

24 May, 2013

Mr Neil Grummit
General Manager, Policy Development
Policy Research and Statistics
Australian Prudential Regulation Authority
GPO Box 9836
SYDNEY NSW 2001

Submission to APRA Discussion paper on the Banking Act exemptions and section 66 guidelines

From Anglican Financial Services

Dear Mr Grummit

We welcome the opportunity to respond to APRA on the issue of the Banking Exemption provided to Religious Charitable Development Funds.

- Anglican Financial Services (ANFIN) is an operating entity of The Corporation of the Synod of the Diocese of Brisbane and is not separately incorporated.
- In addition to providing Treasury services to entities comprising the denominational or other affiliates within the Anglican Diocese of Brisbane, ANFIN is also designed as a means for individuals who wish to support the activities of the Anglican Church community, and for whom profit may not be the primary consideration.
- ANFIN manages circa \$220 million in assets, with net assets of approx \$16.5 million. Our capital adequacy policy aims to keep ANFIN's reserves at a minimum of 10% of risk adjusted assets. We maintain a minimum balance sheet liquidity requirement of 12% of liabilities (excluding capital).
- The funds provided by individuals to ANFIN support the Diocese's ability to fund mission activities in hospital chaplaincy, youth ministry, community services, social welfare, aged care, and education.
- With regards to the investment products available through ANFIN, the Diocese limits its marketing activities to those individuals already within the Anglican community. ANFIN does not actively seek to compete for retail investor funds in competition with APRA authorised institutions or ASIC regulated schemes.

- We submit that the rationale in the existing historical exemption to demarcate the activities of RCDFs from ADIs offering retail banking services is still pertinent.
- To the extent that APRA believes that an individual is still prone to confuse a RCDF with an APRA supervised ADI, and that the source of this potential confusion is related to:
 - The language used to describe the RCDF
 - The functional characteristics of an RCDF's products/services
 - The language used to describe an RCDF's products

Then we submit that there is scope for further developing the conditions under the Banking exemption to address this potential for confusion.

- To the extent that APRA is concerned that the RCDF sector is appropriately meeting the conditions of its exemptions; whether disclosure practices are effective; whether consumers understand that the sector is unregulated; and whether the sector should be prevented from using terms and language describing products and services of ADIs, then we submit that these concerns can and should be addressed through improved enforcement measures and/or modification of the existing banking exemption, rather than through its removal.

Our responses to the issues highlighted in the APRA Discussion paper are set out below.

Issue 1: Confusion of an RCDF with an APRA supervised ADI

*In this Discussion Paper, APRA is proposing requirements **aimed at reducing the likelihood** that an investor, and particularly **a retail investor**, in an RFC would **confuse such an investment with an ADI deposit** or other deposit-like product*

APRA also believes that similar measures are appropriate in respect of RCDFs that currently accept funds from retail investors

ANFIN response:

- a) APRA has offered as a rationale for the proposed changes, that the public response to recent RFC failures has demonstrated that, even with such disclosures as required under the Banking Exemption Act, investors may still consider that the security of their investment is equivalent to a deposit with an ADI.
- b) APRA concludes from this that it is therefore not appropriate to continue to exempt an RCDF from the need to be authorised under the Banking Act where it is offering products to retail investors.
- c) We would note the basis of APRA's concern as set out in its discussion paper is the collapse of an RFC, not the failure of RCDFs, for which APRA does not cite any known failures in Australia. The International Monetary Fund paper which APRA cites as a source underlying its proposals, expresses concern and recommendations in relation to RFCs – not RCDFs - and notes that “there are major global institutions benefitting from this exemption.”
- d) We submit that ANFIN is not a major global institution, and highlight that any benefits that accrue to the Anglican Diocese of Brisbane from the placement of funds by retail investors with ANFIN, are to support our mission activities in community services, social welfare, aged care, and education.
- e) We submit that APRA's issue as described in the discussion paper appears to be substantively related to the language and nature of the warning around the products/services provided by RCDFs, rather than the actual provision of those products/services. The character of the financial institution is not in issue in this discussion paper, what APRA appears to be implying to be insufficient is the warning to retail investors.
- f) We submit that APRA's proposed solution is not in relation to what it identifies to be the problem, namely - confusion on the part of retail investors in relation to the nature of the service/product offered by a RCDF.
- g) We accept APRA's implied proposition that to the extent that a retail client reasonably considers to have placed their funds with an APRA supervised banking business, then they *are* entitled to the expectation of the levels of protection provided for under the *Banking Act* by such a banking business.
- h) Notwithstanding the above, we note that there is already the basis under the existing conditions of the Banking Exemption Act (Schedule 2) to ensure that retail investors are made aware that they are NOT investing with an APRA supervised financial institution.

- i) In light of APRA's concern that there may still be confusion on a retail investors' part, we propose that APRA consider an alternative recommendation that RCDFs can continue to receive funds from retail investors, subject to added conditions under the Banking Exemption which place a greater onus on the RCDF to ensure that retail investors are aware of, and acknowledge the special nature of an RCDF.
- j) An example of increased requirement under the Banking exemption order may be for a requirement for an RCDF to maintain records of each retail client's explicit acceptance of the terms of an investment with an RCDF, and an acknowledgement that in investing with the RCDF the client forgoes any protection under the Banking Act provisions for ADIs. The RCDF could be required to provide a declaration or other proof/undertaking to APRA that it has obtained that confirmation, and maintains those records.

Issue 2: Offering of products by an RCDF likely to cause confusion

The proposed reforms will remove the ability of non-prudentially regulated entities to offer products to retail investors that look like deposit or transactional banking accounts provided by ADIs.

ANFIN response:

- a) We accept APRA's recommendation to change the exemption order to exclude the use of the word 'deposit' or any of its derivatives by an RCDF.
- b) Notwithstanding the above, in light of APRA's concern that a retail client may confuse an investment product offered by an RCDF with a product that offers similar protections under the Banking Act, then we would again submit that there is already the basis under the existing conditions of the Banking Exemption Act to ensure that investors in an RCDF do not perceive that the RCDF's products are subject to the same prudential supervision and Banking Act provisions enjoyed by the products of an APRA supervised ADI.
- c) We submit that the more appropriate response on APRA's part to concerns about the use of retail banking language by a RCDF to describe its products and services, is to amend the conditions of the Banking exemption order.
- d) To the extent that APRA believes there is still ongoing potential confusion on the part of retail investors, then we recommend that APRA considers maintaining within the banking exemption order the ability of an RCDF to accept retail funds, but with the added restriction on the use of certain terminology that APRA considers to be prone to creating confusion on the part of retail investors.

Issue 3: Providing greater safeguards

...the public response to recent failures in the non-prudentially regulated financial sector has highlighted the risks to retail investors associated with such investments, and the need for greater safeguards

ANFIN response:

- a) We believe that the actions identified above in response to Items 1 and 2 represent reasonable steps to remove the potential for confusion on the part of retail investors that APRA is seeking to address.
- b) We would again note the basis of APRA's concern as cited in its discussion paper is the collapse of an RFC, not the failure of RCDFs, for which APRA does not cite any known failures in Australia.
- c) The IMF's own recommendation in its paper "*Australia: Basel Core Principles for Effective Banking Supervision—Detailed Assessment of Observance*" is for APRA to revise the conditions of exemption from Section 11 of the Banking Act for RFCs. There is no reference to RCDFs in that recommendation.
- d) We note the additional point raised by the IMF in its paper that "APRA is subject to an unnecessary reputational risk arising from this source", which we infer substantively to be a reference to RFCs and the "major global institutions" the IMF notes are benefiting from the exemption.
- e) APRA has identified in its discussion paper that retail funds with RCDFs in Australia are in the order of \$1,100 million. The RBA reports \$2,960,371 million in liabilities held by ADIs and RFCs as at 31 March 2013¹. The retail investor liabilities held by RCDFs equates to approximately 0.04% of the liabilities held by those other institutions.
- f) We submit that there is limited reputational risk to APRA generated by RCDFs, and that the inclusion of RCDFs in APRA's response to the IMF's concerns about RFCs is not justified.
- g) We further submit that an RCDF's conduct in making investments is not governed by the same commercial imperatives to maximise profit as an RFC. This gives an RCDF such as ANFIN the scope to take a far more conservative approach in its lending activities, capital adequacy and liquidity management.
- h) To the extent that APRA is concerned that the conditions of the current exemption order offered to an RCDF does not provide sufficient transparency around the operation of an RCDF to a retail investor, then we would propose that APRA consider continuing the exemption order to allow RCDFs to accept retail funds, conditional on the RCDF making its Board management policies (or similar) relating to capital adequacy and liquidity management available to its retail investors, in addition to its audited statement of accounts verifying compliance with those policies.

¹ Source: <http://www.rba.gov.au/statistics/tables>

Issue 4: Continued Exemption for RCDFs operating as de facto Treasuries

APRA considers it is appropriate that RCDFs operating as de facto corporate treasuries for their affiliates, and not taking funds from retail investors, continue to receive a Banking Act exemption. APRA proposes that this exemption order will include conditions that the RCDF will

- *Not use the word 'deposit' or its derivatives in relation to its activities*
- *Not offer Bpay facilities*
- *Not offer ATM, EFTPOS*
- *Not offer cheque account facilities*

ANFIN response:

- a) Notwithstanding our submission that APRA should continue to allow RCDFs to accept retail funds, we agree with APRA's recommendation to extend the Banking Act exemption to RCDFs that are acting as de facto corporate treasuries and do not accept funds from individuals.
- b) We accept APRA's recommendation to change the exemption order to exclude the use of the word 'deposit' or any of its derivatives by an RCDF
- c) We request clarification from APRA as to what would constitute an affiliate under its recommendation. We submit that the definition provided for under Schedule 2 (4) of the Banking Exemption Act is the appropriate basis for such a definition
- d) We further submit that an exemption order offered to RCDFs operating as de-facto treasuries and not taking retail funds should be broadened to accommodate the ability of such an RCDF to take funds from wholesale investors who would not fall within the definition of an affiliate.
- e) We request further clarification from APRA that it did not intend to introduce a new condition excluding the offering of cheque facilities to affiliates. We submit that in the capacity of corporate treasury, we would only offer cheque account facilities to those affiliates already allowed for under Schedule 2 (4) of the existing Banking Exemption Act.
- f) We submit that a RCDF operating as a de facto Treasury should have the ability to offer Bpay to its affiliates, as in substance this service represents no more risk than the use of a cheque account.

Issue 5: Transitional arrangements

APRA proposes to withdraw the current RCDF Exemption Order for RCDFs accepting investments from retail investors as from 28 June 2014

ANFIN response:

- a) As per our response to Items 1 through 3, we submit that the removal of this exemption order is unjustified, unnecessary and inconsistent with the issues identified by APRA in its discussion paper. However, cognisant that this submission may represent our only opportunity to respond to APRA on this matter, we raise the following points.

