1998

THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

FINANCIAL SECTOR REFORM (AMENDMENTS AND TRANSITIONAL PROVISIONS) BILL 1998

EXPLANATORY MEMORANDUM

(Circulated by authority of the Treasurer, the Honourable Peter Costello MP)

13648

Formal Clauses

Regulation Impact Statements

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Outline

1.1 This Bill forms a part of a package of legislation to implement the Government's response to the recommendations of the Financial System Inquiry as announced by the Treasurer, the Hon. Peter Costello, MP, in the House of Representatives on 2 September 1997.

1.2 The Bill contains 19 schedules outlining amendments and additions to a diverse range of legislation affected by the Treasurer's financial sector reform package.

1.3 The Bill implements new legislation consistent with the Treasurer's 2 September announcement, provides necessary transitional provisions to smooth the passage to the new regulatory/legislative framework, and seeks to rationalise and modernise provisions that have become dated or obsolete. The Bill also contains various consequential items arising from legislative amendments to various Acts referred to in the schedules and other Bills included in the broader package.

1.4 The details of the Bill (including summaries of each schedule) are provided in Section 5.

Financial Impact Statement

1.5 There will be an annual budgetary cost associated with the removal of the requirement on banks to hold non-callable deposits (NCDs) with the Reserve Bank of Australia (RBA). This cost reflects the fact that banks pay (via revenue foregone) the RBA via NCDs significantly more than it costs the RBA to supervise these institutions.

1.6 The requirement for banks to make non-callable deposits will be removed from a date to be set by proclamation. From that date, the annual cost to the budget is estimated to be around $200 million based on current NCD levels.

1.7 Under the new regulatory regime, banks and other Deposit Taking Institutions (DTI) will only be required to contribute funds sufficient to meeting their share of

both APRA's costs of prudential supervision and one-off establishment costs and ASIC's costs of consumer regulation in relation to banks and other DTIs.

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Abbreviations

The following abbreviations are used in this explanatory memorandum.

AAPBS	-	Australian Association of Permanent Building Societies
ACCC	-	Australian Competition and Consumer Commission
ACT	-	Australian Capital Territory
ADI	-	Authorised Deposit-taking Institution
AFIC	-	Australian Financial Institutions Commission
APCA	-	Australian Payments Clearing Association
APRA	-	Australian Prudential Regulation Authority
APSC	-	Australian Payments System Council
ASC	-	Australian Securities Commission
ASIC	-	Australian Securities and Investments Commission
CUSCAL	-	Credit Union Services (Australia) Limited
DTI	-	Deposit Taking Institution
FIC	-	Financial Institutions Code
FCA		*Financial Corporations Act 1974*
FSAC	-	Financial Sector Advisory Council
FSI	-	Financial System Inquiry
ISC	-	Insurance and Superannuation Commission
NBFI	-	Non-Bank Financial Institutions
NCDs	-	Non-Callable Deposits
NOHC	-	Non-Operating Holding Company
PSB	-	Payments System Board
RBA	-	Reserve Bank of Australia
RIS	-	Regulation Impact Statement
RTGS	-	Real-Time Gross Settlement
SSA	-	State Supervisory Authority
SSP	-	Special Service Provider
TPA	-	*Trade Practices Act 1974*
UCCC	-	Uniform Consumer Credit Code

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Regulation impact statements

RIS - Schedules 1, 4, 5, 6, 10, 11, 12, 13, 15, 16, 17, 18, 19

This Regulation Impact Statement ('RIS') accompanies the Financial Sector Reform (Amendments and Transitional Provisions) Bill 1998. It deals with a range of reform measures for regulatory arrangements governing corporations and consumer

protection and market integrity in the financial system. In particular, the performance of those functions by a regulator to be known as the Australian Securities and Investments Commission (ASIC).

Regulatory objectives

3.1 To ensure efficiency in financial markets, participants must act with integrity and there must be adequate disclosure to facilitate informed judgements by consumers and investors. The need for regulatory responses to address potential market failure in those areas is well established.

3.2 Market integrity regulation seeks to promote market development by securing confidence and protecting participants from fraud and other unfair practices. Consumer protection aims to ensure that retail investors have adequate information, are treated fairly and have adequate avenues for redress. Often it is difficult to distinguish between regulation directed at market integrity and consumer protection, since both use the regulatory tools of conduct and disclosure rules.

3.3 There are several agencies at the Commonwealth and State/Territory levels which provide specific forms of market integrity and consumer protection regulation for savings, investment, risk management and payment products and the provision of advice. They include the Insurance and Superannuation Commission (ISC), the Australian Securities Commission (ASC), the Australian Competition and Consumer Commission (ACCC), the Australian Payments System Council (APSC), and the Australian Financial Institutions Commission (AFIC) and associated State Supervisory Authorities (SSAs). The regulation of credit is the responsibility of the States and Territories under the *Uniform Consumer Credit Code* (UCCC).

3.4 The Financial System Inquiry (FSI), which reported to the Government in March 1997 considered that, in relation to the regulatory framework for market integrity and consumer protection in the financial system, it would be desirable to ensure that:

- the regulatory structure is flexible and responsive to the forces for change operating on the system;

- there is consistency in regulation of similar financial products to promote competition by improving comparability;

- financial markets are more contestable, efficient and fair;

- regulation of financial conglomerates is effective, which will facilitate competition and efficiency; and

- international competitiveness of the Australian financial system is facilitated.

Problem

3.5 The efficiency and effectiveness of the regulatory framework for the financial system was examined by the FSI. Many persons expressed dissatisfaction to the FSI with the existing framework for delivery of market integrity and consumer protection regulation in the finance sector. The key concerns are that current arrangements with a combination of economy wide and institutionally based approaches produce:

- inconsistency of requirements for functionally equivalent products in a number of areas, particularly product disclosure regulation and financial sales and advice;

• duplication between specific financial system regulation and economy-wide regulation under the *Trade Practices Act 1974* (TPA*)*; and

• a proliferation of dispute resolution mechanisms for consumers leading to overlaps, non-uniformity and inefficiency.

3.6 The FSI found that the financial system is undergoing rapid change due to technological innovation, an evolving business environment and longer-term changes in customer needs and profiles. Entry of new participants, products and distribution channels will cause the financial system to expand beyond the traditional categories of banking, insurance and financial exchanges.

3. The FSI considered that changes to the current regulatory framework were necessary for it to meet the regulatory objectives described above.

Options

3.8 The FSI considered a number of models for the regulatory framework in the financial sector.

STATUS QUO

3.9 The first option considered was the retention of the existing system comprising a combination of multiple institution-based regulators and general economy wide regulation. At the Commonwealth level, the relevant regulators are the ISC (insurance and superannuation), the RBA/APSC (banking), and the ACCC (economy-wide consumer protection). The ASC (corporations and securities/futures) is directly responsible to the Commonwealth Treasurer although, as discussed below, it is based on cooperation between the Commonwealth and other jurisdictions. There are other regulatory agencies at the State and Territory level administering relevant legislation. Chief among those is AFIC and the relevant SSAs which administer legislation concerning non-bank deposit-taking institutions (building societies and credit unions).

DUAL REGULATORY MODEL

3.10 The dual regulatory model involves the creation of a specialist consumer regulator for the financial sector which would take over the consumer protection role of the various existing financial sector regulators. The economy-wide coverage of the TPA and the ACCC would also be retained.

COREGULATORY MODEL

3.11 Under the coregulatory model, regulation would be built upon industry based self-regulatory codes in the various industry sectors. A self-regulatory umbrella organisation would be established and all institutions and individuals with retail clients would be required to be members and it would be governed by a council of representatives from the various lines of business and users. This organisation would be responsible for licensing and monitoring compliance and with codes and overseeing the dispute resolution schemes. The self-regulatory organisation would be monitored by the ACCC (which would retain jurisdiction over the universally applied consumer protection provisions in the TPA), and a small statutory consumer regulator in the Treasurer's portfolio which would be responsible for overseeing and auditing the performance of the self-regulatory arrangements.

SINGLE REGULATOR MODEL

3.12 Under the single regulator model, there would be established a single consumer regulator for the financial system which would take over primary functional

responsibility for the consumer protection roles currently undertaken by the financial system regulators and the ACCC. This model could be advanced by a statutory scheme (as in the dual regulatory model) or a scheme based on self-regulation (as in the coregulatory model).

Impact Analysis

3.13 In assessing the options, there are a number of key issues which it is convenient to address in turn. They are:

- which groups will be affected by a change in the regulatory framework for consumer protection in the financial system?;

- whether the advantages, relative to the costs of change, warrant bringing together into one agency the specific finance sector consumer protection regulation currently undertaken by the various finance sector regulators;

- if so, whether the best approach is to base consumer regulation in the finance sector on self-regulation and industry codes of practice, statutory rules and procedures administered by public agencies, or a combination of each;

- if a specialised agency consumer protection is established, should it be a stand-alone or should also be responsible for regulation of market integrity, securities and corporations; and

- if a specialised agency consumer protection is established, how should it be funded?

who are the affected parties?

3.14 The parties affected by a transfer of regulatory responsibilities for consumer protection functions in the financial system fall into three key categories:

- the relevant regulators, being the ASC, the ISC, the ACCC, and AFIC and associated SSAs;

- institutions offering retail financial services subject to consumer protection regulation, being banks, building societies, credit unions, superannuation trustees, general insurance and life companies, and friendly societies; and

- consumers and investors whose interests are sought to be protected by the consumer protection framework.

Should consumer protection responsibilities in the financial sector be amalgamated?

3.15 The key possible advantages of combining regulatory arrangements for consumer protection across the whole financial sector would be:

- greater consistency of regulation;

- minimisation of regulatory gaps or overlaps;

- reduced risk of regulatory capture; and

- the development of a stronger single body of expertise.

3.16 The key possible disadvantages would be:

- loss of specialisation and coordination with prudential regulation or other related areas of regulation in specific industry sectors;

- loss of competition between regulators;

- costs of transition.

3.17 The FSI found the arguments in favour of amalgamation to be compelling. The existing system's negative consequences included substantially differing disclosure requirements for similar investment vehicles and inconsistency in approach to regulation of financial sales and advice. Although splitting the consumer protection function from other aspects of regulation (such as prudential supervision) means that some participants offering specific services would have to deal with two regulators when they previously dealt with only one which handled both functions, this disadvantage is outweighed by the advantage to participants offering a range of services who currently face a multitude of regulators which take different approaches to consumer protection issues.

3.18 Further, retention of institution-based regulators is unlikely to facilitate flexibility and responsiveness to the forces shaping financial markets, including new entrants to the industry, new products and means of service delivery which increasingly blur distinctions between products and institutions.

3.19 The FSI considered that better focused, more consistent and responsive regulation would be delivered by a single regulator performing the consumer protection function for banking services and comparable services offered by non-bank deposit-taking institutions, retirement savings accounts, superannuation, life insurance and general insurance. Other products and services with similar characteristics should also come within the ambit of the scheme. Accordingly, friendly societies should also be subject to the jurisdiction of the single regulator.

3.20 Although there will undoubtedly be transition costs in changing the regulatory framework, the factors mentioned above mean that the long term costs of retaining the status quo are, potentially, far greater.

What regulatory approach should be used?

3.21 The impact on participants in the financial sector of the regulatory arrangements is dependent to a large extent on the type of regulatory approach adopted. There are a number of approaches which could be adopted, including:

- *a statutory approach* comprising specific detailed laws administered by the regulator;

- *a coregulatory approach* where 'framework legislation' sets out general principles and the specific regulation of particular transactions is provided through detailed codes in particular industries; and

- *a self-regulatory approach* where regulation is based in industry schemes alone with no legislative backing.

3.22 A statutory approach leads to greater consistency across industry sectors and is more effective in industries which are highly dispersed or have a history of conduct and disclosure problems. However, legislation is more difficult to change to reflect market developments.

3.23 A coregulatory approach is more responsive to market developments since codes are more readily modified. It has advantages in terms of funding because a large part

of the cost is borne directly by industry and consumers who benefit. It is more susceptible than a statutory scheme to regulatory capture because of the high level of industry involvement, but oversight and audit by a public agency makes this of less concern than a system based purely on self-regulation. In the context of the financial system, coregulation could lead to disjointed regulation because of the numerous industry-based organisations that would be required to participate. Coregulation is less suitable at the retail level than the wholesale level because of greater information imbalances between consumers and suppliers.

3.24 The complexity of financial products means consumers can easily misunderstand or be misled and the consequences of dishonour are great. The special characteristics of the products, services and participants in the financial system means self-regulation will not normally be appropriate, especially at the retail level.

3.25 Since there are the differences in the environments of various sectors of the financial system, no particular regulatory approach is ideal for use across the board. The FSI considered that the best way to balance the objectives of efficiency and effectiveness would be to establish a regulatory framework which features a combination of regulatory approaches.

should the consumer protection function be combined with other functions?

3.26 The FSI received some support for a dedicated consumer protection regulator on the grounds that there was a danger that, if it were combined with other functions, the consumer protection function would become secondary to other objectives. On the other hand, it is arguable that an agency should have a broader task than merely consumer protection to ensure there is a balance in pursuing regulatory objectives.

3.27 The FSI noted the strong links between market integrity and consumer protection in the financial sector. In fact, in some areas it is difficult to distinguish between them. It is also difficult to distinguish between wholesale and retail markets. Any attempt to draw a dividing line would necessarily involve an arbitrary element. Pragmatic approaches need to be adopted so that the regulatory framework is flexible and able to cope with shifts and imprecision in the dividing line. Furthermore, if a division was attempted, many market participants would be engaged in retail and wholesale transactions and would therefore be subject to more than one regulator covering much the same ground.

3.28 The FSI further noted that there were strong links between market integrity regulation in the finance sector and general corporate regulation. Both aim to promote disclosure to public investors of the nature of investments and both rely heavily on principles of good corporate governance. Furthermore, there are links between financial markets and the finance sector, given that the markets are an important source, and facilitate provision, of corporate finance.

3.29 In light of the above, the FSI considered that the single agency responsible for consumer protection should also have responsibility for market integrity in the financial system and general corporate regulation.

how should the CONSUMER PROTECTION regulator be funded?

3.30 The main options for funding a government agency performing consumer protection functions across the financial system are:

- by budget appropriation (that is, by taxpayers generally) with no cost recovery;

- by budget appropriation but with costs recovered from statutory fees and charges paid by industry participants to the Government; or

- through fees and charges paid by industry participants directly to the regulator.

3.31 The FSI report noted that it is desirable for the costs of regulation in particular industry sectors to be borne directly by the businesses and consumers who benefit from it rather than on the community as a whole. However, this must be applied in a practical way. It was considered that, so far as possible, industries should be levied to meet the cost of regulation in proportion to the agency resources expended on it. The charges of regulatory agencies should reflect their costs.

3.32 The FSI considered that, from the perspective of financial regulation, it is preferable for financial sector regulatory agencies to operate "off-budget". This would allow funding of financial regulation to be determined by reference only to market needs, rather than targets for the overall budget.

3.33 However, the contemplated agency will possess considerable investigative and enforcement tools which can be exercised against persons other than "market players". It is arguable that such an agency should be, and should be seen to be, accountable and responsible to the public as a whole. Further, the real costs of regulation extend beyond the running costs of the regulatory agency itself. Other government agencies, such as police, courts, tribunals and advisory bodies all play an important role in the system and it is appropriate that funds recouped are directed to funding a proportion of their activities also.

Consultation Process

3.34 A consultation process was undertaken by the FSI. The FSI received a total of 421 submissions, including 153 submissions responding to a Discussion Paper published by the FSI in November 1996. These submissions were prepared by a broad cross-section of industry participants and other interested individuals, corporations and groups. The FSI held public consultations in all mainland capital cities during December 1996, and met with a range of financial industry experts and participants, regulatory agencies and consumers, both in Australia and overseas. The FSI also participated in a range of conferences and seminars, and had a home page on the Internet.

3.35 The proposal that consumer regulation in the financial sector be placed under a single entity received wide support in submissions to the FSI from regulators, industry groups and consumers.

Conclusion and Recommended Option

KEY Conclusions

3.36 The consumer protection functions across the financial sector should be combined in a single agency. Retention of the status quo is untenable in the long term.

3.37 A combination of regulatory approaches should be used, with industry-based regulation playing a role as appropriate. None of the regulatory approaches is suitable for use across the board.

3.38 ASIC should assume the primary functional responsibility for consumer protection in the financial system. However, to prevent regulatory gaps emerging, the ACCC should retain its economy-wide jurisdiction, underpinned by administrative arrangements to prevent regulatory duplication. The interaction of State and Territory

provisions and agencies with the financial sector legislation and consumer protection regulator will need to be negotiated with the States and Territories at the same time as other aspects of the proposal.

3.39 The difficulties in separating market integrity regulation and consumer protection regulation is acknowledged. Further, there is merit in combining the function with others so that a balanced approach may be taken. Accordingly, the consumer protection function should be combined with market integrity and corporate regulation, which is currently administered by the ASC.

3.40 The fees and charges made by the regulator should be set to reflect the costs of regulation and, so far as is practicable, particular market segments (such as banking or insurance) should bear an appropriate proportionate burden. However, it is important to ensure that the *total* regulatory costs are taken into account, not merely the running costs of the agency itself.

Recommended option

3.41 A new body, to be known as ASIC, will be formed by using the ASC as a base and adding to its responsibilities the consumer protection functions of the ISC and the APSC. Since the corporate regulatory framework and the ASC exist by virtue of an agreement between the Commonwealth and the States/Northern Territory, the proposed change in structure and addition of functions ASC is subject to the agreement of those jurisdictions. ASIC would also (subject to the agreement of the States/Territories) accept responsibility for market integrity and consumer protection functions in connection with building societies, credit unions and friendly societies.

3.42 This would give ASIC responsibility for:

- regulation of corporations and securities;

- market integrity and consumer protection functions (particularly in connection with product disclosure) concerning:

- banks, building societies, credit unions and friendly societies;

- superannuation interests;

- retirement savings accounts (RSAs); and

- general insurance and life insurance products.

3.43 ASIC would be given broad framework legislation which allowed it to adopt detailed codes where necessary (a statutory approach), or leave it to industry bodies to develop the codes (a coregulatory approach). However, in recognition of the importance of the health, credibility and security of the financial system to the wider economy, ASIC would be given a full range of enforcement options, access to adequate resources and a mandate to use them where appropriate.

3.44 The funding arrangements for ASIC would be modelled on the existing arrangements for the ASC. The ASC collects statutory fees and charges which are channelled into consolidated revenue and the ASC, together with other bodies involved in the national scheme, are funded by Parliamentary appropriation. However, ASIC would be required to report on the costs incurred in regulating specific industry sectors and the fees and charges for those sectors would be set by the Government with a view to matching the charges recovered with the costs. The fees and charges for particular sectors (such as insurance or banking) may differ depending on the level of costs associated with regulating those sectors.

Implementation

3.45 The current legislative and administrative framework for corporate regulation is based on cooperation between the Commonwealth, the States and the Northern Territory ('NT'). The States and the NT continue to play a role in the national corporate regulation scheme and their legislation underpins the scheme.

3.46 Furthermore, the proposed transfer of some responsibilities currently governed by State and Territory law (in connection with building societies, credit unions and friendly societies) will require agreement of all States and Territories to be fully effective.

3.47 It is proposed that the conversion of the ASC to ASIC will occur in two stages.

3.48 The first stage will occur simultaneously with the establishment of APRA. It involves minimal change to the ASC, in particular to the *Australian Securities Commission Act 1989*, but will result in the ASC becoming known as ASIC. ASIC will continue to carry on the roles the ASC does now. In addition, it will perform the following Commonwealth functions:

- those currently performed by the ISC not transferred to APRA (namely consumer protection and market integrity functions relating to insurance and superannuation);

- monitoring of banking codes of conduct (currently performed by the APSC); and

- take over operationally some aspects of the ACCC's jurisdiction over the financial system (although there will be no legislative change to achieve this in the first stage).

3.49 Points to note are that:

- additional resources will be provided to ASIC to fully fund the performance of the additional Commonwealth functions, which will be recouped from regulated industry sectors (primarily superannuation and insurance) through levies, fees and charges collected by APRA and paid into Consolidated Revenue for channelling to ASIC;

- there will be provision for cross appointments and cross delegations to facilitate ASIC and APRA personnel working together in the start up phase;

- aside from being provided with additional resources, and some changes to reporting requirements to take account of the new functions, there are no significant changes to the financial management and governance structures of the ASC; and

- Stage one is primarily a change of administrative arrangements as a significant first step toward substantive harmonisation of regulation in stage two.

3.50 The second stage will occur simultaneously with the transfer of prudential supervision of State/Territory-based institutions which, subject to State and Territory agreement, would occur as soon as possible after the establishment of APRA at the Commonwealth level. As part of the second stage, significant changes to national corporate regulation scheme laws would be required to accommodate the range of new functions in connection with institutions currently regulated at the State/Territory level. The second stage would also involve amendments to harmonise regulatory requirements between industry sectors in matters such as disclosure and licensing.

Development of harmonisation measures is already under way in the context of the Part 6 of the Corporate Law Economic Reform Program ('CLERP'), which is dealing with financial markets and investment products.

3.51 The second stage will also involve more significant administrative reforms for State and Territory-based financial institutions, particularly those regulated under the Australian Financial Institutions Code.

3.52 Since it is proposed that aspects of the regulation of the State-based institutions will be transferred to ASIC, there will need to be further amendments to the national corporate regulation scheme laws accordingly. There will also need to be amendments to the Corporations Agreement to take account of the functions transferred from States and Territories.

Review

3.53 Review and assessment of the success and appropriateness of these regulatory arrangements will be undertaken by various bodies.

- ASIC will be required to make regular, detailed public reports on its operations and sources and uses of funds and will also be answerable to the Parliament through the Treasurer as responsible Minister. This will not only enhance the accountability of ASIC, but will increase the degree of scrutiny on the effectiveness and continued relevance of its regulatory approach.

- The Treasury will continue to fulfil its role in advising the Treasurer on issues including the development, implementation and efficacy of policy in the financial sector.

- The Financial Sector Advisory Council (FSAC), an independent body reporting to the Treasurer, will conduct a review of the regulatory framework five years after the commencement of the measures.

- The regulatory framework will also be reviewed ten years after the commencement of these measures as part of the Commonwealth's Legislative Review Schedule.

Schedule 2 Amendments of the *Banking Act 1959*

3.54 This attachment contains four Regulation Impact Statements:

(a) single licensing and prudential regulatory regime for deposit taking institutions (DTIs);

(b) stability of the financial system and depositor protection;

(c) licensing and regulation of financial conglomerates; and

(d) non-callable deposits (NCDs)

Regulation Impact Statement 1- Single Licensing and Prudential Regulatory Regime for Deposit-Taking

Problem

3.55 The current system of licensing and conducting prudential regulation of deposit-taking is a source of considerable inconsistencies (non-neutrality) between institutions conducting essentially the same business. The current dual State/Commonwealth

system is costly, constrains innovation, confuses consumers, involves considerable duplication of resources in both regulation and licensing, results in slow decision making and hinders non-bank DTIs in their attempts to become national players thereby constraining competition and providing higher cost products and services to consumers than would otherwise be the case. In addition, the current system is inflexible in adapting to change in the financial system.

3.56 Also, the safety of deposits is lowered by excluding unlicensed non-bank DTIs from licensing and prudential regulation.

3.57 The FSI found that the average cost of the Australian banking system between 1986 to 1994 was in the middle of the range of developed countries, but at the upper end of that range. The FSI suggested that this may have been indicative of the unwillingness of some Australian banks to reduce costs due to a lack of competition.

3.58 Government action is required to reduce the costs of conducting prudential regulation and to address the non-neutralities inherent in a system where regulation of the same activity occurs at both the State/Territory and Commonwealth level. At present, however, the Commonwealth scheme for the regulation of DTIs covers only institutions able to be licensed as 'banks'. There is no scheme for federal regulation of non-bank DTIs, which must either operate on a restricted basis without regulation or fall under the State and Territory-based regulation as building societies or credit unions.

Regulatory Objectives

3.59 The purpose of prudential regulation is to:

- protect consumers of retail financial products by increasing the likelihood that a financial promise can be met; and

- limit systemic risk by minimising the risk of insolvency of financial institutions.

3.60 To achieve these objectives, prudential regulation imposes a variety of restrictions on the conduct of financial businesses. While these restrictions are aimed at reducing financial risks, they may also have adverse side effects on competition, regulatory neutrality (applying the same regulation to similar products) and efficiency. The objective of government action should be to reduce the adverse effects of prudential regulation on competition, competitive neutrality and efficiency while maintaining or improving upon the current level of safety and stability in the financial system thereby reducing the associated costs to the community and business.

Options

Status Quo

3.61 Banks are currently licensed under the *Banking Act 1959* (the Act) and regulated by the Reserve Bank of Australia (RBA). Many non-bank DTIs are incorporated under State and Territory statute, are licensed under the Australian Financial Institutions legislation (oversighted by the AFIC) and regulated by the relevant State Supervisory Authority (SSA).

Single Licensing and Regulatory Regime for Deposit-Taking

3.62 This option would adopt an 'objectives-based' or 'functional' approach to the licensing and prudential regulation of DTIs. This would be achieved by the establishment, under the Act, of a single regulatory and licensing regime for all DTIs.

Deposit-taking would also be prohibited unless undertaken by a licensed DTI or by an entity granted exemption by APRA.

Impact Analysis

Status Quo

3.63 The prudential regulation applied to different DTIs and deposit products, and public perceptions of their safety, will continue to vary considerably depending upon the structure of the deposit-taking entity or where it is incorporated. Under the status quo, the current 'institutional' approach to prudential regulation and licensing based on institutional types or labels (eg. bank, credit union, building society) would be retained.

3.64 The FSI found that a total of around 800 staff were employed in the regulation and supervision of the financial system in Australia in 1996. This compared with around 900, 1,400 and 1,500 staff fulfilling the same functions in Canada, UK and Germany respectively, although these countries have significantly larger financial systems. The FSI concluded that the costs of regulation in Australia are high by international standards, with some possible explanations being: the high standard of supervision in Australia; the costs associated with supervising compulsory superannuation; differences in regulatory approaches; the wide extent and overlap of regulation; and the existence of separate bodies undertaking similar regulation (regulatory fragmentation) which leads to duplication.

3.65 The status quo offers no improvements in efficiency, competition, regulatory neutrality, safety or stability from licensing and prudential regulation.

3.66 However, some sectors of the business community (particularly a number of the larger banks) may argue that the current system of prudential regulation has served the financial system and the wider community well with no major bank or insurance failures to date.

3.67 In addition, the RBA and the SSAs have built up considerable industry specific knowledge and expertise in the application of prudential regulation to those institutions they supervise. These arrangements, however, prevent the full consolidation, sharing and enhancement of particular expertise and corporate knowledge that could be achieved under a single regime for the licensing and regulation of DTIs.

3.68 The status quo will entrench the current (real and perceived) advantages conferred on banks as a result of being regulated by the RBA. State and Territory-based financial institutions will remain subject to varying regulation and consumers will continue to be denied the competitive benefits which would accrue from allowing more entities to compete in deposit-taking markets (greater contestability).

Single Licensing and Regulatory Regime for Deposit-taking

3.69 A single licence for all DTIs will enable regulation to be applied consistently across different entities accepting retail deposits (competitive neutrality) to achieve a minimum level of depositor safety. A single licensing and regulatory regime will, in turn, enable non-bank DTIs to operate on a national basis and compete on the same regulatory terms as deposit-taking banks. Greater competition by DTIs may lead to increased choice, improved quality and lower cost products and services for consumers in the medium term. As the financial system feeds into almost every area of economic activity, any reduction in the cost of financial services or improvements in quality and type of services offered will provide ongoing benefits to consumers and other sectors of the economy that use these services.

3.70 By providing APRA with powers over a broader range of DTIs, depositor protection may be increased as currently unlicensed deposit-takers are required to be licensed or apply for an exemption. The stability of the financial system is likely to increase to the extent that these entities are subject to greater scrutiny and regulation.

3.71 The proposed powers to prohibit any aspect of banking business would be general enough to enable APRA to take a flexible approach to licensing, especially as the financial system evolves and new ways of providing deposit-type services arise. It is not proposed to explicitly specify exemptions in the legislation in order to not compromise future flexibility.

3.72 A more flexible regulatory environment will enable APRA to respond quickly to significant change occurring in the financial system as a result of technology, innovation, financial conglomerates and globalisation (ie more dynamically efficient regulation). This will provide a real benefit to financial service providers and may reduce the incidence of instability in the financial system as the financial system evolves and the risks faced by financial entities change.

3.73 Consolidation of the regulatory regimes covering banks and non-bank DTIs currently performed by the RBA, AFIC and the supervisory and inspection roles carried out by the eight SSAs may lower the costs of prudential regulation without lowering the level of safety and, in some cases, increase the safety of deposits.

3.74 The FSI also considered that, historically, building societies and credit unions have been innovative in the development and delivery of financial services. It also argued that State and Territory-based DTIs are capable of increasing market contestability and providing greater choice to consumers. It concluded that the current system of regulation is constraining this innovation and preventing State and Territory-based DTIs from operating on a similar footing to deposit-taking banks, thus reducing their ability to compete on a national basis and be an effective source of competition for deposit-taking banks.

3.75 The facilitation of more equal competition and contestability (the threat that someone else could enter and compete in the market) in deposit-taking markets may result in resources being allocated more efficiently (allocative efficiency) in the financial system. This may also benefit consumers and other sectors in the economy.

3.76 Some banks may lose customers (and hence be critical of these measures) as a result of the greater competition flowing from State and Territory-based institutions and the loss of some of their "special" status in the deposit-taking market.

3.77 The public may perceive that exempt DTIs are subject to the same degree of regulation as licensed DTIs. This risk could be minimised by the disclosure requirements under the Corporations Law.

3.78 Giving general powers may create uncertainty over the treatment of existing unlicensed deposit-takers. The existing exemptions for money market corporations (with respect to banking), the taking of deposits under a prospectus and restricted deposit-taking, such as by pastoral finance companies, would be continued but may be reviewed if the entities' circumstances change.

3.79 There may be some direct employment effects of increasing the degree of competition between DTIs. These effects are likely to be small.

3.80 In the short term, there may also be some transitional costs involved in transferring State and Territory-based DTIs to the Commonwealth level and consolidating State, Territory and Commonwealth regulatory bodies. However, the

ongoing cost savings flowing from consolidated regulation should eventually offset these transitional costs.

3.81 The net cost to the Government would be negligible as financial enterprises will be charged a levy to fund, as far as practicable, the establishment of the new regulator and the ongoing costs of prudential regulation. The costs of amending the relevant legislation are minimal.

Consultation

3.82 The main consultation process was undertaken by the FSI. The FSI received a total of 421 submissions, including 153 submissions responding to a Discussion Paper published by the FSI in November 1996. These submissions were prepared by a broad cross-section of industry participants and other interested individuals, corporations and groups. The FSI held public consultations in all mainland capital cities during December 1996, and met with a range of financial industry experts and participants, regulatory agencies and consumers, both in Australia and overseas. The FSI also participated in a range of conferences and seminars, and had a home page on the Internet.

3.83 In the preparation of the Government's response, the Treasury consulted with the Attorney-General's Department, the Department of Finance and Administration, the Department of Prime Minister & Cabinet and the Department of Industry, Science and Tourism, and with the affected regulators, namely the RBA, the ISC and the ASC. The regulators and key industry bodies were consulted on the proposed legislative changes.

3.84 During the FSI process, the vast majority of submissions supported banks, building societies and credit unions being regulated by the same regulator. Credit Union Services (Australia) Limited (CUSCAL), the National Credit Union Association and the Australian Association of Permanent Building Societies (AAPBS) expressed the strong desire of their members to be regulated at the Commonwealth level on the same basis as deposit-taking banks.

3.85 State and Territory Government agreement is not necessary for the establishment of a prudential regime at the Commonwealth level which encompasses non-bank DTIs. State/Territory agreement would, however, be required for the full transfer of responsibility for building societies and credit unions to the Commonwealth sphere. Negotiation on the proposed transfer of responsibilities is to occur in a two stage process with the first stage seeking in principle agreement. Stage two will require joint Commonwealth-State and Territory working parties to settle matters of policy and administrative detail necessary to implement the changes. It is anticipated that full implementation will be completed if possible by the end of 1998 or soon after.

Conclusion and Recommended Option

3.86 The preferred option is the establishment of a single licensing and prudential regulatory regime. This would result in a more neutral, flexible, efficient (technical, allocative and dynamic) and simple approach to regulation than the status quo. Increasing the powers of the prudential regulator over the general business of deposit-taking would result in the greatest improvement in depositor protection and system stability. In addition, unnecessary regulation can be avoided by APRA having the power to exempt DTIs on a case-by-case basis.

Implementation and Review

3.87 Ongoing review and assessment of the success and appropriateness of these regulatory arrangements will be undertaken by various bodies.

- APRA will be governed by a Board which will be responsible for ensuring that it performs in accordance with its charter, balancing efficiency, competition and stability objectives. It will be required to make regular, detailed public reports on its operations and sources and uses of funds, will be answerable to the Treasurer as responsible Minister and will be subject to budget scrutiny. This will not only enhance the accountability of the prudential supervisor, but will increase the degree of scrutiny on the effectiveness and continued relevance of its regulatory approach.

- The Treasury will continue to fulfil its role in advising the Treasurer on issues including the development, implementation and efficacy of policy in the financial sector.

- The Financial Sector Advisory Council (FSAC) will conduct a review of the regulatory framework five years after the commencement of these measures.

- The regulatory framework will also be reviewed ten years after the commencement of these measures as part of the Commonwealth's Legislative Review Schedule.

Regulation Impact Statement 2 Stability of the Financial System and Depositor Protection

3.88 The potential for market failure provides a role for government in protecting depositors and investors in the financial system. Market failure in the financial sector may result from significant information asymmetries (between institutions and the general public) or concerns relating to systemic risk and the impact that the failure of an institution (and possibility of contagion effects on other financial institutions) would have on the real economy. This regulation impact statement relates to the stability of the financial system and the protection of depositors and investors within that system. It deals with the proposal to clarify current legislation and strengthen the role of the regulator to act in the interests of depositors.

Problem Identification and Regulatory Objectives

3.89 There are two general problems with the current state of regulation for depositor protection:

- A lack of clarity regarding the extent to which deposits are protected and the moral hazard problem (whereby depositors, believing their funds are guaranteed, seek out the highest return without regard to risk) this induces in the behaviour of depositors. The current regulations are ambiguous in nature and lack transparency.

- Concerns that in an era of constant change and increasing globalisation and competition, the powers of the prudential regulator to protect deposits should be updated to allow for earlier intervention, clearer mechanisms for intervention and increased flexibility in the options available for it to act in the interests of depositors.

3.90 The regulatory objectives are to achieve:

- effective levels of depositor protection, consistent with the need to increase competition in the financial system, while minimising moral hazard and ensuring that the regulatory impact is neutral in other respects; and

- clarity in the minds of depositors regarding the extent to which their deposits are protected.

Identification of alternatives

Retention of the Status Quo

3.91 Currently the RBA is responsible for depositor protection in the banking sector. Depositor protection is achieved by the RBA's ability to assume control of a troubled bank and by ranking depositors ahead of other creditors (ie depositor preference) in the event of bank failure.

3.92 The current legislative basis for depositor protection is embodied in Division 2 of the Act. Section 12 of the Act requires the RBA to exercise its powers for the protection of depositors and section 16 gives priority to deposit liabilities above other liabilities. Section 14 provides triggers for management intervention by the RBA and allows the RBA to assume control of a bank. Although such action is in part discretionary (the RBA is required to act in the interests of depositors), once taken, the RBA under subsection 14(5) must remain in control and carry on the business of the bank at least until such time as 'the deposits with the bank have been repaid or the Reserve Bank is satisfied that suitable provision has been made for their repayment'.

Deposit Insurance

3.93 A number of overseas countries rely on deposit insurance as the focal point of their depositor protection regime. Deposit insurance provides clearly identified depositor protection in the event of the failure of an institution. It could replace the depositor preference element of the current regulatory regime.

3.94 There is, however, a wide variety of such schemes in operation, with no agreement on which approach works best. Illustrating this point, deposit insurance schemes may:

- be government funded or industry funded;
- be funded in advance or rely on levies once a problem has been identified;
- be based on levies that are adjusted for risk or based on a flat-rate premium;
- be compulsory or voluntary;
- enforce an upper limit (cap) on insured amounts; and
- involve additional layers of regulation.

Retention of the Present Protection Arrangements with Some Consolidation and Clarification

3.95 This option builds upon the existing depositor protection arrangements, but with some clarification and adjustment to correct the perceived deficiencies in the current regulation. It accepts that the general thrust of the current approach is appropriate but that there is a need for improvement.

3.96 The reforms envisaged in this option retain the current depositor preference regime but:

- amend the current provisions to strengthen the role of the prudential regulator to act swiftly and with a range of options to better protect the interests of depositors;
- better define and extend the existing mechanisms for exercising regulatory control; and

- clarify the extent of protection offered to depositors and investors.

3.97 Specifically, this option would:

- provide the prudential regulator with additional powers to direct the operations of a DTI or suspend any or all of its business activities if, in the opinion of the regulator, such action is in the interests of depositors or if the institution has materially failed to comply with prudential regulations or standards;

- define statutory management powers which enable the regulator to replace the board when taking control and to act surely without intervention arising from external administrators or civil legal proceedings (subject to appropriate safeguards); and

- amend the *Banking Act 1959* to give the prudential regulator the discretion to seek a winding up order where an institution is not solvent and could not be restored to solvency within a reasonable period of time.

Remove Explicit Depositor Protection Provisions Entirely

3.98 The explicit depositor protection provisions could be removed completely and replaced by a reliance on information disclosure. New Zealand is the only developed country to have substantively taken this path.

Industry Self-regulation

3.99 It is possible to conceive of a self regulatory approach to depositor protection but there would be no real benefit to industry or consumers and there would be considerable practical difficulties.

Impact Analysis

Retention of the Status Quo

3.100 While existing arrangements may provide a reasonably effective degree of depositor and investor protection, they have never been tested in practice and do not address the concerns detailed above.

Deposit Insurance

3.101 Given such a range of options and with no consensus approach internationally, the specific elements of any such deposit insurance scheme would require careful consideration.

3.102 The FSI considered the option of deposit insurance for Australia, but rejected it since it was not convinced that it would provide a substantially better approach compared with existing depositor protection arrangements.

3.103 While deposit insurance makes clear the degree of depositor protection available, it does little to prevent a run on a troubled institution. This is particularly so if any attempt is made to narrow the scope of 'insured' deposits to increase the extent of retail deposit protection (eg by restricting the insurance provisions to retail accounts). Such action would simply heighten the risk that deposits outside the definition will become 'hot' money, depleting liquid assets in difficult times, to the detriment of retail investors. In turn, this could contribute to increased instability of the financial system generally.

3.104 Furthermore, deposit insurance can exacerbate the moral hazard problem. Overseas experience suggests that in the long run badly designed deposit insurance may raise the probability and cost of instability by weakening the incentive structure.

3.105 Another concern is the expectation that the Government would underwrite any such scheme. Even where schemes have been 'totally' industry funded, instances exist overseas whereby governments have had to step in to plug a shortfall to maintain confidence and or stability in the financial system.

3.106 The FSI noted that experience of the failure of the savings and loan insurance scheme in the United States has created public resistance to the concept in Australia.

Retention of the Present Protection Arrangements with Some Consolidation and Clarification

3.107 This option provides strong grounds for both earlier and more flexible regulatory intervention than is currently the case, where this is in the interests of depositors.

3.108 International experience shows that the early resolution of failure is the most effective way of avoiding depositor losses. In some countries, (eg the USA and Canada) the requirement for early action has been legislated.

3.109 The increased flexibility is an important element given the current dynamic nature of the financial system and may be particularly relevant in the management of financial conglomerates.

3.110 Increased depositor protection through stronger and better defined powers will help to provide an additional safeguard against any detrimental effects from globalisation and increased competition as the financial sector is liberalised further. This is likely to lead to increased depositor confidence in the stability of the financial sector.

3.111 Providing for the early wind up of an enterprise could prevent further losses for depositors while clarifying that deposits are not guaranteed. This approach gives the prudential regulator substantial flexibility to protect depositors as much as possible but also to terminate efforts once they have reached a point where further protection is not feasible.

3.112 By making it clear that deposits continue to be subject to preference, but are not guaranteed, the ambiguity of the existing regulation is removed and its transparency increased. Importantly this will serve to decrease the extent of moral hazard from current levels. Some consumers may oppose this outcome.

3.113 There are no expected Commonwealth revenue impacts of these reforms the day-to-day role of the prudential regulator is not being altered. No new requirements are being placed on the day-to-day operations of the financial institutions.

Remove Explicit Depositor Protection Provisions Entirely

3.114 In brief, this approach would create a significant burden on: the Government to detail and enforce the degree of disclosure required; financial institutions to comply with the disclosure 'rules'; and consumers to access and investigate the information regarding the investment opportunities available to them. While it would remove the moral hazard problem, it may unduly increase the risk of instability in the financial system - customers may be less confident in the financial system. This could heighten concerns relating to systemic risk and increase the fragility of the economy to economic shocks and shifts in sentiment.

Industry Self-regulation

3.115 Because self-regulation would be unlikely to provide acceptable levels of confidence in DTIs, industry does not want it and the community would be unlikely to regard it as an acceptable approach. Moreover, there are no real public cost implications of current policy because deposits are not guaranteed. From a practical point of view, it would also be very difficult to secure industry-wide agreement because stronger institutions would resist proposals to provide protection to the deposits of those institutions that they perceive to be weaker or more at risk.

Conclusion and Recommended Option

3.116 While retaining the status quo is a viable option, it does not address the current concerns, which are shared by large numbers of smaller financial institutions. These concerns may be heightened by their entry to the Commonwealth's regulatory sphere. There is scope to enhance the current approach to remove present uncertainties relating to the degree of depositor protection and provide additional powers for the regulator to intervene in the interest of depositors. The case for rejecting the general thrust of the current approach has not been clearly demonstrated. For this reason, and due to their risks and costs, the second, fourth and fifth options can be rejected.

3.117 The third option builds on the current approach, addressing the flaws contained therein and is therefore the recommended option.

Administrative Simplicity, Economy and Flexibility

3.118 The depositor protection reforms provide simple methods for intervention, employ Corporations Law processes for winding up an institution and approaches modelled on the AFIC scheme for regulatory intervention. Additional powers for early intervention may prevent the need for more costly control measures and increase the flexibility of crisis management regulation.

Consultation

3.119 Submissions to the FSI relating to depositor and investor protection arrangements, especially those under the Banking Act, expressed a mixture of views.

- Some supported the thrust of the existing arrangements.

- Others advocated extension of the arrangements to other deposit-taking institutions.

- Finally, some submissions argued that depositor protection schemes be limited.

3.120 In general, however, a common theme amongst submissions to the FSI was that the current depositor protection arrangements should be clarified.

3.121 Submissions generally had little to say on the issue of deposit insurance. Most of the submissions which did address the issue opposed the introduction of deposit insurance on the basis that it would:

- create adverse incentives for depositors and management of institutions;

- involve difficulties in setting premiums relating to risk; and

- increase moral hazard.

3.122 In the round of discussions after the Final Report of the FSI was released and again following the Government's announced response to the report, there appears to be general consensus that the recommendations offered in the above discussion amount to a suitable and appropriate course of action. The Commonwealth regulator most affected by the proposed changes to depositor and investor protection, namely the RBA, has been given the opportunity to comment on draft legislation and its comments have helped shape the Bill.

3.123 In the preparation of these reforms, the Treasury consulted with the Attorney-General's Department, the Department of Prime Minister & Cabinet, the Department of Industry, Science and Tourism, and with the affected regulators, namely the RBA, the ISC and the ASC. The Treasury has also participated in some further discussions with industry bodies representing banks, building societies and credit unions.

3.124 There have been some discussions with the States and Territories and further discussions will be held regarding full implementation of the reforms.

Review

3.125 The adoption of an objectives-based approach to regulation (as embodied in the recommendations proposed above) provides the flexibility necessary for regulation to remain relevant in a sector undergoing constant change. Formal reviews after 5 and 10 years will, however, also be undertaken as outlined in the single licensing regime Regulation Impact Statement (RIS).

Regulation Impact Statement 3: Facilitation of Non-Operating Holding Companies and Multiple Bank Licences

Problem

3.126 Currently the Banking Act does not facilitate the use of non-operating holding company (NOHC) structures for the ownership of banks and other financial entities. In addition, the RBA has prohibited financial groups from holding more than one bank or deposit-taking entity licence.

3.127 The financial conglomerates initiative is designed to address inflexibility in the financial system that prevents both the formation of financial conglomerates that would be in the public interest and financial conglomerates holding more than one licensed bank or DTI.

3.128 Government action is needed as the current regulatory regime is responsible for this problem by placing excessive restrictions on the structure of, and licences held by, financial conglomerates.

Regulatory Objectives

3.129 The Government's regulatory objective in acting would be to regulate financial conglomerates in a way that minimises the chances of both systemic risk and possible conflicts of interest within the group without unduly interfering in the commercial decisions of the group.

Options

Status Quo

3.130 Banks or insurance companies would have to remain the ultimate holding company, removing any potential for beneficial regulatory arbitrage. Financial groups

would continue to be prohibited from holding more than one bank or deposit-taking entity licence.

Non Operating Holding Companies and Multiple Bank and Deposit-Taking Licences

3.131 Financial conglomerates could be allowed to adopt a non-operating bank or deposit-taking holding company structure, subject to the conglomerate meeting various prudential requirements. The NOHC may be required to be licensed. Financial conglomerates would also be allowed to hold more than one licensed bank or deposit-taking entity.

Impact Analysis

Status Quo

3.132 The inability of financial conglomerates to use NOHC structures, where a bank is involved, has provided a high level of depositor protection and stability in the financial system. The current arrangements may, however, have unduly interfered with the commercial decision making of conglomerates. By restricting the structure, financial conglomerates may have been forced to adopt less efficient structures and denied some possible benefits of using differences in the costs of regulation between products (regulatory arbitrage) thereby raising costs. As a consequence, these costs may have been passed on to consumers in the form of higher prices and lower returns for financial products and services.

3.133 The prohibition of multiple licences has ensured that depositors are treated equitably in the event of a wind up of a failed financial institution. Financial entities, though, have been prevented from pursuing legitimate commercial practices that require holding more than one bank or deposit-taking licence.

Non-Operating Holding Companies and Multiple Bank and Deposit-Taking Licences

3.134 Under this option, financial conglomerates would have greater commercial freedom in selecting their appropriate structure and number of licences. Allowing the use of NOHC structures will reduce barriers to entry and may result in a more competitive financial system. Entities may be able to provide a wider range of financial services, face reduced regulatory costs and use more efficient corporate structures thereby providing ongoing benefits to consumers and users of financial services in the form of lower cost and more competitive financial products.

3.135 Applications will be considered on a case-by-case basis, however, to ensure that prudential standards are not compromised and depositors and investors are treated equitably in the event of a wind up.

3.136 Requiring the conglomerate to satisfy certain prudential requirements by licensing NOHCs may provide a more transparent mechanism to regulate financial conglomerates thereby improving safety. A possible cost associated with this approach is that the public may perceive that all of the financial entities in the conglomerate are prudentially regulated which need not necessarily be the case.

3.137 As APRA will take a flexible approach to licensing of NOHCs, it is not envisaged that the licensing process will create inappropriate barriers to entry and exit.

3.138 Allowing financial conglomerates to hold more than one class of financial licence would enable greater commercial freedom in decision making by these entities without resulting in a proliferation of licences.

3.139 The net cost to the Government of acting would be negligible as financial enterprises would be charged a levy to fund, as far as practicable, the costs of prudential regulation. The costs of amending the relevant legislation are minimal.

Consultation

3.140 There is widespread industry support for allowing the establishment of a NOHC structure with operating subsidiaries, such as banks and insurance companies.

3.141 Industry groups are also in favour of the proposal to allow conglomerates to hold more than one authorised deposit-taking institution (ADI) licence.

3.142 See consultation in single licensing regime for general consultation process.

Conclusion and Recommended Option

3.143 Maintaining the status quo would maintain stability and depositor protection while restricting flexibility in commercial decision making.

3.144 Allowing both NOHCs, where a bank or DTI is present, and financial groups to hold multiple licences, where appropriate, has the potential to increase commercial freedom in decision making, increase competition and lower costs for financial conglomerates (and thus consumers of financial products) without a significant change in stability and the level of depositor protection.

3.145 On balance, the preferred option is to allow NOHCs, where a bank or DTI is present, and to allow financial groups to hold multiple licences in order to enable greater commercial flexibility while still ensuring that conglomerates meet prudential standards.

Implementation and Review

3.146 Please see single licensing regime for general implementation and ongoing review processes.

Regulation Impact Statement 4: Future of Non-Callable Deposits

Problem

3.147 Under the Act, the banks are required to hold one per cent of eligible liabilities with the RBA as NCDs. Interest currently paid to the banks on these deposits is generally at a rate 5 percentage points below the prevailing market rate. Interest rates have been varied from time-to-time by the RBA. The current rate, which came into effect in May 1995, was justified 'as a payment for the benefits which accrue to banks from being authorised by the Government and subject to RBA supervision'.

3.148 NCDs impose a significant cost on the banking system. Furthermore, as the funds raised greatly exceed the cost of prudential regulation of banks, this excess charge represents a considerable regulatory distortion between banks and non-bank DTIs with implications for the efficiency of the financial system.

Regulatory Objectives

3.149 As the only residual justification for the NCD requirement appears to be as a funding mechanism, its future must be considered against the background of the broader funding issue outlined above that industries should pay only the costs of their supervision. The objective is to remove the regulatory distortion created by the current imposition of NCDs.

Options

Abolition of NCDs

Extension of NCDs to other dtis

Impact Analysis

Abolition of NCDs

3.150 The RBA has advised that there is no prudential rationale for the continued imposition of NCD requirements. The funding role would disappear with the transfer of prudential regulation of banks to APRA. The abolition of NCDs would satisfy the stated regulatory objectives of minimising the cost of regulation and competitive neutrality. The decline in net revenue earned from NCDs would, however, affect the RBA's income and, as such, the Budget. Nevertheless, to continue the use of NCDs on revenue grounds would effectively mean the imposition of a discriminatory and inefficient tax.

3.151 While the banks would be clear beneficiaries of any abolition of NCDs, the extent to which bank customers would benefit would depend on competitive pressures in the industry.

Extension of NCDs to other dtis

3.152 An alternative approach might be to extend NCDs to all other DTIs, with the objective of achieving some element of competitive neutrality. This option, however, would appear to have only an attraction from a revenue raising perspective and would do nothing to provide a means of funding for APRA; it would be in addition to it. Furthermore, an extension could not only seriously undermine the possibility of establishing a rational funding mechanism, but could also discourage other DTIs from participating in the new prudential framework.

3.153 A variation of the extension option would be to pay the full market interest rate on the first $10 million of NCDs. This would effectively exempt most non-bank DTIs from the NCD revenue charge because they are too small to have NCDs above $10 million. Similarly, there would be a $500,000 p.a. benefit to banks which would largely offset the impact of new APRA regulation fees. While this would remove some of the more undesirable features of the original version of this option, the fact remains that, with prudential regulation moved to APRA, there is no reason to maintain NCDs.

Consultation

3.154 See consultation for single licensing regime.

Conclusion and Recommended Option

3.155 Retention of NCDs, whether extended to other DTIs or not, would involve maintaining an anachronism, which would undermine efforts to develop an efficient and simple funding mechanism for APRA. Abolition of NCDs is, therefore, supported.

Implementation and Review

3.156 The adoption of an objectives-based approach to regulation (as embodied in the recommendations proposed above) provides the flexibility necessary for regulation to remain relevant in a sector undergoing constant change. An important implication of a flexible regime is that it significantly reduces the need to establish, at the outset, a

timetable for a formal review. For this reason, and in conjunction with the additional safeguards discussed below, no formal review is proposed for the immediate future. The level of the levy will, by necessity, be the subject of annual review and will require the Treasurer's approval for the rate set.

3.157 For general implementation and review processes please see implementation and review in the single licensing regime RIS.

Schedule 13 (Part 7) - Amendments to the *Life Insurance Act 1995*

Problems

3.158 The *Life Insurance Act 1995* (LIA) establishes a scheme of prudential supervision for the life insurance industry. The LIA came about following a major review of its predecessor, the *Life Insurance Act 1945*. It is administered by the Insurance and Superannuation Commission. Two problems have been identified with the scheme.

3.159 First, the existing shareholder minimum capital requirement provisions of the LIA are being interpreted by some insurers in a way which is inconsistent with the original intentions behind the provisions. As a consequence, some insurers are maintaining unsatisfactory levels of capital. The original intention of the LIA was that at all times a life company shareholders' fund would have paid up share capital of at least $10 million. Further, at least $5 million would be secured by eligible assets in excess of liabilities. To satisfy these requirements simultaneously it was intended that the company would effectively have to have at least $10 million net assets in the shareholders' fund at all times. Due to the wording of the relevant enabling provisions there is some uncertainty as to whether the LIA gives full effect to these intentions. Some insurers have expressed the view that the respective provisions are open to the interpretation that the capital requirements are complied with in a situation where the net asset position of the shareholders fund is less than $10 million but greater than $5 million. This was not the intention.

3.160 The second problem concerns the inability of a life insurer, because of existing statutory provisions, to charge assets of a statutory fund for purposes of entering into relevant derivatives transactions.

Objectives

3.161 The objective in relation to the first problem is to ensure that the interests of policy owners are adequately protected. A key prudential means for achieving this is to ensure that companies who conduct insurance business are companies of financial substance, able to withstand severe business fluctuations, and that shareholders have a financial commitment to the success of the business.

3.162 The objective in relation to the second problem is to ensure that while regulation adequately protects the interests of insurance policy owners it does not unnecessarily interfere with or restrict the business activity of the insurer.

Options

Option 1: Amend the LIA to give effect to measures which would overcome the problems.

Option 2: Take no action to overcome the problems.

Option 3: Overcome the problems by means of education (including guidelines or circulars).

Impact Analysis

Impact Group Identification

3.163 Groups likely to be affected by the proposed amendments include: all life insurers; prospective and existing life insurance policy owners; competitors of life insurers; and APRA.

Assessment of Costs and Benefits

3.164 Two problems are identified. Each is discussed below.

(i) Differing Capital Levels Being Maintained By Insurers.

Option 1 (regulation):

3.165 This option proposes that the relevant provisions of the legislation be amended to reflect the original intent of the LIA. A major benefit of this option is that it would establish certainty and ensure that all insurers provide adequate shareholder commitment to the effective operations of the life company and that additional financial support will ultimately be available to the statutory funds, should this prove necessary, to ensure the interests of policy owners are protected. It would produce consistency and a level playing field across the industry in terms of (minimum) shareholder capital requirements. Consumers and their advisors, in selecting an insurer with whom to place business, could be confident that all insurers were subject to the same minimum capital requirements. The option may also result in some decrease in regulator costs as the maintenance of a minimum $10 million net asset position by all companies would ease the need for close regulatory scrutiny of those companies who were previously maintaining less than that amount.

3.166 In terms of costs, the major potential cost of Option 1 would be for those insurers who are currently interpreting the legislation so as to maintain a lower level of net assets (between $5 million and $10 million). These insurers would have to increase their net assets by a relevant amount (potentially up to $5 million although in practice most are already significantly above the $5 million minimum net asset level and therefore the increase would be less than $5 million). There are not expected to be more than 10 such insurers on the basis of analysis conducted by the ISC in mid-1997. It should be noted, however, that in practical terms the cost is likely to be in the nature of an opportunity cost rather than a direct cost as insurers generally have access to sufficient funds, either within the company itself (such as surplus assets in its statutory funds) or elsewhere in the company grouping.

3.167 A potential cost of Option 1 for the community is that some insurers could decide not to continue business if required to maintain net assets of $10 million, thereby reducing competition. However, a circular sent to each insurer by the ISC in November 1997 seeking an indication as to whether the insurer would have difficulty in meeting a $10 million net asset requirement has, to date, elicited no response. On the basis of this feedback and consultations the ISC has had with insurers it is extremely unlikely that any insurer would withdraw from the market as a result of this measure.

3.168 However, even if there were one or two withdrawals, the industry would still comprise more than 50 insurers, making the possibility of a diminution in competition remote.

Option 2 (no action):

3.169 The major cost of not taking any action to address the problem, would be that some insurers would continue to maintain amounts of shareholder capital that are considered insufficient to provide a prudential level of protection to the interests of policy owners.

3.170 A further possible cost of this option is that it may result in increased regulatory costs as the regulator intensifies its attention on those insurers maintaining the lower capital levels. As well, there may be increased costs for prudent consumers and their advisors as they undertake a process of ascertaining the capital levels being maintained by individual insurers before placing insurance. On the benefit side, the opportunity for the existing provisions to be interpreted so as to require a lower level of capital than that originally intended may entice newcomers into the market, thereby increasing competition and potentially producing consumer benefits in terms of price reductions and product innovations. As well, insurers would continue to have the option of maintaining lower amounts of capital in their insurance business and could employ that capital elsewhere.

Option 3 (education):

3.171 Using means such as guidelines or circulars to address the problem would produce costs and benefits similar to that for option 2. That is, as there would be no legal obligation on insurers to follow the guideline or circular the existing situation would largely continue.

(ii) Reduction in current restrictions relating to charging of assets.

Option 1 (regulation):

3.172 Section 40 of the LIA severely restricts the extent to which a registered life insurer may charge or mortgage an asset of a statutory fund. In particular, the prohibition effectively prevents a life insurer from engaging in the internationally accepted practice of lodging cash or share scrip with a broker on a recognised trading exchange as collateral to meet obligations associated with derivatives transactions entered into on behalf of the life company. Under this option, the legislation would be appropriately amended to enable an insurer to charge assets of a statutory fund for purposes of entering into relevant derivatives transactions.

3.173 The prohibition, by restricting the ability of the insurer from using derivatives transactions to manage risks to which the statutory fund may be exposed (eg market risk, currency risk), may not be in policy owners best interests. Thus, under option 1 both the life insurer and policy owners potentially benefit. On the cost side, there is the potential that proceeding with the amendment could pose some prudential risk in that improperly managed derivatives transactions may expose statutory funds to additional loss. However, it is proposed that the amendment will include a regulation power to allow APRA to set appropriate conditions to ensure prudential risk is minimised. This would impose some regulatory cost in terms of establishing and monitoring compliance with conditions but it would be relatively minor and outweighed by the potential benefits to insurers and policy owners.

Option 2 (no action):

3.174 Under this option, the status quo would remain. There is little benefit in this option except to the extent that minor additional regulatory processing may be saved, however it would be at the cost of the potential benefits to both the insurer and policy owners (better management of risks).

Option 3 (education):

3.175 Since the prohibition on charging of assets is enshrined in existing primary legislation (that is, section 40 of the LIA) option 3 is not a workable way in which to solve this problem.

Consultation

3.176 The Investment and Financial Services Association Ltd (IFSA), the industry body for life insurers, has recently been consulted on the proposed measures and in their response foreshadowed no significant concerns with them.

3.177 In regard to the first problem (ie, minimum capital requirements), extensive consultation took place with interested parties, including the industry body and individual insurers, during the formulation of the LIA. Further consultation has taken place with various individual insurers on a number of occasions since the LIA's enactment (in 1995). In November 1997 the ISC sent a circular to all insurers that advised of the ISC position in regard to the LIA s capital requirement provisions and requesting all life companies comply with intent of the LIA by their next balance date. The circular invited feedback from any insurer who would have difficulty complying with that proposal. To date, no responses have been received.

Conclusion and recommended option

3.178 In respect to the capital requirements, given the importance of capital as a fundamental prudential means of safeguarding the interests of life insurance policy owners, Option 1 is the preferred option. This option will give effect to the original intentions relating to the LIA's capital requirements and establish certainty and consistency in the legislation. Insurers have been aware of the intended capital requirement for many years through various ISC written and verbal communications. As a consequence, most insurers already comply and of the few who don't none have indicated an inability to comply. The IFSA has not raised concerns about any costs of compliance. The potential benefits of Option 1 in terms of policy owner security far outweigh the costs, which are mainly in the form of opportunity cost to insurers. Option 2 would perpetuate the present uncertainty in relation to the relevant provisions, an undesirable regulatory situation reducing policy owner protection. It is not recommended. Option 3, using education to overcome the problem, has actually been practiced by the ISC since the problem first became known. However, as there is no legal obligation for insurers under this option, this option has the same disadvantages as Option 2, and is also not recommended.

3.179 In respect of expanding the scope for life insurers to charge assets of a statutory fund (to include derivatives transactions), Option 1 is recommended. It will give greater flexibility to operations of life insurers whilst continuing to ensure adequate consideration is given to the interests of policy owners. Option 2 is not recommended as it would continue to require life insurers to manage risks in a less efficient manner than would otherwise be possible.

Implementation & Review

3.180 Regulation of life insurance was the subject of a major review in the early 1990 s. Subsequent to that review, the life insurance legislation at the time (that is, the Life Insurance Act 1945) was repealed and replaced by the current LIA. The LIA is the subject of ongoing review by the ISC to ensure its continuing efficiency and effectiveness in light of trends and developments in the marketplace and the community. This review will be continued by APRA.

Explanation of Items

Formal Clauses

Clause 1 - Short Title

The Short Title of the Bill is defined here.

Clause 2 - Commencement

Commencement as provided for in individual Schedules.

Clause 3 - Schedule(s)

Schedule 1 - Amendment of the Australian Securities Commission Act 1989

Schedule 2 - Amendment of the Banking Act 1959

Schedule 3 - Repeal of the Banks (Shareholdings) Act 1972

Schedule 4 - Amendment of the existing Corporations Law

Schedule 5 - Amendment of the Corporations Law as proposed to be amended by the Company Law Review Act 1998

Schedule 6 - Amendment of the Corporations Law as proposed to be amended by the Managed Investments Act 1998

Schedule 7 - Amendment of the Financial Corporations Act 1974

Schedule 8 - Amendment of the Insurance Acquisitions and Takeovers Act 1991

Schedule 9 - Amendment of the Insurance Act 1973

Schedule 10 - Amendment of the Insurance (Agents and Brokers) Act 1984

Schedule 11 - Repeal of the Insurance and Superannuation Commissioner Act 1987

Schedule 12 - Amendment of the Insurance Contracts Act 1984

Schedule 13 - Amendment of the Life Insurance Act 1995

Schedule 14 - Amendment of the Reserve Bank Act 1959

Schedule 15 - Amendment of the Retirement Savings Accounts Act 1997

Schedule 16 - Amendment of the Superannuation Industry (Supervision) Act 1993

Schedule 17 - Amendment of the Superannuation (Resolution of Complaints) Act 1993

Schedule 18 - Amendment and repeal of other Acts

Schedule 19 - Transitional Provisions

Explanation of Items

Schedule 1 Amendment of the Australian Securities Commission Act 1989

The purposes of Schedule 1 are to change the name of the Australian Securities Commission, to provide it with additional functions, particularly in relation to the consumer protection and market integrity aspects of insurance and superannuation regulation, and to make certain ancillary amendments to the *Australian Securities Commission Act 1989* (the Act).

In brief, the Act establishes the Australian Securities and Investments Commission (and certain other bodies under the national companies and securities scheme), provides its investigatory powers in relation to matters under that scheme and includes certain related matters.

Commencement

5.1 Schedule 1 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Change of Name of the Australian Securities Commission

Items 1, 4, 6, 7, 8, 33, 34

5.2 From the date of commencement of this schedule, the Australian Securities Commission is to be known as the Australian Securities and Investments Commission (item 8).

5.3 This change of name indicates the new functions which the Commission will acquire - at this stage, in relation to insurance, superannuation and the payments system but, subject to agreement being reached with the States and Territories, further functions may be added in relation to building societies, credit unions and friendly societies.

5.4 The body corporate established by the *Australian Securities Commission Act 1989*, however, will continue in existence.

5.5 The changed name is substituted in the short title of the Act (items 4; 33; 34).

5.6 The long title of the Act is amended consistently with this change (item 1) and a new definition of Commission inserted (item 7). A definition of APRA is also inserted (item 6).

The new functions

Item 10

5.7 The new functions and powers of the Commission are referred to in proposed section 12A (Item 10).

5.8 In brief, they are:

- the functions of the Insurance and Superannuation Commissioner under the *Insurance (Agents and Brokers) Act 1984*, the *Insurance Contracts Act 1984* and the *Superannuation (Resolution of Complaints) Act 1993*;

- certain functions and powers of the Insurance and Superannuation Commissioner under the *Insurance Act 1973*, the *Life Insurance Act 1995,* the *Retirement Savings Accounts Act 1997* and the *Superannuation Industry (Supervision) Act 1993*.

Administrative responsibility for these four Acts will be divided between APRA and ASIC. Those functions which relate to prudential supervision of the relevant bodies will be performed by APRA while those functions which relate to consumer protection and market integrity will be performed by ASIC.

5.9 In accordance with the Government's response to the recommendations of the Financial System Inquiry, the Commission will also be given the function of monitoring and promoting market integrity and consumer protection in relation to the payments system (proposed subsection 12A(3)). This function was previously undertaken by the Australian Payments System Council which is to be disbanded.

5.10 Proposed subsection 12A(5) also empowers the Commission to make recommendations to the Minister, including in relation to law reform, within the scope of ASIC's superannuation and insurance responsibilities. This is consistent with section 11 of the Act, which describes the functions and powers of the Commission in relation to the national companies and securities scheme.

5.11 The amendments to the individual Acts to effect this transfer of responsibility are included in Schedules 9-10, 12-13 and 15-17 of this Bill.

The new functions and the national companies and securities legislative scheme

Items 5, 15 and 29

5.12 The Act forms part of the legislative structure of the national companies and securities scheme.

5.13 The national companies and securities scheme involves:

- the enactment by the Commonwealth of the *Corporations Act 1989* (which includes the Corporations Law) and the *Australian Securities Commission Act 1989* as laws for the Australian Capital Territory;

- the automatic application of the Commonwealth Corporations Law and the relevant provisions of the *Australian Securities Commission Act 1989* as the law of each State and the Northern Territory; and

- its administration by the ASC and its enforcement on a national basis.

5.14 In contrast, the superannuation and insurance legislation, parts of which the ASC is to administer, are enacted by virtue of Commonwealth constitutional power to apply of their own force across Australia.

5.15 It is therefore desirable that the amendments relating to the new functions do not form part of the applied laws regime and do not apply in relation to the ACT as a part of the national companies and securities scheme. For this reason, amendments are to be made to subsection 1B(1) and sections 102 and 127 of the Act:

- subsection 1B(1) of the Act is amended to provide that the new functions (specified in proposed section 12A) do not form part of the ASC Law of the ACT (Item 5).

- Sections 102 (delegations) and 127 (confidentiality) are provisions which are applied as the law of each State and the Northern Territory by virtue of the Corporations ([Name of State]) Acts. They are to be amended in relation to the additional functions which the Commission is undertaking (see below). The amendments therefore include a provision which states that if the section is being

applied as a law of a State, it applies only in relation to functions and powers conferred by a national scheme law (Items 15 and 29).

Consequential amendments

The objects of the Act

Items 2 and 3

5.16 The objects of the Act have been amended so that they include a reference to the Commonwealth laws to be administered by ASIC (item 2).

5.17 Subsection 1(2), which gives directions to the Commission as to how it will perform its functions and exercise its powers, is amended consistently with the wider functions of the Commission (item 3).

5.18 Thus, the amended provision urges the Commission:

- to 'maintain, facilitate and improve the performance of the financial system and the entities within that system' and no longer refers only to companies and the securities and futures markets; and

- to promote the 'confident and informed participation of investors and consumers in the financial system', consistently with the increased consumer protection role to be undertaken by the Commission.

5.19 Subsection 1(2) of the Act also refers to the activities of the Commission in receiving and processing information and making it available to the public. References in the appropriate paragraphs to both documents and information have been amended to refer only to information. This change does not alter the effect of this provision.

Delegation

Items 12 14

5.20 It is desirable that APRA and ASIC be able to work closely together. For this reason, the power in the Act to delegate is to be amended to permit the Commission to delegate to a member of the staff of APRA without the Minister's approval, but only with the agreement of the Chief Executive Officer of APRA (items 12-14).

Disclosure of interests by the Chairperson

Item 16

5.21 The Act currently requires the Chairperson of the Commission to give written notice to the Minister of all direct or indirect pecuniary interests that the Chairperson has or acquires in, or in a body corporate carrying on, a business carried on in Australia (section 123).

5.22 This provision is to be amended by specifically mentioning the interests, relating to superannuation and retirement savings accounts, which the Insurance and Superannuation Commissioner is currently required to disclose (item 16).

How the Commission's money is to be applied

Items 30 and 31

5.23 The provision of the Act (section 135) which sets out the purposes for which the Commission can apply its money is to be amended so that it can apply its funds in relation to its new functions (item 30).

5.24 In addition, this section is to be amended so that the ASC can administer unclaimed monies under the *Superannuation Industry (Supervision) Act 1993* in accordance with the procedures currently set out in Part 22 of that Act (item 31).

Annual report

Item 32

5.25 The Commission is required by the *Commonwealth Authorities and Companies Act 1997* to provide the Minister with an annual report.

5.26 Section 138 of the Act requires that the Commission include certain matters in that report.

5.27 That section is to be amended to include the additional matters which the Insurance and Superannuation Commissioner has been required to include in the annual reports under *Retirement Savings Accounts Act 1997*, the *Insurance (Agents and Brokers) Act 1984* and the *Superannuation Industry (Supervision) Act 1993* and for which ASIC is taking responsibility (item 32).

Confidentiality

Extension to new functions

Items 17 and 29

5.28 The Act requires the Commission to take all reasonable measures to protect from unauthorised use or disclosure information given to it 'in confidence in or in connection with' the performance of its functions and the exercise of its powers under a national scheme law (subsection 127(1)).

5.29 This provision is to be amended so that the obligation extends to information obtained under the additional functions of the Commission (item 17 and the definition of 'protected information' in proposed subsection 127(9)(item 29)).

Disclosure of statistics and superannuation/RSA information, and to the Minister and APRA

Items 18 and 19

5.30 The current confidentiality provision of the Act will be amended (items 18; 19) so that the following additional disclosure will be authorised:

- summaries of information or statistics provided that information relating to any particular person cannot be found out from the summaries or statistics;

- certain information about retirement savings account providers and superannuation funds which is currently available under the *Retirement Savings Accounts Act 1997* and *Superannuation Industry (Supervision) Act 1993*;

- disclosure to the Minister, the Secretary of the Department (or an authorised officer), or APRA.

Disclosure to additional specified Commonwealth and State bodies

Items 20 and 21

5.31 Currently, where the Chairperson is satisfied that particular information will enable or assist a Commonwealth agency to perform or exercise any of the agency's functions or powers, the disclosure of the information is taken to be authorised (paragraph 127(4)(a)). The class of agencies to which this provision applies is those which are an agency within the meaning of the *Freedom of Information Act 1982*. The same section permits disclosure to an agency of a State or Territory.

5.32 The proposed amendments will enlarge this class by including the Australian Bureau of Criminal Intelligence, the Australian Financial Institutions Commission, the Superannuation Complaints Tribunal and the Office of Law Enforcement Co-ordination (items 20; 21). These bodies do not fall within the categories of agency to which disclosure is currently permitted, for technical reasons.

Disclosure to prescribed professional disciplinary bodies

Items 22 23 and 26

5.33 In addition, the Commission is to be empowered to disclose information to prescribed professional disciplinary bodies to enable or assist them to perform their functions (items 22 and 23).

5.34 It should be noted that the Chairperson can impose conditions on the disclosure of information (subsection 127(4A)) and that further disclosure by a member of the professional disciplinary body is prohibited (item 26).

Disclosure to foreign financial exchanges

Item 24, 25 and 27

5.35 The current confidentiality provision in the Act also permits disclosure to a prescribed body corporate which conducts a securities or futures market or is a clearing house for securities or futures in certain circumstances. Disclosure is only authorised when the Chairperson is satisfied that the information will enable or assist the body corporate to monitor compliance with or exercise powers under the Corporations Law or the business or listing rules of the body corporate (subsections 127(4B) to (4F)).

5.36 This power is to be extended so that the Chairperson may, in comparable circumstances, disclose information to foreign financial exchanges (items 24 and 25). This is in accordance with the recommendation of the Parliamentary Joint Committee on Corporations and Securities following the collapse of Barings. The penalty provision is to be appropriately amended (item 27).

Updating cross-references

Item 28

5.37 References to the new provisions are inserted in subsection 127(6) which provides that nothing in the specified subsections limits anything else in any of them and what might otherwise constitute authorised use or disclosure of information (item 28).

Repeal of provision

Item 9

5.38 Subsection 9(3A) of the Act refers to a person being appointed as a full-time member of both the ASC and the National Companies and Securities Commission (which supervised regulation under the previous, 'co-operative' scheme).

5.39 This subsection has been omitted because the *National Companies and Securities Commission Act 1979* has been repealed (item 9).

Other amendments

Items 11 and 35

5.40 Under proposed section 93A (item 11), the Commission will be empowered to accept a written undertaking without having first to initiate court proceedings. If the Commission considers that the person who gave the undertaking has breached any of its terms, the Commission can apply to the Court which is empowered to make a wide range of orders. The Australian Competition and Consumer Commission already has this power.

5.41 This Schedule also contains a general transitional provision in relation to the changes of name of ASC and the Act (item 35). Provisions in the Corporations ([Name of State]) Acts will assist in relation to the name of the body and the Act.

5.42 Specific amendments to such references in other Commonwealth Acts are included in Part 2 of Schedule 18 of this Bill.

6

Schedule 2 Amendment of the *Banking Act 1959*

Schedule 2 to this Bill will extend the coverage of the *Banking Act 1959* (the Act) to establish a single licensing and prudential regime for DTIs. This will be achieved by capturing both the business of banking and the business of taking deposits and making advances by corporations under the Commonwealth's Constitutional powers. Scope will, however, be available to extend this definition as the nature of financial products changes and the financial system evolves.

NOHCs containing an ADI will be facilitated by allowing APRA to authorise and regulate these entities under the Act and enabling conglomerates to hold multiple ADI authorities (current policy has precluded this in most circumstances). APRA will, however, process requests for NOHC authorities and multiple licences on a case-by-case basis to ensure that prudential requirements are not compromised. APRA will have greater access to information about non-regulated entities within a financial conglomerate allowing APRA to better manage potential sources of risk to ADIs. In addition, APRA will be able to make standards on prudential matters in relation to ADIs and NOHCs of ADIs.

The amendments will also abolish the requirement on banks to hold NCDs with the RBA from a date to be determined by proclamation.

This Bill will strengthen existing depositor protections contained within Division 2. Currently, Division 2 provides for:

(a) an obligation for the prudential regulator to use its Division 2 powers to protect depositors and an obligation upon banks to provide information to the prudential regulator;

(b) options for the prudential regulator to appoint an investigator or *take control* when a bank is likely to become unable to meet its obligations or to suspend payment (or is actually experiencing these problems) and a requirement that the prudential regulator, if it has taken control, remain in control at least until provision has been made for the repayment of deposits; and

(c) a requirement that banks back Australian deposit liabilities with assets in Australia and that Australian depositors rank ahead of other creditors.

These features are retained in the amended Division 2 but are supplemented by the following measures.

(a) The regulator will have new powers in Division 1BA to direct the activities of an ADI or NOHC in the interests of depositors or when it has contravened a prudential standard or regulation. These direction powers enable the prudential regulator to impose specific corrective action without actually taking control and are intended to facilitate early intervention to prevent a crisis from emerging. The inclusion of the powers outside Division 2 extends their coverage to branches of foreign banks and to NOHCs and is consistent with their early intervention character (including the direction trigger of failure to comply with a prudential regulation or standard).

(b) The mechanisms for taking control (statutory management) of an ADI within Division 2, including provision for the appointment of an administrator to exercise that power, will be clarified. The statutory manager has all the powers of the institution's board so that it can effectively manage the institution in crisis for the protection of depositors.

(c) In addition, when APRA considers that an ADI under statutory management is insolvent and could not be restored to solvency within a reasonable period, it will be able to apply to the Federal Court for an order that the ADI be wound up. The timely wind up of an insolvent institution could prevent further losses from accruing.

A number of minor amendments have been included to update the Act and bring it in line with international prudential practice and plain English requirements.

Commencement

6.1 The amendments to the *Banking Act* will become effective when the APRA is established. The only exception is the removal of the requirement for banks to hold NCDs with the RBA which will take effect from a date specified by proclamation (capped at 24 months).

Section 5 - Definitions

APRA issues

Items 4, 5 and 6

6.2 Definitions of APRA, APRA board members and APRA staff members will be inserted to enable APRA to assume responsibility for exercising prudential regulation under the Act.

Authorised Deposit-taking Institution

Items 1 and 7

6.3 An authorised deposit-taking institution or ADI will refer to a body corporate granted an authority to carry on banking business by APRA under subsection 9(3) of

the Act. Generally, "authorised deposit-taking institution" replaces previous references to the word "bank" throughout the Act and extends the coverage of "banking business" to State and Territory-based DTIs. State and Territory-based DTIs will, however, be given an exemption initially while negotiations are underway between the Commonwealth, State and Territory governments.

Non-operating Holding Company

Items 8, 14, 15 and 16

6.4 Under the *Banking Act 1959*, an authorised NOHC will be a company incorporated in Australia that owns one or more ADIs and is authorised under subsection 11AA(2). The difference between an authorised NOHC and a NOHC authority will be that the former contains one or more ADIs while the latter does not contain any ADIs.

6.5 A NOHC will be precluded from carrying on any business directly but will be able to satisfy the other corporate and regulatory requirements of being a company, such as owning assets, possessing a balance sheet and receiving and paying dividends.

Bank

Item 9

6.6 While the word "bank" will be replaced by the phrase "authorised deposit-taking institution" or "ADI" in most parts of the Act, a definition of "bank" will still be necessary for the bank holiday and unclaimed moneys provisions of the Act. The term "bank" will capture any ADI permitted to use the word "bank" or like words. In the first instance, consistent with current policy, to use the word "bank" an ADI will be required to possess $50 million in capital and hold an exchange settlement account with the RBA. This policy may be reviewed at a future time if changes in the financial system warrant consideration of a change.

Banking Business

Item 10

6.7 In order to regulate all DTIs within the scope of the Act, a broad definition of banking business will be inserted. Banking business will therefore be defined to cover not only the concept of banking under the Constitution but corporations that are both engaged in the business of accepting deposits and the business of making advances. Given the potential for any definition of financial system activity to become dated, the Governor-General will be given the power to make a regulation extending the definition.

Updating other definitions

Items 20 and 22

6.8 References to bodies that no longer exist will be removed. Therefore, definitions of the Queensland Industry Development Corporation and State Bank Limited will be deleted.

Subsidiary

Items 23 and 25

6.9 The definition of subsidiary is the same as that in the Corporations Law.

Section 6 Application of the Act

Items 26 and 27

6.10 Section 6 will be amended to remove references to entities that no longer exist.

Division 1 Authority to Carry on Banking Business

Applications and Approval

Items 29 to 39

6.11 The application process to gain an authority to carry on banking business will be streamlined. APRA will be responsible for approving or rejecting written applications for an authority to carry on banking business in Australia.

6.12 The Treasurer and Governor-General will no longer have any role in the licensing process for ADIs under the Act.

Revocation of Authority

Item 40

6.13 Under the proposed section 9A, APRA will be able to revoke an authority to carry on banking business in certain circumstances without the body corporate requesting a revocation. For example, APRA may revoke an authority where an institution consistently does not comply with, nor endeavour to achieve compliance with, a condition of its licence or a direction made consistent with the Act. Generally, APRA will be required to give the institution written notification of its intention to revoke an authority; allow the body sufficient opportunity to make a submission presenting any mitigating factors or other concerns; and have regard to any submissions made.

Bodies that cease to exist or change their name

Items 40 and 47

6.14 These provisions will allow APRA to quickly and effectively revoke authorities of ADIs and NOHCs that no longer exist and deal with body corporates that hold authorities when they change their name.

Publication

Item 40

6.15 This item will ensure that an up-to-date list of ADIs is readily available to industry, the public and interested persons on a regular basis.

Documents

Items 41 to 44

6.16 Documents required as part of an application for an authority to carry on banking business will be provided to APRA rather than the Treasurer.

Exemptions

Items 45 and 46

6.17 Under proposed replacement subsection 11(1), APRA may exempt a body corporate from the need to get a banking authority or from the need to comply with all or specified provisions of the Act. These exemptions are normally granted to institutions carrying on a limited range of banking business.

6.18 All existing exemptions granted by the Treasurer under section 11 will be retained. However, APRA may review any existing exemption at any time as the circumstances of the institution change.

Proposed Division 1AA Authority to be a Non-operating Holding Company

Item 47

Whether a NOHC needs to be Authorised?

6.19 APRA may require a NOHC that holds an ADI or intends to hold an ADI to be licensed under proposed section 11AA of the *Banking Act 1959*.

Application Process

6.20 A body corporate will be able to apply, in writing, to APRA, at any time, seeking an authority to own or become an authorised NOHC under the Act. APRA will be able to grant the body corporate approval to be a NOHC and attach prudential conditions to its authority, which may be varied, added to or revoked at any time by APRA.

6.21 A body corporate may also be required to obtain other approvals under the *Foreign Acquisitions and Takeovers Act 1975* and the proposed *Financial Sector (Shareholdings) Act 1998* and may be required to meet other requirements of the Government's foreign investment policy.

Why Authorise NOHCs?

6.22 By authorising NOHCs, APRA will be able to access information, as necessary, about the NOHC and other financial and non-financial entities within the group thus providing early warning of any potential risk imposed on the ADI from other parts and activities of conglomerates.

Can APRA Revoke a NOHC Authority?

6.23 APRA may revoke a NOHC authority upon the request of the body corporate or without a request in certain circumstances. The revocation process for a NOHC will be similar to the revocation process for an ADI.

Publication

6.24 APRA will be able to choose whether to publish a list of authorised NOHCs from time-to-time.

Division 1A Prudential Supervision

Item 49

6.25 APRA will be given the power to make standards on prudential matters for ADIs and authorised NOHCs. These prudential standards will specify the requirements to be met by ADIs and NOHCs and will become effective from the date of release, unless a later date is specified.

Item 53

Proposed Division 1BA APRA's Power To Issue Directions

6.26 APRA is provided with both a general directions power in relation to ADIs and NOHCs, and a specific power relating to enforcing certified liquidity contracts.

Proposed Subdivision A Directions other than directions to enforce certified liquidity contracts

Proposed Section 11CA

6.27 The general directions power provides a means for APRA to correct institutional behaviour before a crisis develops. These powers may be contrasted with the control powers in Division 2, which the regulator may wish to exercise in more troubled circumstances. At such times, the regulator may wish to use these directions powers in conjunction with control powers to more effectively resolve a crisis but their primary function is intended to be preventative.

6.28 Clearly, failure of an ADI to comply with a prudential standard or regulation is an important trigger for a direction intended to ensure that the institution remains sound, but some early corrective action may be appropriate in the interests of depositors even if a standard has not been breached. Of course, directions may also be motivated, in part, by the desire of APRA to ensure financial system stability but the depositor protection trigger should prove sufficient for this purpose also since financial instability would directly threaten the safety of deposits.

6.29 The prudential regulator may also issue directions to an authorised NOHC where APRA considers that the NOHC has contravened a prudential regulation or standard; or where it is in the interests of the depositors of an ADI that is a subsidiary of the NOHC.

6.30 The legislation draws upon the *Financial Institutions Code 1992* by providing an indicative list of the kinds of directions which APRA may make. However, since the circumstances under which directions powers may be used are difficult to prescribe before the event, the list also includes a broad power to make a direction regarding the way the affairs of a body corporate are to be conducted. APRA must therefore also be given broad discretion in relation to decisions about the time period for compliance and nature of such directions.

6.31 The power to revoke a direction must likewise be flexible to allow an appropriate response in the face of compliance, changed circumstances or valid objection by the institution concerned.

Proposed Subdivision B Directions to enforce certified industry liquidity contracts

6.32 The current State-based regulatory regime requires institutions to contribute funds to an Emergency Liquidity Support Scheme. Under the new Commonwealth regulatory framework, it is envisaged that some parties may wish to voluntarily participate in a liquidity support scheme through a 'liquidity contract' with other institutions. The terms and conditions of that contract would be a matter for the parties to agree amongst themselves and, in developing prudential standards, APRA may wish to take such participation into account.

6.33 Before doing so, however, APRA would need to be sure that participants will promptly meet their obligations if and when they become due. APRA will, therefore,

have the power under proposed section 11CB to certify a liquidity contract upon the request of the parties concerned, where it believes the terms of that contract are appropriate, and to subsequently direct the parties to comply with the terms of that certified liquidity contract, under proposed section 11CC, in the interests of those depositors whose financial safety is put at risk by the failure to extend liquidity. By the same token, APRA may also revoke the certification of any industry liquidity contract if it considers it appropriate to do so for any reason.

Proposed Subdivision C General provisions relating to all directions

Proposed Section 11CD

6.34 Because there is a risk that a direction from APRA may trigger conditions in contracts or agreements that would destabilise an already fragile institution, the Bill provides that directions should not provide grounds for other parties to deny obligations, accelerate any debt or close out any transaction with the institution unless, because of the direction, it has failed to meet its contractual obligations. The possibility that one party may unfairly benefit from this process, or react disproportionately to a partial failure by the ADI to meet its obligations, is addressed by allowing the Federal Court to resolve problem cases (but not in a way that would contravene the direction).

6.35 The qualification allowing other parties to deny obligations, however, does not extend to a direction to not repay any money on deposit or advance because certainty in outcome may be required in this case eg to suspend the payment of deposits in the event of a bank run.

Proposed Section 11CE

6.36 APRA may publish information relating to any direction it has issued in the Gazette, but is under no obligation to do so since this may, in particular circumstances, cause needless concern in the community about the soundness of the institution involved. If it has previously published a direction and then revokes that direction, APRA must also publish the revocation.

6.37 Accountability is addressed by requiring APRA to report to the Treasurer or the RBA on directions when requested. However, this does not prevent APRA reporting at any other time.

Proposed Section 11CF

6.38 Information relating to directions is confidential unless it has been published in the Gazette.

Proposed Section 11CG

6.39 Non-compliance with a direction gives rise to criminal sanctions, applicable to both a body corporate or an individual, as appropriate, because the consequences for the safety of deposits may be very severe possibly with implications for the confidence and stability of the financial system in general.

Division 2 Protection of Depositors

Items 60, 61, 62, and 63

6.40 Although most of the provisions of Division 2 have been repealed and replaced by new sections, the content of the repealed sections has largely been retained in the new provisions, as has been outlined above in the summary of this schedule. The

subsequent discussion is therefore confined to those amendments that reflect new provisions.

Proposed Subdivision A General provisions relating to depositor protection

6.41 This subdivision houses the current Banking Act provisions relating to: APRA's powers to demand, and an ADI's obligations to provide, information; APRA's powers to appoint an investigator; the triggers for regulatory control of an ADI that is facing difficulties; and the existing depositor priority provisions.

6.42 Under proposed section 13A(1), the prudential regulator may now appoint an administrator to take control of an ADI rather than assume control itself. The appointment of an administrator provides APRA with the flexibility to avail itself of skills that exist outside its ranks. The term 'statutory management' is also introduced in this proposed section to refer to either control by the prudential regulator or control by the administrator it appoints. The provisions, however, relating to statutory management and the administrator are fleshed out in the proposed Subdivision B.

6.43 In addition to the existing conditions for the termination of control, proposed section 13C(1) allows APRA to relinquish statutory management control of an insolvent ADI provided that it has applied to the Federal Court (which it may now do under Subdivision C) and a liquidator has been appointed. The liquidator would then follow processes set down in the Corporations Law. The importance of the insolvency provision has already been discussed. Firstly, it clarifies the fact that deposits are not guaranteed, which should reduce moral hazard and so enhance system stability. Secondly, it helps to protect deposits by removing a possible source of regulatory forebearance and by preventing an ADI from accumulating further loss.

6.44 Because the exercise of statutory management replaces other forms of control (directors and external administrators, see below), special provision has been made in proposed section 13C(2) to ensure that such controls are in place before statutory management may be ultimately terminated. Where control is to be handed to directors, provisions specify the duration of such control.

Item 64

Proposed Subdivision B Provisions dealing with control of an ADI's business by an ADI statutory manager

Proposed Section 14A

6.45 Under current arrangements, the prudential regulator is permitted to take control of an enterprise in the interests of depositors while there remains in place a board of directors, acting on behalf of shareholders and/or, possibly, an external administrator acting for a range of possible interests. The potential for conflict between these parties may not only compromise the resolution of problems in depositors' interests but could deter the supervisor from intervening when needed. The amendments in proposed section 14A(1) remove this potential for conflict by giving the statutory manager the powers and functions of the board it replaces (although it is acting in the interests of depositors not shareholders) and by precluding (or terminating) the appointment of any external administrators.

6.46 At the same time, these parties and other former officers (for example, an executive who has resigned during the crisis) may possess information needed by the statutory manager to perform its duties. Therefore, the proposed section also provides the statutory manager with the power to require them to provide such information,

even if self incriminating (however, individuals are indemnified against the direct use of such incriminating information). A criminal sanction applies for a breach of this provision because the information sought might be essential in a period of crisis.

6.47 This proposed section also makes it clear that the statutory manager has the power to sell or otherwise dispose of the whole or any part of the business. Although this would also follow from the fact that the statutory manager replaces the board, the proposed section removes any possible uncertainty.

Proposed Section 14B

6.48 APRA's powers to make directions or to initiate wind up action may not be delegated to an administrator since decisions regarding these are appropriately left in the hands of the prudential regulator. An administrator appointed by APRA is, however, able to recommend such action to APRA.

Proposed Section 14C

6.49 Taking control of an institution in such circumstances is an onerous responsibility and a statutory manager will therefore not be held liable for losses (but must report them to APRA) unless they arise because of fraud, dishonesty, negligence or wilful failure to comply with the Act. For that reason, also, while a statutory manager has the powers and functions of the board, it is not taken to be a director for the purposes of section 588G of the Corporations Law, which relates to a director's duty to prevent insolvent trading.

Proposed Section 14D

6.50 Where the statutory management function is exercised by an administrator appointed by APRA, the administrator will not have any additional powers that APRA would not have in the circumstances (other than those that arise from the appointment of an external person such as the power to make recommendations to APRA). The administrator must report to and accept direction from APRA.

Proposed Section 14E

6.51 Regardless of any contractual arrangement that may exist between APRA and the administrator, APRA may terminate the administrator's appointment if the latter does not comply with the proposed provisions of Division 2 (provided other control arrangements are put in place).

Proposed Section 14F

6.52 The new insolvency provision in the proposed Subdivision A is accompanied by a power for APRA to apply to the Federal Court for an ADI to be wound up (in accordance with the Corporations Law) when an institution is under statutory management. Statutory management would conclude upon appointment of a liquidator under these circumstances.

Proposed Sections 15, 15A, and 15B

6.53 The need for the statutory manager to be able to act with certainty has been discussed. Provision is therefore made in this proposed subdivision to remove any scope for participation by directors or external administrators in the affairs of the ADI. While a statutory manager is in control, existing directors cease to hold office, the appointment of external administrators is terminated, and no one may take their place. Similarly, legal proceedings could foul effective crisis management so the Bill provides the regulator with the discretion to suspend and prevent them. The discretion

will enable APRA to allow proceedings that do not compromise the statutory manager's effective control. In any case, the court will have ultimate discretion where hardship is involved.

Proposed Section 15C

6.54 Because there is a risk that statutory management may, like directions, trigger conditions in contracts or agreements that would destabilise an already fragile ADI, the Bill provides that statutory management should not provide grounds for parties to deny obligations, accelerate any debt or close out any transaction.

Proposed Section 16

6.55 Statutory management also involves administrative costs associated with running the enterprise. The legislation provides that these costs are a debt owed to APRA and that their repayment ranks ahead of other unsecured debts but behind deposits. The statutory manager is seen as fulfilling certain obligations to depositors that an ADI should have met but did not and a fee for that service is considered appropriate under these circumstances.

Proposed Section 16A

6.56 The exercise of these powers carries with it reporting requirements. The regulator must not only inform the Treasurer when such action is commenced but also annually if statutory management arrangements have been exercised in that year. Moreover, because other community interests are involved, the assumption or termination of statutory management must be notified in the Gazette. The public media may be expected to report such notices.

Proposed Division 2A - Auditors

Item 65

6.57 The proposed sections 16B and 16C will enable adequate voluntary and compulsory disclosure of significant irregularities by external auditors of ADIs. These provisions may enable APRA to obtain earlier warning of potential problems with an ADI.

6.58 Auditors will be compelled to report to APRA when, in their opinion, the institution they are auditing is in financial difficulty or failed to comply with a licence condition, prudential standard, regulation, direction, provision of the Act or any other requirement which, as a result, might jeopardise the interests of depositors. The use of compulsory disclosure is necessary to ensure that APRA receives a minimum level of disclosure from external auditors on prudential matters. Moreover, external auditors will be provided with direct protection from damages (or proceedings instigated by the body corporate they are auditing) for information reported to APRA except from any loss caused by a wilful or negligent action on the auditor's part.

6.59 Auditors that fail to fulfil these compulsory reporting requirements will commit an offence under the Act with a maximum penalty of six months imprisonment. An auditor would not be liable, however, where he or she could prove that the information was immaterial, he or she was unaware of the information or had reasonable grounds for believing that no breach of the Act had occurred or that a matter did not materially prejudice the interests of depositors.

Division 3 Non-callable deposits

Item 86

Why remove Non-Callable Deposits?

6.60 Banks are required to hold one per cent of their eligible liabilities with the Reserve Bank as non-callable deposits (NCDs). The RBA pays interest half yearly to each bank based on the daily level of each bank's NCDs at a rate set, currently around five percentage points below the prevailing market rate. Significantly more funds are collected from the banks via NCDs than it costs the RBA to supervise these institutions.

6.61 NCDs are no longer serving any necessary prudential purpose. Their use as a means of imposing a financial impost on banks is not consistent with principles of regulatory neutrality.

6.62 As part of the process of recouping only the costs of consumer and prudential regulation of ADIs from that sector, NCDs will be removed and costs will be recouped under separate new levy Acts.

Timing of the Removal of NCDs

6.63 NCDs will be removed from a date to be determined by proclamation. This proclamation date has been given a 24 month cap from the date that this Bill is enacted, rather than the usual 6 months cap, to allow its removal to be in the context of bringing non-bank DTIs (not subject to the requirement) into the Banking Act scheme, if agreed by States and Territories.

Part IIA Bank Mergers

Items 109, 110, 111 and 112

6.64 Subsection 38A allows the Treasurer to make a declaration to bind the Commonwealth, Northern Territory and Norfolk Island in respect of a law of a State or Territory relating to a merger. This amendment will extend that power to cover the Australian Capital Territory (ACT) and is similar to those made to other pieces of Commonwealth legislation as a result of the ACT achieving self government. The amendments also extend the reach of this Part to all ADIs.

Part VI Collection and publication of information

Collection and Publication

Items 115 to 124

6.65 The changes to section 51 will give the Governor-General the power to make regulations about the collection and publication of specific information about ADIs and NOHCs.

Investigations

Item 127

6.66 Presently, the RBA has the power under section 61 to conduct investigations and report on prudential matters in relation to banks. These proposed changes will update the wording of the existing provision and extend this power to all ADIs, authorised NOHCs and, where relevant, their subsidiaries. In addition, these amendments will ensure that APRA appointed investigators receive the required level of assistance from employees of the entity being investigated.

Supply of Information

Item 128

6.67 The purpose of these changes is to extend the current 'provision of information' requirement to all ADIs, authorised NOHCs and, where relevant, their subsidiaries.

6.68 In addition, a new provision will be included to ensure that self incrimination does not prevent persons from providing to APRA the requested information, which may be necessary to protect depositors.

6.69 To balance the requirement to provide information even if it may incriminate the provider, the new provisions will also provide persons with indemnities from the use in a court proceeding of any information given by the person to APRA (use indemnity) where they invoke that privilege.

Part VII Miscellaneous

Restructuring an ADI

Items 129 to 132

6.70 The consent of the Treasurer is necessary before an ADI can sell or dispose of its business, enter a partnership with another ADI or effect a reconstruction of the ADI. The Treasurer will be able to delegate all or any of his or her powers under section 63 to APRA, an APRA Board member, a member of APRA's staff or an officer in the Treasury.

Settlement of Balances

Item 133

6.71 Section 64 on the settlement of balances will be repealed as this provision is superseded by the proposed *Payment Systems (Regulation) Act 1998*. In addition, payment system issues will remain the responsibility of the RBA and therefore these provisions should not be retained in an Act administered by APRA.

Directed Compliance with the Act

Item 139

6.72 Section 65 of the Act, amongst other things, allows the Federal Court of Australia to authorise the RBA to assume control of, and to carry on, the business of a bank under certain circumstances. This item transfers that responsibility to APRA, extends coverage to ADIs and NOHCs and provides for the same notion of control as APRA will now have for depositor protection purposes.

Use of Certain Business Names

Items 143 to 146

6.73 Under section 66, any financial business wanting to use certain financial names, namely "bank", "building society", "credit union", "credit society" or related names, will need to obtain written approval from APRA before using the name. APRA will be able to attach conditions to the use of any of these business names and these conditions may be varied by APRA at any stage.

6.74 The legislation will not describe the conditions that must be met before APRA will approve the use of a particular business word. Instead, APRA will take into account current policy with respect to these names. For example, under current policy, a bank is required to possess at least $50 million in capital and an exchange settlement account with the RBA while only mutuals are allowed to be a "credit union" or "credit society".

6.75 Approval to use certain business names may be given for a range of persons or a particular person.

6.76 Only financial businesses authorised to carry on banking business under subsection 9(3) will be able to use the expression "authorised deposit-taking institution" or "ADI" under section 66A. These institutions will not require approval from APRA.

Deceased estates

Item 150

6.77 Banks are often called upon to release funds prior to a grant of probate or letters of administration in order to meet the immediate needs of the executor, next of kin, or other relevant persons in relation to funeral and probate expenses.

6.78 These proposed amendments will provide protection to banks and other DTIs from legal action, in the event of an error, where payments of up to $15,000 are made from deceased customers' accounts before the granting of probate or the provision of letters of administration, or where the person dies intestate. These amendments will offer some protection to ADIs similar to that already given to credit unions, building societies and life insurance companies.

Offences

Item 152

6.79 The new table of offences will preserve existing offences and their associated penalty levels and add additional offences for the new provisions elsewhere in the Act. The table contains the maximum penalty for a person convicted of an offence. For corporations, the maximum penalty is five times the maximum applicable to an individual convicted of the same offence.

Compensation for Acquisition of Property

Item 154

6.80 This proposed provision ensures that the Act is not in contravention of section 51 (xxxi) of the Constitution which requires any acquisition of property or removal of property rights to be on just terms. If an acquisition is not on just terms, the affected person may apply for compensation from the Commonwealth. There is, however, no expectation that the operation of the Act will lead to an acquisition of property other than on just terms.

Constitutional Issues under the Act

6.81 The proposed section 69F will assist a court in determining the valid operation of the provisions relating to NOHCs and subsidiaries of ADIs and NOHCs under the Constitution.

Indemnity

Item 155

6.82 The proposed section 70A will be similar to that currently contained in the *Reserve Bank Act 1959*. It will ensure that employees of APRA, administrators, statutory managers, auditors etc are indemnified for any actions connected with carrying out their functions under the Banking Act or any directions given under the Act. A global indemnity item for APRA employees, APRA Board members and executives will be contained in the proposed *Australian Prudential Regulation Authority Act 1998*.

Schedules to the Banking Act 1959

Items 158-159

6.83 Schedule 1 is being repealed and Schedule 3 is being renumbered as Schedule 1.

7

Schedule 3 Repeal of the Banks (Shareholdings) Act 1972

The proposed streamlining of legislation governing ownership of financial institutions is outlined in the proposed Financial Sector (Shareholdings) Act (FSSA). The FSSA streamlines regulation by applying common shareholding rules to the deposit-taking and insurance sectors, and by allowing approvals for holding companies to carry through to all regulated members of a company group.

The FSSA requires a person to ensure that their stake (voting power of the person and their associates) does not exceed 15 per cent and that they do not have practical control (the power to control the policies and operations of the financial sector company), regardless of the size of their shareholding. The Treasurer may declare a person to have practical control of a financial sector company and under such a declaration the person must relinquish practical control or reduce their stake in the financial sector company.

The regulations may require records to be kept, and information to be given, for the purposes of determining the restrictions on shareholdings.

The proposed FSSA will replace the Banks (Shareholdings) Act.

Commencement

7.1 Schedule 3 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Item BS1

7.2 Item BS1 proposes to repeal the *Banks (Shareholdings) Act 1972* (BSA).

8

Schedule 4 Amendment of the Corporations Law 1989

The purpose of Schedule 4 is to amend the Corporations Law to reflect the change of name of the Australian Securities Commission (ASC) to 'Australian Securities and Investments Commission' (ASIC).

Commencement

8.1 Schedule 4 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Change of name of regulator

Items 1 47

8.2 Item 1 of Schedule 4 amends the definitions section of the Corporations Law (section 9) by repealing the definition of the 'ASC' and inserting a definition of 'ASIC'.

8.3 Items 2; 3; 5 and 6 of Schedule 4 amend references to the *Australian Securities Commission Act 1989* in the definitions of 'Advisory Committee'; 'Board'; 'Commission Act' and 'unclaimed money account' in section 9 to refer to the *Australian Securities and Investments Commission Act 1989*.

8.4 Item 4 amends the definition of 'Commission' in section 9 to refer to the Australian Securities and Investments Commission.

8.5 Items 7 and 8 of Schedule 4 replace the words 'Australian Securities Commission' with the words 'Australian Securities and Investments Commission' in 2 places in the Small Business Guide.

8.6 Items 9 12 amend 4 references to the *Australian Securities Commission Act 1989* to refer to the *Australian Securities and Investments Commission Act 1989*.

8.7 The following items omit references to the ASC in the Corporations Law and substitute references to ASIC: 13 - 47.

9

Schedule 5 Amendment of the Corporations Law 1989 to take account of the Company Law Review Act 1998

The purpose of Schedule 5 is to amend the Corporations Law taking into account the changes in the proposed *Company Law Review Act 1998* to reflect the change of name of the Australian Securities Commission (ASC) to 'Australian Securities and Investments Commission' (ASIC).

Commencement

9.1 In the event that item 32 of Schedule 3 to the proposed *Company Law Review Act 1998* (a provision which renumbers 11 sections in the Corporations Law) commences before the proposed *Australian Prudential Regulation Authority Act* commences, Parts 1 4 of Schedule 5 come into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act*.

9.2 In the event that item 32 of Schedule 3 to the proposed *Company Law Review Act* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Parts 1 4 of Schedule 5 come into effect immediately after the commencement of item 32.

9.3 Because of the possibility that Schedule 5 to the proposed *Company Law Review Act* will commence at a different time from the other schedules to that Act, Part 5 of Schedule 5 to the proposed *Financial Sector Reform (Amendments and Transitional Provisions) Act*, which amends Schedule 5 to the proposed *Company Law Review Act*, has a separate commencement provision.

9.4 In the event that Schedule 5 to the proposed *Company Law Review Act* (a schedule dealing with amendments in relation to nominal value and share capital reductions) commences before the proposed *Australian Prudential Regulation Authority Act* commences, Part 5 of Schedule 5 comes into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act*.

9.5 In the event that Schedule 5 to the proposed *Company Law Review Act* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Part 5 of Schedule 5 comes into effect immediately after the commencement of Schedule 5 to the proposed *Company Law Review Act.*

Change of name of regulator

Items 1 156

9.6 Items 1 and 2 of Schedule 5 replace the words 'Australian Securities Commission' with the words 'Australian Securities and Investments Commission' in 2 places in the Small Business Guide.

9.7 Items 3 5 amend 3 headings in the Corporations Law taking into account the changes in the proposed *Company Law Review Act* to refer to ASIC.

9.8 Item 6 repeals a reference to the ASC's powers in section 1362CH and substitutes a reference to ASIC's powers.

9.9 The following items in Part 2 of Schedule 5 omit references to the ASC in the Corporations Law taking into account the changes in Schedule 1 of the proposed *Company Law Review Act* (the main amendments of the Corporations Law) and substitute references to ASIC: 7 123.

9.10 The following items in Parts 3 and 4 of Schedule 5 omit references to the ASC in the Corporations Law taking into account the changes in Schedules 2 - 4 to the proposed *Company Law Review Act* (the consequential amendments of the Corporations Law, the structural amendments of the Corporations Law and the consequential amendments of other legislation) and substitute references to ASIC: 124 152.

9.11 The following items in Part 5 of Schedule 5 omit references to the ASC in the Corporations Law taking into account the changes in Schedule 5 to the proposed *Company Law Review Act* (amendments in relation to nominal value and share capital reductions) and substitute references to ASIC: 153 - 156.

10

Schedule 6 Amendment of the Corporations Law 1989 to take account of the Managed Investments Act 1998

The purpose of Schedule 6 is to amend the Corporations Law taking into account the changes in the proposed *Managed Investments Act 1998* to reflect the change of name of the Australian Securities Commission (ASC) to 'Australian Securities and Investments Commission' (ASIC).

Commencement

10.1 In the event that the proposed *Managed Investments Act 1998* commences before the proposed *Australian Prudential Regulation Authority Act* commences, Schedule 6

comes into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act.*

10.2 In the event that the proposed *Managed Investments Act* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Schedule 6 comes into effect immediately after the commencement of the proposed *Managed Investments Act.*

Change of name of regulator

Items 1 69

10.3 The following items in Parts 1 and 2 of Schedule 6 omit references to the ASC in the Corporations Law taking into account the changes in Schedule 1 of the proposed *Managed Investments Act* (the new managed investments provisions and transitional provisions) and substitute references to ASIC: 1 - 55.

10.4 The following items in Parts 3 and 4 of Schedule 6 omit references to the ASC in the Corporations Law taking into account the changes in Schedule 2 of the proposed *Managed Investments Act* (the consequential amendments) and substitute references to ASIC: 56 - 59.

11

Schedule 7 Amendment of the Financial Corporations Act 1974

Consistent with the changes in the *Banking Act 1959*, the amendments contained in Schedule 7 of this Bill will exempt authorised deposit-taking institutions from data collection requirements under the *Financial Corporations Act 1974* (FCA). As a consequence, in the event that building societies and credit unions are regulated under the *Banking Act 1959*, these institutions will not be required to provide the same data to both the Reserve Bank of Australia (RBA) and the Australian Prudential Regulation Authority (APRA).

The Treasurer's powers with respect to categorising registered corporations and exempting corporations from the application of the FCA will be transferred to the Governor of the RBA.

Commencement

11.1 The amendments to the *Financial Corporations Act 1974* will become effective when the APRA is established

Amendments

Item FC1

11.2 This Item inserts a definition of the Governor of the RBA into subsection 4(1) of the FCA.

Item FC5

11.3 This item replaces the reference to "banks" being exempted under the *Banking Act 1959* with a reference to "authorised deposit-taking institutions" in paragraph 8(2)(b). This change is necessary given that the amendments to the *Banking Act 1959* (in Schedule 2 of this Bill) will widen the scope of that Act to encompass banks and other deposit taking institutions.

Item FC10

11.4 This item transfers the power from the Treasurer to the Governor of the RBA to exempt corporations from the application of the Act.

Item FC15

11.5 This item repeals the existing paragraph 9(9)(c) and substitutes it with a paragraph to enables corporations that cease to exist or cease to be covered by the Act to be removed from the Register kept by the RBA, whether or not these corporations apply for removal from the Register.

Items FC20, 25, 35, 40, 50, 65 and 70

11.6 These items transfer the Treasurer's power under section 10 to the Governor of the RBA with respect to listing, varying and categorising registered corporations under the FCA and publishing the list of registered corporations and any variations.

Item FC30 and 60

11.7 This item repeals subsections 10(3), (5B) and (5C) as the Treasurer will no longer have a role in categorising or varying registered corporations under the FCA.

Item FC55

11.8 This item removes the requirement of the Treasurer to give to the RBA a copy of any list of registered corporations.

Item FC75

11.9 This item repeals subsection 10(8) as the RBA advice is no longer required by the Treasurer in exercising his or her functions under subsection 10(7).

Item FC80

11.10 This item repeals subsection 11(12) as there is no longer a need to direct the Statistician to prepare and publish statements containing such information as requested.

Item FC85

11.11 This item allows the Governor of the RBA to exempt a corporation from the requirement to prepare statements in accordance with regulations.

Item FC90

11.12 This item repeals the existing delegation provision in section 22A and replaces that provision with an item to allow the Governor of the RBA to delegate the powers under paragraph 8(2)(l) and section 10 other than subsection 10(1) to an officer in the Reserve Bank Service as defined in section 66 of the *Reserve Bank Act 1959*.

12

Schedule 8 Amendment of the Insurance Acquisitions And Takeovers Act 1991

Schedule 8 will streamline the *Insurance Acquisitions and Takeovers Act 1991* (IATA) to facilitate integration with the proposed Financial Sector (Shareholdings) Act 1998 (FSSA) and transfer regulatory responsibility for IATA to APRA. The FSSA will

streamline regulation by applying common shareholding rules to the deposit-taking and insurance sectors, and by allowing approvals for holding companies to carry through to all regulated members of a company group.

The FSSA requires a person to ensure that their stake (voting power of the person and their associates) does not exceed 15 per cent and that they do not have practical control (the power to control the policies and operations of the financial institution), regardless of the size of their shareholding. The regulations may require records to be kept, and information to be given, for the purposes of determining the restrictions on shareholdings.

Commencement

12.1 Schedule 8 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Items 1 to 27 - Proposed amendments to sections 3, 4, 19, 63, 64, 65, 69, 74, 75, 77, 78, 79 *81 and 82 of the IATA*

12.2 The schedule proposes numerous minor amendments to the IATA reflecting that matters relating to acquisitions of insurance companies will be covered in the proposed FSSA. The proposed amendments also provide for the transfer of regulatory responsibility for the IATA from the Insurance and Superannuation Commissioner to APRA.

12.3 Item 10 proposes to repeal Part 2 of the IATA dealing with the control of acquisition or issue of shares in Australian-registered insurance companies and related companies. All matters relating to acquisitions of insurance companies will be covered in the proposed FSSA. The FSSA will enable the Treasurer to declare a person to have 'practical control', that is, the power to control the policies and operations of a financial sector company, regardless of the size of their shareholding. Under such a declaration the person must relinquish practical control or reduce their stake in the financial sector company.

13

Schedule 9 Amendment of the Insurance Act 1973

The purpose of Schedule 9 is to amend the *Insurance Act 1973* (the Act) to transfer regulatory responsibility for the Act to APRA except for one provision which is to be transferred to ASIC. The Act regulates the general insurance industry, including Lloyds underwriters. All of the functions and powers under the Act were formerly performed and exercised by the ISC. Schedule 9 incorporates amendments to the Act that are proposed in the *Insurance Laws Amendment Act 1998*.

Commencement

13.1 Schedule 9 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

13.2 It is anticipated that the Insurance Laws Amendment Bill 1998, once enacted, will commence by or on 1 July 1998. Schedule 9 amends provisions in the proposed *Insurance Laws Amendment Act*. In the event that the proposed *Insurance Laws Amendment Act 1998* commences before the *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998* (the FSR Act), Schedule 9 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998.* In the event that the proposed *Insurance Laws Amendment Act* and the proposed

FSR Act commence on the same day, the provisions of Schedule 9 commence immediately after the provisions of the proposed *Insurance Laws Amendment Act.*

Change of name of regulator

13.3 Until the commencement of the *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998* (the FSR Act), the Insurance and Superannuation Commissioner is responsible for the supervision of all aspects of compliance with the Act. On commencement of the FSR Act, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of the Insurance and Superannuation Commissioner will no longer exist. Items 1 and 2 insert definitions of 'APRA' and 'ASIC' into section 3 of the Act, and item 4 repeals the definition of Commissioner, which will no longer be required under the Act.

13.4 Schedule 9 therefore amends references in the Act to the Insurance and Superannuation Commissioner by replacing them with references to APRA, except in one instance where it is replaced by a reference to ASIC.

13.5 ASIC is to have general responsibility for the administration of section 113 which relates to approval of and compliance with codes of practice relating to general insurance (Items 6 and 86). It therefore fits into ASIC's role in relation to consumer protection. ASIC is also given certain ancillary powers (Item 87).

13.6 Since APRA is not a natural person, references in the Act to 'he or she' or 'him or her' are replaced with 'APRA', 'his or her' by 'APRA's' and 'himself or herself' with "itself'. Further, because only a natural person can enter premises, section 54 is amended to replace 'Commissioner' with 'an authorised person'. An authorised person is defined in proposed subsection 54(3) as an APRA staff member.

Repeal of provisions

13.7 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the specific APRA Act. For example, the proposed APRA Act includes comprehensive provisions dealing with the delegation of powers by APRA. For this reason it is no longer necessary to include in the Act a separate power to delegate functions. Therefore, the delegation power in section 59 refers to the APRA Act's delegation powers.

13.8 Similarly, APRA's annual reporting requirements are dealt with in the APRA Act, and it is therefore no longer necessary to retain s125 of the Act.

13.9 The secrecy provisions in s126 and s127 of the Act dealt with the manner in which the ISC was required to treat information gathered by it under the Act in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, e.g. the S*uperannuation Industry (Supervision) Act 1993* and the *Life Insurance Act 1995.* Therefore, the secrecy provisions included in the APRA Act mean that it is no longer necessary to retain individual provisions in each Act. Requirements peculiar to any Act can be addressed through the power in the APRA Act that allows disclosure of otherwise protected information with the approval of the Board of APRA.

13.10 The Schedule also deletes Part IX of the Act, which set transitional provisions that applied on commencement of the Act, but are now unnecessary. The provisions will, however, continue to apply for any company to whom Part IX applied before the commencement of these amendments.

13.11 The Items that repeal superfluous provisions in the Act are : IA926 and IA17.

Schedule 10 Amendment of the Insurance (Agents And Brokers) Act 1984

The purpose of Schedule 10 is to transfer regulatory responsibility for the *Insurance (Agents and Brokers) Act 1984* (the Act) to ASIC. The Act regulates insurance intermediaries, in part by requiring that insurance brokers and foreign insurance agents are registered under the Act. All of the functions and powers under the Act were formerly performed and exercised by the ISC.

Commencement

14.1 Parts 1 - 3 of Schedule 10 (comprising items 1-64) will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

14.2 In the event that items 47, 52, 60 and 66 of Schedule 1 to the proposed *Insurance Laws Amendment Act 1998* commence before the proposed *Australian Prudential Regulation Authority Act* commences, Part 4 of Schedule 10 (comprising items 61 64) comes into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act*.

14.3 In the event that items 47, 52, 60 and 66 of Schedule 1 to the proposed *Insurance Laws Amendment Act* commence after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Part 4 of Schedule 10 comes into effect immediately after the commencement of those items in the proposed *Insurance Laws Amendment Act.*

Change of name of regulator

Items 1, 3 - 10, 12, 13, 16 60

14.4 Until the commencement of the proposed *Financial Sector Reform (Amendments and Transitional Provisions) Act* (the FSR Act), the Insurance and Superannuation Commissioner is responsible for supervising all aspects of compliance with the Act. On commencement of the proposed FSR Act, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist. Item 1 inserts a definition of 'ASIC' into s9 of the Act. Item 3 repeals the definition of 'Commissioner', which is no longer required under the Act.

14.5 Schedule 10 therefore amends references in the Act to the Insurance and Superannuation Commissioner by replacing them with references to ASIC.

14.6 The items which insert references to ASIC in place of references to the Insurance and Superannuation Commissioner are: 8 - 10 and 16 60.

14.7 Because the Act no longer refers to regulation conducted by a natural person (the Insurance and Superannuation Commissioner), but rather to the acts of an agency (ASIC), the Act no longer uses the expressions 'he or she', 'his or her' or 'him or her' when referring to the Commissioner. Amendments of the Act to refer to 'it' or to 'ASIC' are in items 4; 5; 8; and 13.

14.8 Similarly, because ASIC is not a natural person, references to documents in writing signed by the Insurance and Superannuation Commissioner are amended to refer to documents prepared 'in writing'. Items 6 10 and 12 make this change.

Co-operation between regulators

Items 2 and 15

14.9 To assist ASIC and APRA to co-operate, a new section 47 empowers ASIC to appoint a member of the staff of ASIC or APRA to carry out the functions of an 'authorised person' under the Act. It is expected that the two regulators will enter a memorandum of understanding which will refer to such provisions and other matters. The relevant items are items 2 and 15.

Repeal of provisions

Items 11, 14 and 15

14.10 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the specific ASIC Act. For example, the ASIC Act includes comprehensive provisions dealing with the delegation of powers by ASIC. For this reason, it is no longer necessary to include in the Act a separate power to delegate functions. Therefore, the delegation power in s47 of the Act is repealed.

14.11 Similarly, ASIC's annual reporting responsibility is dealt with in the *Commonwealth Authorities and Companies Act 1997* and the ASIC Act. It is therefore no longer necessary to retain s45 of the Act.

14.12 The secrecy provision in the Act (s34U) deals with the manner in which the ISC was required to treat information gathered by it under the Act in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, eg the *Superannuation Industry (Supervision) Act 1993* and the *Life Insurance Act 1995*. However, it is different from the secrecy regime under which the ASC operated in relation to its corporate law functions.

14.13 Section 127 of the *ASIC Act*, which previously related only to corporate regulatory functions, will be extended to cover ASIC's new functions under the Act, so that ASIC will be able to perform all of its functions under the same secrecy regime. Therefore, section 34U is repealed.

14.14 The items which repeal superfluous powers and functions in the Act are: 11; 14 and 15.

Schedule 10, Part 4: Amendments to take account of the Insurance Laws Amendment Act 1998

Items 61 64

14.15 The purpose of Part 4 of Schedule 10 is to amend the Act as amended by the proposed *Insurance Laws Amendment Act 1998* to reflect the change of regulatory responsibility under the proposed FSR Act. References to the Insurance and Superannuation Commissioner in provisions amended by Schedule 1 to the proposed *Insurance Laws Amendment Act 1998* are repealed and references to ASIC substituted. Items 61 64 of Part 4 make this change.

15

Schedule 11 Repeal of the Insurance and Superannuation Commissioner Act 1987

Schedule 11 repeals the *Insurance and Superannuation Commissioner Act 1987* ('the Act'). The Act establishes the office of the Insurance and Superannuation Commissioner, and provides the terms and conditions for the position of Insurance and Superannuation Commissioner, and the staff required to assist the Commissioner. With the establishment of APRA and ASIC, this position will cease to exist, and current staff of the Commissioner will transfer to the employ of APRA or ASIC.

Commencement

15.1 Schedule 11 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Item ISC1

15.2 The whole of the *Insurance and Superannuation Commissioner Act 1987* is repealed.

16

Schedule 12 Amendment of the Insurance Contracts Act 1984

The purpose of Schedule 12 is to transfer regulatory responsibility for the *Insurance Contracts Act 1984* (the Act) to ASIC. The Act regulates such aspects of insurance contracts as the duty of good faith, insurable interests, expiration and subrogation. All of the functions and powers under the Act have been performed and exercised by the ISC.

Commencement

16.1 Schedule 12 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Change of name of regulator

Items 1 3 and 8 13

16.2 Prior to the commencement of the proposed *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998*, the Insurance and Superannuation Commissioner has been responsible for supervising all aspects of compliance with the Act. On commencement of Schedule 11, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist.

16.3 Schedule 12 therefore amends references in the Act to the 'Insurance and Superannuation Commissioner' by replacing them with references to ASIC.

16.4 The items which insert references to ASIC in place of references to the Insurance and Superannuation Commissioner are: 1; 3; 8 -13.

16.5 The definition of Commissioner is repealed (Item 2).

Repeal or winding back of provisions

Items 4 7

16.6 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the specific ASIC Act. For example:

• the ASIC Act includes comprehensive provisions dealing with the delegation of powers by ASIC. For this reason, it is no longer necessary to include in the Act a separate power to delegate functions. Therefore, the delegation power in section 11G of the Act is repealed (Item 5).

• ASIC is already required to produce an annual report by the *Commonwealth Authorities and Companies Act 1997*. For this reason, it is no longer necessary to include in the Act a separate requirement to give the Treasurer a written report on the operation of this Act during each financial year. Therefore, section 11H which includes this requirement is repealed (Item 6).

16.7 The secrecy provision in the Act (section 11F) deals with the manner in which the ISC was required to treat information gathered by it under the Act in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, eg the *Superannuation Industry (Supervision) Act 1993* and the *Life Insurance Act 1995*. However, it is different from the secrecy regime under which the ASC operated in relation to its corporate law functions.

16.8 Section 127 of the ASIC Act, which previously related only to corporate regulatory functions, will be extended to cover ASIC's new functions under the Act, so that ASIC will be able to perform all of its functions under the same secrecy regime (see Schedule 1). Therefore, section 11F is repealed (Item 4).

16.9 A minor technical amendment is made to paragraph 66(a) (Item 7), to substitute "insured's" in the place of "insurer's". The incorrect word was inserted by the *Financial Laws Amendment Act 1997*.

17

Schedule 13 Amendment of the Life Insurance Act 1995

The purpose of Schedule 13 is to amend the *Life Insurance Act 1995* (the Act) so as to separate responsibility for the administration of the Act between ASIC and APRA. All of the functions and powers under the Act were formerly performed and exercised by the Insurance and Superannuation Commissioner. Consistent with the amendments of the *Insurance Act 1973*, the *Superannuation Industry (Supervision) Act 1993* and the *Retirement Savings Accounts Act 1997*, ASIC will take on responsibility for market integrity and consumer protection functions under the Act, and APRA will have responsibility for the prudential supervision of life insurance businesses.

Commencement

17.1 Parts 1 - 6 of Schedule 13 (comprising items 1 - 187) will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*. Part 7 (comprising items 188 - 197) will commence on the day on which the proposed *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998* (the FSR Act) receives the Royal Assent.

Division of responsibility

Items 2 and 23

17.2 Item 2 of Schedule 13 allocates functions under the Act to ASIC or APRA, or to both ASIC and APRA. Item 2 explains which regulator has the general administration of the various provisions of the Act. APRA, for example, has Parts 3, Registration of Life Companies, 4, Statutory Funds of Life Companies, 5, Solvency and Capital Adequacy Standards, and 6, Financial Management of Life Companies. These powers

relate to the prudential supervision of life companies, and endow APRA with functions and powers to enable it to supervise the financial security of these companies.

17.3 Proposed paragraph 7(1)(a) confers functions and powers on APRA.

17.4 Proposed paragraph 7(1)(b) confers functions and powers on ASIC. ASIC has the general administration of Part 10 (other than sections 206 210), which contains provisions about policies, such as section 211, which deals with when probate is required in order to pay out a life policy after the death of an insured person, and section 226, which requires life companies to maintain registers of their life policies in each State and Territory. These matters relate to market integrity and consumer protection in the life insurance business, and are therefore matters within the responsibility of ASIC.

17.5 Under section 216 of Part 10, ASIC will take responsibility for the administration of unclaimed money. Items 23 and 163-165 amend section 216 to reflect the transfer of this function to ASIC.

17.6 Proposed subsection 7(2) confers powers and duties which will be shared by ASIC and APRA.

17.7 For example, Part 7 of the Act, which deals with investigatory powers, will be able to be used by both ASIC and APRA, because both regulators will need to have access to a full range of powers in order to conduct their supervisory functions under the Act.

17.8 Close liaison between ASIC and APRA will ensure that the regulators adopt a co-ordinated approach to their dealings with entities in which they both have an interest. The Minister will have the power to give ASIC or APRA directions about the performance or exercise of their functions or powers under the Act (proposed subsection 7(3)). This power is equivalent to subsection 3(3) of the *Retirement Savings Accounts Act 1997* and subsection 6(3) of the *Superannuation Industry (Supervision) Act 1993*, and extends to the actions of ASIC when it is acting under the authority of the Act.

Change of regulator and regulator's name

Items 1, 3 22, 26 28, 30 187

17.9 Until the commencement of the proposed FSR Act, the Insurance and Superannuation Commissioner is responsible for supervising all aspects of compliance with the Act, and conducts both market integrity/consumer protection and prudential regulation. On commencement of Schedule 11 of the proposed FSR Act, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist.

17.10 Schedule 13 repeals references in the Act to the Insurance and Superannuation Commissioner and replaces them with references to ASIC or APRA where appropriate. Item 1 of Schedule 13 amends the objects clause of the Act (section 3) to provide that APRA and ASIC will supervise life companies. In the case of other provisions which are referable to both ASIC and APRA, the expression 'the Regulator' replaces references to the Insurance and Superannuation Commissioner. Item 34 inserts a definition of 'Regulator' into the dictionary in the Schedule to the Act. Items 30 and 31 insert definitions of 'APRA' and 'ASIC' into the Act.

17.11 Because the Act no longer refers to regulation conducted by a natural person (the Insurance and Superannuation Commissioner), but rather to the acts of an agency

(ASIC or APRA), the Act no longer uses the expressions 'he or she', 'his or her' or 'him or her' when referring to the Commissioner. Amendments of the Act to refer to 'it', 'ASIC', 'APRA', or 'the Regulator' are in items 3; 4; 5; 12; 16; 18; 20; 22 and 28.

17.12 Items 7 11, 14, 15, 17 and 19 of Schedule 13 also amend the Act to reflect the fact that regulation under the Act is no longer carried out by a natural person and that the relevant regulator may be either ASIC or APRA, or an authorised person acting on their behalf.

17.13 Item 6 substitutes subsection 127(1) with a provision enabling ASIC or APRA to appoint a member of its own or the other regulator's staff for the purpose of certain investigations under the Act. The expression 'member of staff' is defined in the dictionary in the Schedule to the Act (Item 32). The purpose of this definition is to refer readers to the relevant provisions of the APRA and ASIC Acts in order to interpret the use of those expressions in the Act.

17.14 The items which insert references to APRA in place of references to the Insurance and Superannuation Commissioner are: 35 136.

17.15 The items which insert references to ASIC in place of references to the Insurance and Superannuation Commissioner are: 161 165.

17.16 The items which insert references to the Regulator in place of references to the Insurance and Superannuation Commissioner are: 13; 166 187.

17.17 Items 21, 26 and 27 repeal references in the Act to the 'Australian Securities Commission' and substitute references to ASIC.

17.18 Item 33 inserts into the dictionary in the Schedule to the Act a definition of 'Prudential Rules'. This change enables the renaming of the Commissioner's rules, made under section 252 of the Act. Items 137 160 of Schedule 13 (Part 4 of the Schedule) repeal references in the Act to the 'Commissioner's rules' and substitute references to the 'Prudential Rules'.

Repeal of provisions

Items 24, 25 and 29

17.19 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the *Australian Securities and Investments Commission Act 1989* and the proposed *Australian Prudential Authority Act 1998*. For example, both these Acts include comprehensive provisions dealing with the delegation of powers by the regulators. For this reason, it is no longer necessary to include in the Act a separate power to delegate functions under the Act. Therefore, the delegation power in section 232 of the Act is repealed.

17.20 Similarly, the annual reporting responsibilities of APRA and ASIC under the *Commonwealth Authorities and Companies Act 1997* are dealt with in the *Australian Securities and Investments Commission Act 1989* and the proposed *Australian Prudential Authority Act 1998*. It is therefore no longer necessary to retain section 231 of the Act.

17.21 The secrecy provision in the Act (section 251) deals with the manner in which the ISC was required to treat information gathered by it about life companies in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, eg the *Superannuation Industry (Supervision) Act 1993* and *Retirement*

Savings Accounts Act 1997. However, it is different from the secrecy regime under which the ASC operated in relation to its corporate law functions.

17.22 The proposed *Australian Prudential Authority Act 1998* contains a secrecy provision governing all of APRA's activities. Section 127 of the *Australian Securities Commission Act 1989*, which currently relates only to corporate regulatory functions, will be extended to cover ASIC's new functions in insurance and superannuation regulation, so that ASIC will be able to perform all of its functions under the same secrecy regime. Therefore section 251 is also repealed.

17.23 The items which repeal superfluous powers and functions in the Act are: 24, 25 and 29.

Additional amendments

17.24 Part 7 of the Schedule also includes two minor amendments to the Act.

17.25 The first amends sections 22 and 23 of the Act, to ensure that the original intentions of the requirements for minimum shareholders capital are met. The current provisions have been open to differing interpretations by the life industry. The purposes of the amendments are to remove the uncertainty in respect of interpretation and ensure consistency of application of the capital requirements to all companies. The amendment does not take effect until 31 December 1998 or later (depending on the company's financial year) in order to provide sufficient time for compliance.

17.26 The second amends the restriction the Act currently places on life insurers in relation to mortgaging or charging the assets of a statutory fund. The amendment removes the restriction in particular limited circumstances, the intention being to facilitate the internationally accepted practice of lodging cash or securities (as collateral) in association with derivatives transactions entered into via recognised trading exchanges. This amendment will enhance competitive neutrality for life companies in respect of derivative transactions while not diluting the security of policy owner interests.

18

Schedule 14 Amendment of the Reserve Bank Act 1959

Schedule 14 to the Bill proposes a range of amendments to the *Reserve Bank Act 1959* (the Act). Included among these are provisions establishing the PSB, which will operate as the policy making board of the RBA in relation to the payments system. In this context, the PSB will develop policy for the payments system consistent with the objectives of promoting competition and efficiency in the payments system while controlling risk and ensuring the stability of the financial system. The establishment of the PSB within the RBA complements proposed legislation presented in the Payment Systems (Regulation) Bill 1998 and will substantially increase the accountability of the RBA in relation to its role in the payments system.

Another significant measure proposed in Schedule 14 is a reduction in the size of the RBA Board from 11 to 9 members (due to a reduction in the number of Deputy Governor positions from 2 to 1, and a reduction in the number of other positions from 7 to 6). Schedule 14 also includes a number of miscellaneous amendments to the Act which are largely consequential upon other elements of the financial sector reform package or seek to rationalise or modernise existing provisions that have become dated or obsolete. The diagram below shows the relationship of the RBA with its two Boards.

Items 16, 17, 18, 22, 23, 24, 35, 49, 56, 57, 63, and 64

18.1 Throughout this Bill there are numerous minor amendments that arise due to the establishment of the PSB. There will be two parallel Boards operating under the Act, each with its own specific responsibilities. These items amend the Act to specify the particular Board that is responsible in each instance.

Items 5, 25, 27, 28, 29, 36, 39, 41, 42, 43, 45, 46, 47, 55, 61, and 62.

18.2 These items amend the Act to reduce the number of Deputy Governor positions from 2 to 1.

Items 30, 32, and 40

18.3 In the interests of administrative efficiency, and due to the transfer of some responsibilities to APRA, the size of the Board will be reduced from 11 to 9 members. The reduction will be achieved via the non-renewal of 1 of the 2 Deputy Governor positions and the non-renewal of 1 of the 7 non ex officio positions. As a result, a quorum of the RBA Board will be reduced to 5 members (previously 6 members). These items reflect those changes.

Items 1, 2, 3, 6, 7, 8, and 9

18.4 These items provide a range of new definitions required in the Act consequent upon the creation of APRA and the PSB and their intended functions. Examples include definitions for monetary and banking policy, payment system, and payments system policy.

Item 4

18.5 This item repeals the single definition of the RBA Board. The definitions of the two Boards will be outlined in sections 8A, 10, 10A and 10B of the Act.

Item 10

18.6 This item states that a reference to another Act includes a reference to regulations under that Act.

Items 11, and 12

18.7 These items divide Part II of the Act into two divisions to enhance readability. In addition, they append existing Part II provisions to reflect the creation of the PSB and the enactment of the *Commonwealth Authorities and Companies Act 1997*. Item 12 provides that, for the purposes of the CAC Act, the RBA Board (rather than the PSB) are the directors of the Bank and as such have responsibilities for, amongst other things, financial reporting and the overall administration of the RBA. The PSB is, however, subject to certain provisions of the CAC Act in respect to conflicts of interest and other disclosures.

Items 13, and 14

18.8 These items amend section 8 (describing the general powers of the RBA) primarily to accommodate the additional powers conferred on the RBA under the *Payment Systems (Regulation) Act 1998*.

Item 15

18.9 This item distinguishes the responsibilities of the RBA Board and the PSB. The RBA Board will be responsible for monetary and banking policy while the PSB will be responsible for payments system policy.

Item 19

18.10 This item amends subsection 10(2) of the Act, describing the functions of the RBA Board, to accommodate the intended transfer of RBA powers under the *Banking Act 1959* to APRA (see Australian Prudential Regulation Authority Bill 1998).

18.11 The item makes clear that the RBA Board will not control the powers of the RBA with respect to the proposed *Payment Systems (Regulation) Act 1998* and the proposed *Payment Systems and Netting Act 1998*; these are the responsibility of the PSB.

Item 20

18.12 This item formally establishes the PSB (proposed section 10A), outlines its intended functions and responsibilities (proposed section 10B), and describes procedures for resolving differences between the RBA Board and the PSB (proposed section 10C).

18.13 The PSB's duties will be the supervision of the payments system in order to minimise risk, promote efficiency and to enhance competition contingent upon maintaining the stability of the financial system.

18.14 Where there is a conflict between the two Boards on a policy issue, the RBA Board will generally prevail to the extent of any inconsistency between the two Boards' objectives. If there is a dispute as to which Board is responsible for determining policy on a particular matter, however, the RBA Governor (who is Chair of both Boards) has responsibility for its resolution.

18.15 The policies of both Boards are subject to procedures for the resolution of disagreements with the Government (section 11 of the Act). Specifically, if the Treasurer and the RBA Board, or the Treasurer and the PSB, are unable to reach agreement on a matter of policy, the relevant Board will submit a statement to the Treasurer on the matter in dispute. The Treasurer may then recommend to the Governor-General that the RBA be directed to comply with a policy. Should the Governor-General in Council agree, the relevant Board would implement the policy of the Treasurer in accordance with the Governor-General's direction. The Treasurer will ensure that copies of the relevant documentation (including the Treasurer's statement of the reason for the disagreement) are tabled in the Senate and the House of Representatives within 15 sitting days.

Item 21

18.16 In the interests of transparency and accountability, this item will amend subsection 11(1) of the Act to require the RBA Board and the PSB to periodically report to the Government on their respective policies. Such reports will be provided at least annually.

Item 26

18.17 This item amends a reference regarding the responsibilities of the Governor so that he or she is subject to policy direction by both the RBA Board and the PSB.

Item 31

18.18 This item adds the specification that appointments by the Governor-General are to be made in writing.

Items 33 and 34

18.19 RBA Board members are currently appointed for a period of 5 years. Where Board members vacate their position prior to the completion of their five-year term, the Act caps the length of any replacement appointment to the residual duration of the previous Board member's appointment. This arrangement is inflexible and potentially adds unnecessary iterations to the Board appointment process. To enhance flexibility associated with RBA Board appointments, item 33 will amend section 14 of the Act to provide for flexible terms of up to 5 years. This flexibility will extend to all Board appointments under the Act. This arrangement is consistent with the proposed Board appointment arrangements for APRA and the PSB.

Item 37

18.20 This item clarifies the issue of the oath and secrecy declaration to be made by the members of the two Boards. If a person is a member of both Boards (for example the RBA Governor), the item will ensure that the person is not required to take the same oath and secrecy declarations twice.

Item 38

18.21 Section 19 of the Act deals with the operation of the RBA Board, and the validity thereof, when there is a vacancy on the Board. This section is now unnecessary because of subsection 33(2B) of the *Acts Interpretation Act 1901*. The item will repeal the redundant provision.

Item 44

18.22 Item 44 provides additional provisions relating to the conduct of RBA Board. To ensure consistency with provisions drafted for the PSB (see item 48, Division 2), the item will amend section 22 of the Act to provide for similar provisions to apply for the conduct of meetings of the RBA Board. This provision will permit the RBA Board to pass resolutions using a 'flying minute'; that is, without holding a meeting.

Item 48

18.23 This item will provide for the inclusion of Part IIIA of the Act entitled "The Payments System Board". Part IIIA will describe various administrative issues and procedures applicable to the PSB. The item will create three divisions under Part IIIA, the proposed contents of which are discussed below.

Division 1 - The Members of the Payments System Board

18.24 This Division outlines the composition of the PSB, procedures for nominations to the PSB, and governance issues.

18.25 The PSB will number 8 members comprising the RBA Governor, one other representative of the RBA, one representative of APRA, and 5 other members (proposed section 25A). A quorum of the PSB will be 5 members.

18.26 The representative of the RBA is to be appointed by the Governor and must be either a sitting member of the RBA Board and/or a staff member of the RBA (proposed section 25B). The representative of APRA will be appointed by the Chief Executive Officer of APRA. The Governor-General in Council will appoint the other 5 (independent) members for a period of up to 5 years.

18.27 It is envisaged that the members appointed by the Governor-General will be independent and free of any material direct conflicts of interest. This should not preclude people with substantial past industry experience and expertise in the fields of the payments system and banking regulation. Disclosures of material personal interest will be made in accordance with section 21 of the *Commonwealth Authorities and Companies Act 1997*.

18.28 The Chair of the PSB will be the Governor of the RBA (proposed section 25C). The Deputy Chair is to be the other representative of the RBA (proposed section 25D). The Deputy Chair is to act in place of the Governor when the Governor is unable to attend PSB meetings.

18.29 Some of the deliberations of the PSB will be confidential and may be of commercial value and as such the importance of secrecy is vital. Accordingly, PSB members will be required to make an oath or affirmation of allegiance and a declaration of secrecy (proposed section 25E) in accordance with section 16 of the Act (as for RBA Board members).

Division 2 Meetings

18.30 This Division (proposed sections 25F to 25H) outlines the procedures for PSB meetings, defines a quorum (5 members), defines the rules for voting and gives the Chair both a deliberative and casting vote. The process of passing Board resolutions without meetings is also defined. These provisions are identical to those that apply to the RBA Board under sections 21 (note that amendments to section 21 are proposed in items 40 to 43), 22A and 22B.

18.31 Of note, proposed section 25H (Resolutions without meetings) will permit 'flying minutes' and other forms of resolutions to be passed outside of formal meetings. The provisions are similar to those provided under section 26 of the *Air Services Act 1995*.

Division 3 - Other administrative provisions.

18.32 The remuneration of the five other members of the PSB is to be determined by the Remuneration Tribunal subject to the *Remuneration Tribunal Act 1973* (proposed section 25I). This is equivalent to the conditions applying to the RBA Board. The members that receive full-time salaries from the RBA or APRA are not eligible for additional remuneration as a member of the PSB.

18.33 Leave of absence may be granted to members of the PSB on conditions determined by it (proposed section 25J).

18.34 A member of the PSB may resign by providing a written resignation to the person who appointed that member (proposed section 25K).

18.35 The appointment of the RBA representative (other than the Governor) may be terminated at any time by the RBA Governor; the appointment of the APRA representative may be terminated at any time by the Chief Executive of APRA; and the appointment of the five other members may be terminated by the Governor-General for misbehaviour or mental incapacity (and must be terminated if any of the conditions in proposed section 25L(4) are met). The APRA representative and the RBA representative have their memberships terminated automatically if they cease to be a member/employee of APRA or the RBA respectively.

Item 50

18.36 Section 31 of the *RBA Act* 1959 requires the RBA to publish sterling exchange rates. This is no longer necessary as a wide range of exchange rates is published daily in the financial press. This item will repeal section 31.

Item 51

18.37 This item corrects the Act in section 37 by changing 'bank' to 'Bank' the correct form for the RBA.

Item 52

18.38 Section 35 of the Act describes the denomination of notes that may be issued in Australia by the RBA. The $100 note is not included at present. This item amends the section to reflect the introduction of the $100 note (which is presently authorised through a notice from the Treasurer in the *Gazette*).

Item 53

18.39 Section 44 of the Act provides that a person shall not issue a Bill or note for the payment of money to bearer on demand and intended for circulation. The present penalty for an offence against this part is 10 penalty units. This item will upwardly revise this penalty to 50 penalty units.

Item 54

18.40 Section 45 of the Act provides that any reference to Wednesday in Part V of the Act shall be read as a reference to such other day as prescribed. Section 45 is archaic as there is no longer a reference to Wednesday in Part V of the Act. The item accordingly repeals section 45.

Items 58, 59, 60, and 65

18.41 These items will amend the secrecy provision contained in sections 79A(1), (2) and (8). Definitions of "protected document", "protected information" and other points make reference to various other Acts under which the RBA may be privy to confidential information. These items will amend these provisions for completeness with the proposed legislation (and to reflect the intended repeal of another Act the *Banks (Shareholdings) Act 1972*).

Item 66

18.42 The Act presently provides that the RBA annual report will include a report on any investigations on prudential matters pursuant to section 61 of the *Banking Act 1959.* With the reallocation of prudential responsibilities, APRA will now assume this role with the result that this part should be repealed. Section 81(2) concerning the disclosure of reports with respect to the affairs of an individual bank or customer, arising from investigations reported under section 81(1), becomes redundant with the repeal of section 81(1). Item 66 will repeal section 81.

Item 67

18.43 Item 67 amends section 85 concerning the affixing of the RBA seal to documentation. The provision enables the RBA seal to be kept in such custody as the RBA Board directs and ensures that the seal is not used except as authorised by the RBA Board. This item will expressly allow the RBA Board to decide how the seal is to be affixed, and to control the circumstances of its use.

Item 68

18.44 This item will provide for a higher penalty for offences against regulations, consistent with standard practice. The Governor-General will be able to prescribe penalties not exceeding 10 penalty units as opposed to the present penalty that must not exceed $100.

19

Schedule 15 Amendment of the Retirement Savings Accounts Act 1997

The purpose of Schedule 15 is to amend the *Retirement Savings Accounts Act 1997* (the Act) so as to separate responsibility for the administration of the Act between ASIC and APRA. All of the functions and powers under the Act were formerly performed and exercised by the Insurance and Superannuation Commissioner. Consistent with the amendments of the *Superannuation Industry (Supervision) Act 1993* and the *Life Insurance Act 1995*, ASIC will take on responsibility for market integrity and consumer protection functions under the Act, and APRA will have responsibility for the prudential supervision of retirements savings account providers.

Commencement

19.1 Schedule 15 will commence on the commencement of the proposed *Australian Prudential Authority Act 1998*.

Division of responsibility

Items 1, 4, 6, 7, 20, 23 and 24

19.2 Item 1 of Schedule 15 allocates functions to ASIC or APRA, or to both ASIC and APRA. It states who has the general administration of the various provisions of the Act. APRA, for example, has Part 3, Approval of RSA Institutions, and section 42, which provides that an RSA provider is not to breach the capital guarantee. These powers relate to the prudential supervision of RSA providers, and endow APRA with functions and powers to enable it to supervise the financial security of these providers.

19.3 Proposed paragraphs 3(1)(a) and (b) confer functions and powers on APRA.

19.4 Proposed paragraphs 3(1)(c) and (d) confer functions and powers on ASIC. For example, subparagraph (c)(i) states that ASIC has the general administration of Part 5 of the Act (other than section 49), dealing with the duties of RSA providers and employers. The duty of an RSA provider to keep minutes and records (section 48 of the Act) and to ensure that employers who apply for RSAs on behalf of employees are properly informed about the RSA (section 54 of the Act) are matters relating to market integrity and consumer protection in the RSA market, and are therefore matters within the responsibility of ASIC.

19.5 Proposed subsection 3(2) confers powers and duties which will be shared by ASIC and APRA. These are functions and powers which can equally be used as a tool of market integrity/consumer protection or prudential regulation. ASIC and APRA will both have an interest, for example, in supervising compliance with section 38 of the Act, which sets out the operating standards with which RSA providers must comply. Part 10 of the Act, which deals with investigatory powers, confers powers and duties on both regulators. This is because ASIC and APRA will both need to have access to a full range of powers in order to conduct their supervisory functions under the Act.

19.6 Close liaison between ASIC and APRA will ensure that the regulators adopt a co-ordinated approach to their dealings with entities in which they both have an interest.

The Minister will have the power to give ASIC or APRA directions about the performance or exercise of their functions or powers under the Act (proposed subsection 3(3)). This power is transferred from subsection 3(2) of the Act, and extended to the actions of ASIC in order to preserve the Minister's discretion over the regulators' conduct under the Act.

19.7 In addition, subsection 114(3) is amended by item 23 to provide that ASIC and APRA must give to each other copies of reports of any investigation carried out under the Act.

19.8 To assist ASIC and APRA to co-operate, new section 129A (item 24) enables either regulator to appoint a member of staff of the other regulator to carry out the functions of an 'authorised person' (defined in item 4) under the Act. Items 6 and 7 therefore insert definitions of the expressions 'member of the staff of APRA' and 'member of the staff of ASIC' into section 16. Item 20 makes a similar amendment specifically in relation to the appointment of inspectors under Division 3 of Part 10.

19.9 It is expected that ASIC and APRA will enter a memorandum of understanding which will refer to such provisions and other matters.

Change of regulator and regulator's name

Items 2, 3, 5, 10, 12 22, 25, 26, 30, 31, 34 115

19.10 Until the commencement of the proposed *Financial Sector Reform (Amendments and Transitional Provisions) Act* (the FSR Act), the Insurance and Superannuation Commissioner is responsible for supervising all aspects of compliance with the Act, and conducts both market integrity/consumer protection and prudential regulation. On commencement of the proposed FSR Act, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist. Item 5 therefore amends section 16 by repealing the definition of 'Commissioner'.

19.11 Schedule 15 also repeals other references in the Act to the 'Insurance and Superannuation Commissioner' or the 'Commissioner' and replaces them with references to ASIC or APRA where appropriate. In the case of provisions which are referable to both ASIC and APRA, the expression 'the Regulator' replaces references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner'. Item 10 inserts a definition of 'Regulator' into section 16 of the Act. The provisions which insert references to the Regulator in place of references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner' are: 15 ;17; 18; 20; 70 115.

19.12 Items 2 and 3 insert definitions of 'APRA' and 'ASIC' into the Act. The items which insert references to APRA in place of references to the 'Insurance and Superannuation Commissioner', the 'ISC' or the 'Commissioner' are: 16; 30; 31; 34 63.

19.13 The items which insert references to ASIC in place of references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner' are: 17; 18; 64 69.

19.14 Because the Act no longer refers to regulation conducted by a natural person (the Insurance and Superannuation Commissioner), but rather to the acts of an agency (ASIC or APRA), the Act no longer uses the expressions 'he or she' or 'his or her' when referring to the Commissioner. Amendments of the Act to refer to 'it', 'its' or 'the Regulator' are in items 12; 13; 14; 22; 25 and 26.

19.15 Similarly, because ASIC and APRA are not natural persons, references to documents in writing signed by the 'Insurance and Superannuation Commissioner' or

the 'Commissioner' are amended to refer to documents prepared 'in writing'. Subsection 96(1) is amended to clarify that APRA may appoint an inspector under that provision in this way (item 19). Item 21 makes an equivalent change for delegations made under subsection 97(1).

Repeal of provisions

Items 8, 9, 11, 27 - 29, 32 and 33

19.16 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the *Australian Securities and Investments Commission Act 1989* and the proposed *Australian Prudential Regulation Authority Act*. For example, both the *Australian Securities and Investments Commission Act* and the proposed *Australian Prudential Regulation Authority Act* include comprehensive provisions dealing with the delegation of powers by the regulators. For this reason, it is no longer necessary to include in the Act a separate power to delegate functions under the Act. Therefore, the delegation power in section 198 of the Act is repealed.

19.17 Similarly, the annual reporting responsibilities of ASIC and APRA under the *Commonwealth Authorities and Companies Act 1997* are dealt with in the *Australian Securities and Investments Commission Act* and the proposed *Australian Prudential Regulation Authority Act*. It is therefore no longer necessary to retain section 199 of the Act.

19.18 The secrecy provision in the Act (section 191) deals with the manner in which the ISC was required to treat information gathered by it about RSA providers in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, eg the *Superannuation Industry (Supervision) Act 1993* and *Life Insurance Act 1995*. However, it is different from the secrecy regime under which the ASC operated in relation to its corporate law functions.

19.19 The proposed *Australian Prudential Regulation Authority Act* contains a secrecy provision governing all of APRA's activities. Section 127 of the *Australian Securities and Investments Commission Act 1989*, which previously related only to corporate regulatory functions, will be extended to cover ASIC's new functions in insurance and superannuation regulation, so that ASIC will be able to perform all of its functions under the same secrecy regime. Therefore section 191 is also repealed.

19.20 The items which repeal superfluous powers, functions and definitions in the Act are: 8; 9; 11; 27 - 29; 32 and 33.

20

Schedule 16 Amendment of the Superannuation Industry (Supervision) Act 1993

The purpose of Schedule 16 is to amend the *Superannuation Industry (Supervision) Act 1993* (the Act) so as to separate responsibility for the administration of the Act between ASIC and APRA. All of the functions and powers under the Act were formerly performed and exercised by the Insurance and Superannuation Commissioner. Consistent with the amendments of the *Retirement Savings Accounts Act 1997* and the *Life Insurance Act 1995*, ASIC will take on responsibility for market integrity and consumer protection functions under the Act, and APRA will have responsibility for the prudential supervision of superannuation entities.

Commencement

20.1 Parts 1 - 6 of Schedule 16 (comprising items 1 - 222) will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Part 7 commencement

20.2 In the event that Part 1 of Schedule 2 to the proposed *Superannuation Legislation Amendment Act 1998* commences before the proposed *Australian Prudential Regulation Authority Act* commences, Part 7 of Schedule 16 comes into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act.*

20.3 In the event that Part 1 of Schedule 2 to the proposed *Superannuation Legislation Amendment Act 1998* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Part 7 of Schedule 16 comes into effect immediately after the commencement of Part 1 of Schedule 2 to the proposed *Superannuation Legislation Amendment Act 1998*.

Part 8 commencement

20.4 In the event that Part 3 of Schedule 5 to the proposed *Taxation Laws Amendment Act (No. 3) 1998* commences before the proposed *Australian Prudential Regulation Authority Act* commences, Part 8 of Schedule 16 comes into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act.*

20.5 In the event that Part 3 of Schedule 5 to the proposed *Taxation Laws Amendment Act (No. 3) 1998* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, Part 8 of Schedule 16 comes into effect immediately after the commencement of Part 3 of Schedule 5 to the proposed *Taxation Laws Amendment Act (No. 3) 1998*.

Division of responsibility

Items 2, 5, 6, 21 and 22

20.6 Item 2 of Schedule 16 allocates functions, powers and duties to ASIC or APRA and explains which regulator has the general administration of the various provisions of the Act. APRA, for example, has Parts 13, Accounts, Statements and Audits of Superannuation Entities, and 15, Standards for Trustees, Custodians and Investment Managers of Superannuation Entities. APRA will also receive notifications of adverse events in relation to the financial position of superannuation entities under section 106. These powers relate to the prudential supervision of superannuation entities, and endow APRA with functions and powers to enable it to supervise the financial security of these providers.

20.7 Proposed paragraphs 6(1)(a) and (b) confer functions and powers on APRA.

20.8 Proposed paragraphs 6(1)(c) and (d) confer functions and powers on ASIC. For example, subparagraph (c)(iv) states that ASIC has the general administration of Parts 18 , Prohibited Conduct in relation to Superannuation Interests, and 19, Public Offer Entities Provisions relating to Superannuation Interests and Disclosure of Information. ASIC will also administer section 101, dealing with the duty of trustees to establish arrangements for dealing with inquiries or complaints from fund members and others. These matters relate to market integrity and consumer protection in superannuation, and are therefore matters within the responsibility of ASIC.

20.9 Proposed subsection 6(2) confers powers and duties on ASIC and APRA jointly. These are powers and duties which can equally be used as a tool of market integrity/ consumer protection or prudential regulation. For example, Part 25 of the Act, which

deals with investigatory powers, confers powers and duties on both regulators (other than Division 3, which confers powers on APRA alone). This is because ASIC and APRA will both need to have access to a full range of powers in order to conduct their supervisory functions under the Act. ASIC and APRA will also share Part 26, dealing with offences relating to statements and records and Part 28, dealing with proceedings.

20.10 Close liaison between ASIC and APRA will ensure that the regulators adopt a co-ordinated approach to their dealings with entities in which they both have an interest. The Minister will have the power to give ASIC or APRA directions about the performance or exercise of their functions or powers under the Act (proposed subsection 6(3)). This power is transferred from subsection 6(2) of the Act, and is extended to the actions of ASIC in order to preserve the Minister's discretion over the regulators' conduct under the Act.

20.11 In addition, section 284 is amended by item 21 to provide that APRA and ASIC must give to each other copies of reports of any investigation carried out under the Act.

20.12 To assist ASIC and APRA to co-operate, new section 298A (item 22) enables either regulator to appoint a 'member of staff' of the other regulator to carry out the functions of an 'authorised person' (defined in item 5) under the Act. Item 6 therefore inserts a definition of the expression 'member of staff ' into section 10. It is expected that ASIC and APRA will enter a memorandum of understanding which will refer to such provisions and other matters.

Change of regulator and regulator's name

Items 1, 3, 4, 9, 12 20, 23, 28, 31 222

20.13 Until the commencement of the proposed Financial Sector Reform (Amendments and Transitional Provisions) Act (the FSR Act), the Insurance and Superannuation Commissioner is responsible for supervising all aspects of compliance with the Act, and conducts both market integrity/consumer protection and prudential regulation. On commencement of the proposed FSR Act, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist.

20.14 Schedule 16 repeals references in the Act to the Insurance and Superannuation Commissioner and replaces them with references to ASIC or APRA where appropriate. Item 1 of Schedule 16 amends the objects clause of the Act (section 3) to provide that APRA and ASIC will supervise superannuation funds, approved deposit funds and pooled superannuation trusts. In the case of provisions that are referable to both ASIC and APRA, the expression 'the Regulator' replaces references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner'. Item 9 inserts a definition of 'Regulator' into section 10 of the Act. The items which insert references to the Regulator in place of references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner' are 19 and 169 222.

20.15 Items 3 and 4 insert definitions of 'APRA' and 'ASIC' into section 10. The items which insert references to APRA in place of references to the 'Insurance and Superannuation Commissioner', the 'ISC' or the 'Commissioner' are: 14; 15; 18; 28 and 31 155.

20.16 The items which insert references to ASIC in place of references to the 'Insurance and Superannuation Commissioner' or the 'Commissioner' are 17 and 156 168.

20.17 Because the Act no longer refers to regulation conducted by a natural person (the Insurance and Superannuation Commissioner), but rather to the acts of an agency (ASIC or APRA), the Act no longer uses the expressions 'he or she' or 'his or her' when referring to the Commissioner. Amendments of the Act to refer to 'it' or 'its' are in items 12; 13; 16 and 23.

20.18 Similarly, because ASIC and APRA are not natural persons, references to documents in writing signed by the Insurance and Superannuation Commissioner are amended to refer to documents prepared 'in writing'. Subsection 265(1) is amended to clarify that ASIC and APRA may appoint an inspector under that provision in this way (item 20).

Repeal of provisions

Items 7, 8, 10, 11, 24 27 and 29 - 30

20.19 Some of the provisions in the Act deal with general administrative matters which are more appropriately dealt with in the *Australian Securities and Investments Commission Act 1989* and the proposed *Australian Prudential Regulation Authority Act*. For example, both the *Australian Securities and Investments Commission Act* and the proposed *Australian Prudential Regulation Authority Act* include comprehensive provisions dealing with the delegation of powers by the regulators. For this reason, it is no longer necessary to include in the Act a separate power to delegate functions under the Act. Therefore, the delegation power in section 351 of the Act is repealed.

20.20 Similarly, the annual reporting responsibilities of ASIC and APRA under the *Commonwealth Authorities and Companies Act 1997* are dealt with in the *Australian Securities and Investments Commission Act* and the proposed *Australian Prudential Regulation Authority Act*. It is therefore no longer necessary to retain section 352 of the Act.

20.21 The secrecy provision in the Act (section 346) deals with the manner in which the ISC was required to treat information gathered by it about superannuation entities in the course of conducting its functions. This provision is broadly consistent with the secrecy provisions administered by the ISC under other legislation for which it had responsibility, eg the *Retirement Savings Account Act 1997* and *Life Insurance Act 1995*. However, it is different from the secrecy regime under which the ASC operated in relation to its corporate law functions.

20.22 The proposed *Australian Prudential Regulation Authority Act* contains a secrecy provision governing all of APRA's activities. Section 127 of the *Australian Securities and Investments Commission Act*, which previously related only to corporate regulatory functions, will be extended to cover ASIC's new functions in insurance and superannuation regulation, so that ASIC will be able to perform all of its functions under the same secrecy regime. Therefore section 346 is also repealed.

20.23 The items which repeal superfluous powers, functions and definitions in the Act are: 7; 8; 10; 11; 24 - 27; 29 and 30.

Schedule 16, Parts 7 and 8: Amendments to take account of the Superannuation Legislation Amendment Act 1998 and the Taxation Laws Amendment Act (No. 3) 1998

Items 223 233

20.24 The purpose of Parts 7 and 8 of Schedule 16 is to amend the Act taking into account the changes in the proposed *Superannuation Legislation Amendment Act 1998* and the proposed *Taxation Laws Amendment Act (No. 3) 1998*, to reflect the change of

regulatory responsibilities under the proposed FSR Act. References to the Insurance and Superannuation Commissioner in provisions of the Act amended by Part 1 of Schedule 2 to the proposed *Superannuation Legislation Amendment Act 1998* and in Part 3 of Schedule 5 to the proposed *Taxation Laws Amendment Act (No. 3) 1998* are repealed and references to ASIC, APRA or the Regulator, as appropriate, are substituted.

20.25 The items which substitute references to APRA in place of references to the Insurance and Superannuation Commissioner are 223 - 229. The items which substitute references to ASIC in place of references to the Insurance and Superannuation Commissioner are 232 and 233. The items which substitute references to the Regulator in place of references to the Insurance and Superannuation Commissioner are 230 and 231.

21

Schedule 17 Amendment of the Superannuation (Resolution of Complaints) Act 1993

The purpose of Schedule 17 is to transfer regulatory responsibility for the *Superannuation (Resolution of Complaints) Act 1993* (the Act) to ASIC. The Act establishes the Superannuation Complaints Tribunal and sets out its procedure. A number of provisions of the Act refer to the Insurance and Superannuation Commissioner.

Commencement

21.1 Schedule 17 will commence on the commencement of the proposed *Australian Prudential Regulation Authority Act 1998*.

Change of name of regulator

Items 1 11

21.2 Prior to the commencement of the *Financial Sector Reform (Amendments and Transitional Provisions) Act* (the Act), the Insurance and Superannuation Commissioner was responsible for certain functions referred to in the Act. On commencement of Schedule 11, the *Insurance and Superannuation Commissioner Act 1987* will be repealed and the office of Insurance and Superannuation Commissioner will no longer exist.

21.3 Schedule 17 therefore amends references in the Act to the 'Insurance and Superannuation Commissioner' by replacing them with references to ASIC, APRA or the regulator, as is appropriate.

21.4 References to the Commissioner will be amended to refer appropriately to ASIC, APRA or the Regulator. The relevant items are items 4 11.

21.5 The note to the definition sections which points to the relevant definitions in the *Superannuation Industry (Supervision) Act 1993* has been amended to refer to the relevant new definitions of APRA, ASIC and Regulator (Item 1).

21.6 The definition of 'death benefits' which refers to a decision under the *Superannuation Industry (Supervision) Act 1993* has been amended to refer to APRA, which will be the decision-maker under the relevant provision of that Act (Item 2).

21.7 The Act empowers the Tribunal to give details of a settlement to the Commissioner that it thinks may require investigation by the Commissioner

(subsection 31(2)). References to the Commissioner in this provision are to be amended to 'Regulator', that is, either ASIC or APRA, depending on the circumstances (Item 3).

21.8 When the reference to 'Commissioner' refers to the Commissioner of Taxation, the reference will not be amended.

22

Schedule 18 Amendment and repeal of other Acts

Schedule 18 provides for miscellaneous amendments and repeals of Acts consequent upon legislation proposed in the schedules to this Bill and other Bills included in the financial system reform package.

Commencement

22.1 Except for items 41 and 42, Schedule 17 commences on the commencement of the proposed *Australian Prudential Authority Act 1998*. If the proposed *Public Service Act 1998* commences before the proposed *Australian Prudential Regulation Authority Act*, items 41 and 42 of Schedule 18 come into effect at the time of the commencement of the proposed *Australian Prudential Regulation Authority Act*. If the proposed *Public Service Act* commences after or at the same time as the proposed *Australian Prudential Regulation Authority Act*, items 41 and 42 come into effect immediately after the commencement of the proposed *Public Service Act*.

Part 1 - Amendment and repeal of levy acts

Items 1 to 39

22.2 The existing *Life Insurance Supervisory Levy Act 1989*, *General Insurance Supervisory Levy Act 1989, Insurance Supervisory Levies Collection Act 1989 and Retirement Savings Accounts Supervisory Levy Act 1997* will all be repealed (items 1 4). These Acts are to be replaced by the proposed levy imposition and collection Bills.

22.3 References in the *Superannuation Supervisory Levy Act 1991* and the *Superannuation Entities (Taxation) Act 1987* to "the Commissioner" are to be substituted with "APRA". References in these Acts to "RSA providers" are to be deleted as these entities are to be levied under the new imposition Act (items 7 14, 19 33).

22.4 The *Superannuation Supervisory Levy Act 1991* will be amended so that only excluded superannuation funds are liable for a levy under this Act (items 37 39). This will require a reference to excluded superannuation funds in Part IIIAA of the *Superannuation Entities (Taxation) Act 1987* (items 16 - 18).

22.5 To reflect this change in those bodies subject to levies, the title of the imposition Act is to be amended to "Superannuation (Excluded Funds) Supervisory Levy Imposition Act 1991 (item 36). The title of the collection Act is also to be amended to "Superannuation (Excluded Funds) Taxation Act 1987 (items 5, 6 and 15).

22.6 Section 21 of the *Superannuation Entities (Taxation) Act 1987* has been repealed as reasonable benefits limit calculations are now included in the *Income Tax Assessment Act 1936* (item 34).

Part 2 Amendment of other Acts

Item 40

22.7 Item 40 amends a reference in section 40A of the *Acts Interpretation Act 1901* to the "*Australian Securities Commission Act*", so that the provision refers instead to the "*Australian Securities and Investments Commission Act*".

Items 41 and 42

22.8 These items are designed to incorporate relevant provisions of the proposed *Public Service Act 1998* into the proposed *Australian Prudential Regulation Authority Act 1998*.

Items 43 and 44

22.9 Items 43 and 44 amend references in subsections 4(1) and 39(1) of the *Corporations Act 1989* to the "*Australian Securities Commission Act*", so that the provisions refer instead to the "*Australian Securities and Investments Commission Act*".

Item 45

22.10 Item 45 amends a reference in paragraph 4AB(3)(b) of the *Crimes Act* to the "*Australian Securities Commission Act*", so that the provision refers instead to the "*Australian Securities and Investments Commission Act*".

Item 46

22.11 The *Financial Corporations (Transfer of Assets and Liabilities) Act 1993*, describes the Treasurer's power to approve the transfer of assets and liabilities following the granting of a banking authority. Item 46 will allow the Treasurer to delegate this power to APRA and APRA staff members.

Item 47

22.12 Item 47 amends a reference in paragraph 27(9)(b) of the *Financial Transactions Reports Act 1988* to the "*Australian Securities Commission Act*", so that the provision refers instead to the "*Australian Securities and Investments Commission Act*".

23

Schedule 19 Transitional Provisions

Schedule 19 outlines the necessary transitional provisions required to smooth the passage to the new regulatory/legislative framework outlined in this and other Bills attached to the broader package.

Commencement

23.1 Schedule 19 commences on the day on which this Bill receives the Royal Assent.

Part 1 Transitional provisions relating to amendments of the Banking Act 1959

23.2 The following items will preserve the current authorities and exemptions provided by the Treasurer and the various State Supervisory Authorities (SSAs) as if they were issued by APRA under the new regime. In addition, existing activities commenced by or with RBA, such as applications and investigations, will be continued as if commenced by or with APRA.

23.3 The items will also enable APRA to smooth the transition of prudential regulation for deposit-taking institutions under the State regime to the *Banking Act 1959* subject to Ministerial agreement.

Item 1

23.4 This item will enable the amendments to the Banking Act to commence with the commencement of APRA.

Item 2

23.5 This item will ensure that authorities to carry on banking business made under subsections 9(1) and 9(3) of the Banking Act prior to the commencement of APRA Act are preserved and these authorities will be treated identically to subsection 9(3) authorities under the amended Act.

Items 3 and 4

23.6 These items will enable applications to the Treasurer under subsection 9(3) received before the commencement of APRA to be processed by APRA and require APRA, rather than the Treasurer, to fulfil any undischarged publication obligations with respect to authorities under section 9.

Item 5

23.7 This item will enable APRA to transfer building societies and credit unions regulated under the Financial Institutions Code (FIC) to the Commonwealth scheme without these bodies having to apply under subsection 9(3) of the *Banking Act 1959*. APRA will have the power to make a determination for an individual FIC body or class of bodies and may subject the authorities to the same, additional, varied or new conditions. These determinations will be disallowable instruments and will be published in the Gazette.

23.8 APRA will not be able to make a determination unless the Treasurer and the State or Territory Minister responsible for the administration of that FIC have agreed that the body or class of bodies should be covered by the amended *Banking Act 1959*. This process will be consistent with facilitating the efficient transferral of prudential regulation for building societies and credit unions to the Commonwealth upon agreement of the relevant governments.

23.9 Until determinations are made FIC bodies may be provided with exemptions from the application of the *Banking Act 1959* under section 11.

Item 6

23.10 This item will preserve all existing exemption orders made by the Treasurer as if they were exemption orders made under the amended legislation. This transitional provision does not however preclude the possibility that these exemptions may be reviewed by APRA as the circumstances of these institutions change.

Item 7

23.11 This item will deem approvals received from the Governor of the RBA for foreign banks to accept deposits from persons in Australia to have been made by APRA under subsection 11E(2).

Item 8

23.11 Item 8 explains how the RBA's role in depositor protection matters is either transferred to APRA or lapses. If:

- an institution is obliged to provide information to the RBA, that information should be supplied to APRA;

- the RBA has appointed an investigator that appointment shall continue as if the appointment had been made by APRA;

- the RBA has assumed control of an institution's business, that control will be transferred to APRA (and regulations may provide for any unforseen complications associated with such a transfer);

- a bank had applied to the Federal Court under subsection 14(6) of the old Act to end RBA control of that bank such proceedings will lapse because, under the new reforms, the statutory manager replaces the bank's board and so is not separate from the bank;

- the RBA is under an obligation to publish a notice of a matter, the discharge of that obligation will fall to APRA; and

- if the RBA has authorised a bank to hold assets of a value less than its liabilities, that authorisation shall continue as if it were an authorisation made by APRA.

23.12 In addition, section 15 of the old Act, relating to indemnities, will continue to have effect (despite being repealed) in relation to things done or not done before that commencement.

Item 9

23.13 This item will preserve the effect of any instruments made with respect to non-callable deposits under the old legislation and will extend the coverage of NCDs from banks to authorised deposit-taking institutions.

Item 10

23.14 This item will provide that when the non-callable deposit provisions in Division 3 are repealed on a date specified by Proclamation (rather than on the date of APRA commencement) any ADI with a NCD account held with the RBA will be repaid these funds as soon as practicable.

Items 11 and 12

23.15 These items will continue the effect of any regulations in force with respect to the control of interest rates under section 50 and the collection and publication of information under Part VI of the old legislation as if these regulations were made after the commencement of APRA. In addition, these regulations will be applied to ADIs in the same way as they covered banks.

Item 13

23.16 This item will deem any investigator appointed by the RBA and still undertaking an investigation pursuant to section 61 to have effect as if it were an appointment by APRA under the amended Act.

Item 14

23.17 This item will require any bank or person that was obliged to provide information to the RBA under section 62 prior to the commencement of APRA to provide this information to APRA.

Item 15

23.18 This item preserves the continuity of an order relating to RBA control of a bank by ensuring that it has effect as if it had authorised APRA. Similarly, the exercise of control is transferred to APRA (and regulations may provide for any unforeseen complications associated with such a transfer).

Item 16

23.19 This item will preserve the existing consents received from the Treasurer for the use of the word "bank" or bank-related words by financial businesses prior to the commencement of APRA. Any conditions attached to these consents will be taken to be conditions applying under section 66 of the amended Act.

Item 17

23.20 This item will enable financial institutions that were authorised to carry on banking business in Australia under subsection 9(3) of the old Act to be taken as having received consent from APRA to use the word "bank" under the amended section 66. This provision will prevent these institutions from having to apply for consent to use the word bank.

Item 18

23.21 This item will preserve the existing consents received from the Treasurer for the establishment or maintenance of representative offices of overseas banks prior to the commencement of APRA. Any conditions attached to this consent will be taken to be conditions applying under section 67 of the amended Act.

Item 19

23.22 This item preserves existing regulations made under section 71 of the old Act and replaces references to the RBA and banks with APRA and ADIs respectively as far as practicable.

Part 2 Transitional provisions relating to amendments of the Financial Corporations Act 1974

23.23 This part preserves the list of registered corporation, exemptions and determinations made under the *Financial Corporations Act 1974* prior to the commencement of APRA.

Item 20

23.24 This item will insert definitions of the old and amended Act which are effectively pre and post the commencement of APRA.

Item 21

23.25 Exemptions or determinations that were in force immediately prior to APRA commencement will continue to have effect.

Item 22

23.26 The list of categories of registered corporations prepared by the Treasurer will continue to have effect as if the Governor of the RBA had prepared the list. Any undischarged obligations of the Treasurer will be assumed by the Governor of the RBA. In addition, any determination in force or request under section 10 will continue to have effect.

Item 23

23.27 Any exemption on furnishing of statistics made by the Treasurer under subsection 11(14) will continue to have effect under the amended Act.

Part 3 Transitional Provisions Relating To The Establishment Of APRA And The Repeal Of The Insurance And Superannuation Commissioner Act 1987.

Divisions 1 - 3

23.28 These provisions will come into effect with the commencement of the *Australian Prudential Regulation Authority Act 1998*.

23.29 This schedule essentially provides for the transfer of staff from the Reserve Bank of Australia (RBA) and the Insurance and Superannuation Commission (ISC) to APRA and the transfer, as appropriate, of the assets and liabilities of the ISC to APRA or Australian Securities and Investments Commission (ASIC).

Item 24 Interpretation

23.30 This item provides various definitions that are used in this schedule.

Item 25 Transfer of Staff from the Reserve Bank

23.31 This item provides for the transfer of specified staff from the RBA to APRA. A determination transferring staff from the RBA will only occur following consultation between both APRA's Chief Executive Officer (CEO) and the Governor of the Reserve Bank as it would not be appropriate for either the RBA Governor or the CEO of APRA to unilaterally determine who is to become an APRA employee. The 'consultation' approach provides a balance between the respective employment interests and obligations of the RBA and APRA.

23.32 As Commonwealth employees, separate transfer provisions for ISC staff are not required. ISC staff will be transferred under section 81C of the *Public Service Act 1922* and their accrued rights and entitlements will be protected under the Part IV mobility provisions of the same Act.

Item 26 Terms and conditions

23.33 This item is essentially designed to protect the interests of RBA staff transferring across to APRA. While APRA may vary the terms and conditions of its employees, this provision will ensure that any revised terms and conditions relating to remuneration are no less favourable, as a whole, to that which the employees had enjoyed immediately before they transferred across to APRA.

23.34 Sub-item (4) is designed to preclude any RBA staff member taking redundancy benefits from the RBA before taking up a position with APRA.

Item 27 Statement of Accrued Benefits

23.35 This item is included to ensure that RBA employees transferring across to APRA and APRA management are fully aware of RBA staff accrued entitlements before they become APRA employees.

Item 28 Transfer of Assets

23.36 This item provides for the Treasurer to declare certain specified assets of the ISC to be those of vest in APRA or ASIC. As the ISC is not a separate legal entity from the Commonwealth, it is necessary to refer to 'the Commonwealth' when talking about the assets and liabilities of the ISC in this item.

Item 29 Transfer of liabilities

23.37 This item provides for a similar arrangement to that under Item 28, but in this case it addresses liabilities rather than assets.

Item 30 Transfer of records

23.38 To remove any doubt that may exist, this item explicitly provides for the transfer of records that relate to the functions of APRA or ASIC to APRA or ASIC.

Item 31 Exemption from stamp duty and other taxes

23.39 This item provides for an exemption from Commonwealth, State and Territory taxes of matters arising out of the transfer of assets and liabilities to APRA or ASIC.

Item 32 - Delegation

23.40 This item provides for the Treasurer to delegate any or all of his powers under this Division to an officer of the Treasury Department.

Division 4

23.41 This Division facilitates the transfer of roles to ASIC and APRA. The items provide for the continued operation and validity of instruments made by the Insurance and Superannuation Commissioner and for the substitution of APRA and/or ASIC as parties to legal proceedings in which the ISC was a party.

23.42 Provisions of this type are not required to facilitate the transfer of functions and powers from the Australian Securities Commission to ASIC because they are the same legal entity and references to the Australian Securities Commission will be taken to be references to ASIC as appropriate by virtue of interpretation provisions (see, in particular, Item 34 of Schedule 1).

Item 33 - Definitions

23.43 This item defines a number of terms used in this Part.

"commencement" means the date of commencement of the legislation which repeals the *Insurance and Superannuation Commissioner Act 1987* (see Schedule 11).

Items 34 and 35

23.44 These items deal with the continued effect of instruments made or issued by the Insurance and Superannuation Commissioner under Acts which, under the proposed arrangements following the cessation of the ISC, will be administered by ASIC and/or APRA. Which regulator is responsible for administering provisions of particular Acts

following the cessation of the ISC is determined by items in the other Schedules to this Bill.

23.45 Instruments made by the Insurance and Superannuation Commission that, under the new administrative scheme for those Acts, could be made by APRA and/or ASIC, continue in force as if they were made by the appropriate regulator under the new administrative scheme.

23.46 Instruments which were made by the Insurance and Superannuation Commission to have effect for a limited period will only continue in force under the new arrangements until the expiration of that period.

23.47 The items deal with those instruments made or issued by the Insurance and Superannuation Commissioner under those Acts which, under the proposed administrative scheme following the cessation of the ISC, will be administered by APRA; those which will be administered by ASIC; and those under which both regulators will perform roles.

Item 36 Proceedings etc by or against the ISC

23.48 This item provides for the substitution of the responsible agency (ASIC and/or APRA) for the Insurance and Superannuation Commissioner as a party to proceedings in court or tribunal proceedings.

23.48 To the extent that a proceeding in which the Insurance and Superannuation Commissioner was a party relates to a function which is the responsibility of APRA under the new administrative scheme, APRA is substituted as a party. Similarly, to the extent that a proceeding in which the Insurance and Superannuation Commissioner was a party relates to a function which is the responsibility of ASIC under the new administrative scheme, ASIC is substituted as a party.

23.49 The item does not alter the powers of a court or tribunal might otherwise have to make orders or give directions about whether APRA and/or ASIC continue as a party to proceedings, or the rights in the proceeding of any of the parties.

Item 37 Continued operation of Part IX of the Insurance Act

23.50 This item provides for the continued operation of Part IX of the Insurance Act, despite its repeal in Schedule 9, for bodies corporate to which it applied immediately before the commencement of APRA.

Part 4 - Transitional provisions relating to amendments of the Reserve Bank Act 1959

Item 38

23.51 This item deals with interpretations of the phrases 'amended Act', 'APRA commencement' and 'old Act'. The 'old Act' is that which stands before the amendments in Schedule 14 take effect.

Item 39

23.52 This item outlines the transitional arrangements in the case that there are 2 Deputy Governors of the RBA at the time that APRA is established (and the number of deputy governor positions is reduced to one). The provision will permit the persons occupying those positions to continue under the provisions of the old Act. However, once one of the deputy governor positions is vacated, the Act will take effect with one deputy governor.

Item 40

23.53 This item ensures that the terms of incumbent RBA Board members continues to the presently scheduled termination date despite the repeal of subsection 14(5) of the RBA Act.

Item 41

23.54 This item provides that the repeal of section 81 of the RBA Act, where it relates to investigations on prudential matters, should not have any impact on investigations that are currently being undertaken. The RBA will be required to report on such investigations up to the date of transfer to APRA.

Part 5 Transitional provisions relating to the Payment Systems (Regulation) Act 1998.

Item 42

23.55 This item ensures that all corporations that are the holders of the stored value of a purchased payment facilities within a class of purchased payment facilities are treated under the Act as if they had been granted an authority under proposed section 23 of the Payment Systems (Regulation) Bill 1998. This provision ensures that existing holders of the stored value do not breach the provisions of that Bill upon its commencement.

Part 6 Transitional provisions relating to levies

Item 43

23.56 This Part allows for transitional arrangements relating to levies to be dealt with in regulations. This will remove the possibility of a leviable entity paying levies under both the existing arrangements and the proposed arrangements.

Part 7 Regulations dealing with transitional matters

Item 44 and 45

23.57 Items 44 and 45 provide that the Governor-General should be given the power to make regulations relating to other transitional matters arising as a result of the amendments and repeals included in this bill.