration from this review is due to the developments which have taken place as a result of the Royal Commission recommendations which were specific to broker remuneration and which superseded the Sedgwick Review recommendations relating to brokers. This means that some recommendations from the 2017 review will be out of scope for the 2021 review.
For clarity:

- Recommendations 1-15 relating to Bank staff are in-scope;
- Recommendations 16-19 relating to Mortgage Brokers are out-of-scope; and
- Recommendations 20-21 relating to Introducers and Referrers, and Franchisees are in-scope.

An assessment of the implementation of banks of the in-scope Sedgwick Recommendations will involve:

1. Collation and analysis of:
    a. Current remuneration structures for retail bank staff, including remuneration packages, incentive plans, and 'balanced scorecard' arrangements, and consistency of these current remuneration structures with the Sedgwick Recommendations; and
    b. Current remuneration policies for all bank staff relevant to the Sedgwick Recommendations and performance management systems, and consistency of these current policies and systems with the Sedgwick Recommendations.
2. Consideration of remuneration structures for retail bank staff and any remuneration policies for all bank staff relevant to the Sedgwick Recommendations.
3. Consideration of responses by participating banks and whether these responses strengthen the alignment of remuneration and incentives and good customer outcomes.

Examination

In completing the assessment, the following industry commitments, policies and practices, and processes should be examined:

- Remuneration packages, incentive plans and balanced scorecard arrangements for retail bank staff and retail bank management in individual banks;
- Remuneration policies and performance management systems in individual banks;

- Statements made by senior executives and senior managers in individual banks regarding changes made and/or proposed to remuneration structures, governance and performance management systems across the bank, including, for example, public statements, media releases, internal updates (newsletters, intranet), etc;
- Examples of staff training, formal or informal, regarding the remuneration policies and performance management systems in individual banks;
- Overarching principles on remuneration and incentives to support good customer outcomes and sound banking practices, developed under Initiative 1 of the Banking Reform Program;
- Other materials that an individual bank may have which are relevant to the assessment, such as implementation plans, status updates, and/or comparisons between old remuneration structures and new remuneration structures; and
- The industry frontline staff and management survey commissioned for this review.

In examining the extent to which the Sedgwick Recommendations have been implemented in part or full, the following factors should be considered:

- Different business models adopted by banks and the nature, scale and complexity of their businesses, including remuneration structures impacting internal staff, external relationships, and contractual obligations; and
- Ensuring the principles of competition, customer choice and commerciality, including the importance of recognising and rewarding good performance, are balanced.

Appendix E – Glossary

General	
2017 Report/Review	Independent Review of product sales commissions and product-based payments in retail banking in Australia
2019 Report/Review	Mid-term Review into the industry level assessment of progress in implementing the 21 Recommendations of the 2017 Review
ABA	Australian Banking Association
ACCC	Australian Competition and Consumer Commission
AFCA	Australian Financial Complaints Authority
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
COVID-19	The Coronavirus pandemic
CRO	Chief Risk Officer
EA	The Fair Work Act 2010 (Cth) contains provisions that protect employees against breaches of the terms of modern awards and collectively bargained employment agreements; that is, Enterprise Agreements (EA).
FOFA	Future of Financial Advice (FOFA) reforms
FSRC	Financial Services Royal Commission – used in reference to volumes 1 of both the Interim and Final Reports.
FSU	Finance Sector Union
Leaderboard	Leaderboards compare the performance against target of individuals with others within the team/business unit.
Internal audit	An internal audit function forms part of a bank's third line of defence, independently evaluating the effectiveness of the bank's risk management and compliance with regulatory requirements.
Issues Paper	The Retail Banking Remuneration Review Issues Paper published on 17 January 2017
Questionnaire	Remuneration Assessment Review Questionnaire as at January 2021 sent out to participants for the purposes of data gathering.
Terms of Reference	Framework and parameters under which the Review operates. Refer to Appendix D.
Tier 2 products	Tier 2 products as defined by ASIC's Regulatory Guide 146 include financial products that are generally simpler and therefore have lighter training standards. Tier 2 products are: General insurance products except for personal sickness and accident, Consumer credit insurance,

	Basic deposit products, Non-cash payment products and First Home Saver Accounts (FHSA) issued by ADIs.
Role Type	
Managers	Limited to the first- and second-line managers and supervisors of the customer facing staff (that is Tellers and Sellers: General, Home Lenders and Financial Advisers)
Sellers: Financial Advisers	For the purpose of this Review, Financial Advisers include individuals who are bank staff and who provide personal and general advice to retail and small business customers on Tier 2 products only.
Sellers: General	Include personal bankers, small business banker-equivalent roles and call centre roles that can sell products to customers.
Sellers: Home Lenders	Staff whose primary function and responsibility relates to the sale of home loans (including new mortgages and top-ups) to retail and small business customers.
Tellers	Customer-facing staff who primarily refer customers to other parts of the business or to other staff.
Specialist Lender/Bankers	Primary role is home lending, but some banks have defined a unique role for groups of home lenders and this role requires a higher level of qualification, training and capability.
Rewards and reward types	
At-risk pay	Variable reward paid together with the annual increase in fixed pay (if any).
Fixed pay	The guaranteed level of monetary reward paid by an employer to an individual, typically comprising base salary plus Superannuation Guarantee in Australia.
Recognition programs and campaigns	As well as fixed pay and variable reward payments, individuals may also be eligible to receive other monetary and non-monetary rewards that are provided on an ad hoc basis to recognise special effort, performance or the attributes of an individual or team. Banks may also supplement the formal performance rewards with ad hoc rewards that are related to the conduct of campaigns, typically to increase sales of specific products.
Variable reward payments (rewards)	The level of monetary reward paid by an employer to an eligible individual. It includes bonuses, incentives or product-based payments/product sales commissions.
Reward mechanics	
Accelerator	An arrangement whereby a higher rate of reward is earned with higher levels of performance, for example increasing volumes of sale.
Clawback (for staff)	A mechanism whereby all or part of an individual's variable reward payment is recovered by the bank from the individual if certain conditions are met. In some instances, the reward may be forfeited entirely if the payment has not yet been made to the individual.
Clawback (for third-party channels)	A mechanism in place for the bank to take back the commissions paid to the third-party channel if the loan is repaid/settled/closed or refinanced within a specific period.

Cross selling	Sale of additional or 'add-on' products to customers in addition to the primary product(s) an individual is rewarded on.
Gateway	Condition that must be met before potential bonus/incentive/product sales commissions and product-based payments can be accessed by the individual.
Malus	A mechanism in place for the bank to require a payment as compensation for poor performance.
Modifier	Increases or decreases the bonus or incentive payable once a condition has been met.
Third Party	
Brokers, Aggregators and Franchises	Brokers deal with and sell a range of products from numerous banks with whom they have a relationship. Brokers may be members of aggregator groups and in such cases the interaction with the bank (whose products they are selling to the customer) will occur at the aggregator level rather than at the broker level. Aggregators will also facilitate the relationship between the customer and the Broker. Brokers and Aggregators are the primary point of contact with the customer. However, the bank itself makes its own assessment of the credit-worthiness of the proposed borrower and makes the final decision as to whether or not to grant a loan. Other models include profit-sharing arrangements with locally owned entities or Franchises. In both of these cases the third party operates (and may at least partially own) a branch (or several branches) that exclusively sell branded products on behalf of the primary bank.
Introducers and Referrers	Introducers and Referrers are not required to hold a credit licence provided they fall within the exemption provided by regulation 25 of the National Consumer Credit Protection Regulations 2010. Unlicensed introducers cannot undertake any other credit activities and cannot 'sell' products. However, they may refer customers to the bank and provide the bank with the customer's name and contact details along with a brief description of the purpose for which the customer may want the credit – provided that they have disclosed any commissions or other benefits they may receive from the referral.