

FINANCIAL CLAIMS SCHEME

Questions and Answers

What is the Financial Claims Scheme?

The Financial Claims Scheme (FCS) was established by legislation in October 2008. Its purpose is to protect depositors in authorised deposit-taking institutions (ADIs) - such as banks, building societies and credit unions - from loss on their deposits (up to a specified limit) and give them prompt access to their deposits if their ADI becomes insolvent.

The FCS also protects certain policyholders and other claimants (certain individuals, small businesses, family trusts and not-for-profit organisations) who make valid claims on a general insurance company in a situation where the insurance company is insolvent.

When does the Financial Claims Scheme apply?

In the case of an ADI, the FCS applies when the Australian Prudential Regulation Authority (APRA) has decided to use its powers under the *Banking Act 1959* to place the ADI into wind-up (liquidation) and when the Treasurer determines that the FCS will be applied to that ADI. The FCS would only be used in a situation where an ADI is insolvent or severely under-capitalised, and where the best course of action is to close the ADI and wind it up.

In the case of a general insurance company, the FCS applies when APRA has determined that the insurance company is insolvent, the insurance company has been placed into judicial management and when the Treasurer determines that the FCS will be applied to the insurance company. The FCS would only be used in a situation where a general insurance company is insolvent and where the best course of action is to close the insurer and wind it up.

Who is responsible for administering the Financial Claims Scheme?

APRA is responsible for the administration of the FCS and for making payments to depositors and policyholders.

Who provides the money to make payments under the Financial Claims Scheme?

The Government initially provides the funds to make payments under the FCS. Monies paid under the FCS are then recovered from the ADI or general insurance company in the winding up process. There is provision to make up any shortfall by applying a levy on the ADI or general insurance sector.

Financial Claims Scheme applicable to deposits

Which deposit-taking financial institutions are covered by the Financial Claims Scheme?

The FCS applies to deposits held with Australian ADIs - banks, building societies and credit unions. A list of ADIs can be obtained from the APRA website - www.apra.gov.au

The FCS does not apply to deposits held in the following types of financial institution:

- Australian branches of foreign banks - because they are not permitted to take retail deposits. Note that Australian branches of foreign banks can apply for a guarantee through the Australian Government Guarantee Scheme for a fee.
- Foreign subsidiaries of Australian-owned banks.
- Interest-bearing investments in finance companies and other institutions that are not ADIs supervised by APRA.
- Specialist Credit Card Institutions and Providers of Purchased Payment Facilities.

What deposits are covered by the Financial Claims Scheme?

The FCS applies to a wide range of deposits held with an ADI, including the following:

- Call accounts
- Term deposits
- Current accounts
- Cheque accounts
- Debit card accounts
- Transactions accounts
- Personal basic account
- Cash management accounts
- Farm management deposits
- Pensioner deeming accounts
- Mortgage offset accounts, either 100 per cent or partial offset, that are separate deposit accounts
- Trustee accounts
- Retirement Savings Accounts
- First home saver accounts that are deposit accounts

The FCS applies to deposits denominated in Australian dollars and in any other currency.

How much money is covered by the FCS?

The Commonwealth Government has issued a guarantee of deposits at ADIs up to \$1 million per depositor in any one ADI. The guarantee will remain until 12 October 2011. This means that, for the period through to 12 October 2011, depositors are protected against loss on their deposits up to \$1 million. Depositors with more than \$1 million in

deposits at a particular ADI will be able to access the guarantee if their ADI applies for and pays a fee in relation to the guarantee.

After 12 October 2011, the current Government guarantee on deposits will be removed. However, the FCS will continue to apply to deposits under the scheme for amounts up to a new limit to be determined by the Government. Depositors will therefore continue to be protected from loss on deposits up to that limit. The new limit will be announced well before the \$1 million government guarantee expires.

The FCS is applied on an aggregated basis across all eligible deposit accounts held by a particular depositor with the ADI being wound up. For example, under the current limit of \$1 million, if a depositor has three deposit accounts in an ADI, each with a balance of \$400,000, these will be added together and the FCS will protect the depositor for \$1 million. The remaining \$200,000 will not be guaranteed unless the ADI has applied for and obtained a guarantee for deposit balances above \$1 million.

In the case of joint accounts, a depositor's share of the joint account will be added to their other deposits and the FCS limit will be applied to the aggregated amount.

In the case of deposits denominated in a foreign currency, the amount will be converted into Australian dollars at the exchange rate prevailing at the time FCS is applied for the purpose of determining the FCS limit.

How will deposits be repaid under the Financial Claims Scheme?

APRA will aim to pay eligible depositors their money as quickly as possible.

As administrator of the FCS, APRA is responsible for determining the amounts payable to each depositor and for arranging the payments to depositors. The means of payment will be determined on a case-by-case basis. Options include:

- payment by cheque;
- electronic transfer of funds into bank accounts nominated by depositors at another ADI; or
- electronic transfer of funds into new bank accounts opened by APRA in the names of depositors in a designated ADI.

Depositors will be advised at the time of the means by which their deposits will be paid to them and what actions they need to take in order to access their money.

How quickly will payments be available?

It is intended that depositors will be able to access their funds (up to the limit applicable at the time) within a week or so of the FCS being invoked.

Financial Claims Scheme applicable to insurance

Which insurance companies are covered by the Financial Claims Scheme?

The FCS applies to insurance policies (other than certain types of excluded policies) provided by general insurance companies authorised by APRA. A list of these general insurers can be obtained from the APRA website - www.apra.gov.au

The FCS does not apply to insurance policies issued by life insurance companies.

Which types of insurance policies are covered by the Financial Claims Scheme?

The FCS applies to any insurance policy issued by a general insurance company, other than insurance policies excluded from the scheme. Regulations made from time to time will specify the types of policies excluded from the scheme. The exclusions include:

- insurance policies covered by state or territory mandated insurance cover, such as compulsory third party insurance and workers' compensation;
- reinsurance and retrocession; and
- insurance claims from persons, entities or third parties determined by APRA as having knowingly taken out insurance coverage to benefit from the FCS.

What types of policyholders and other claimants are protected under the Financial Claims Scheme?

The FCS applies to certain categories of policyholders with eligible insurance policies issued by general insurers supervised by APRA. It also applies to certain categories of third parties who are able to claim against a general insurer pursuant to a policy issued to another party by that insurer. The eligible claimants are:

- individuals who are Australian citizens or permanent residents;
- non-resident individuals who have insured against risks in Australia;
- small businesses, as defined in section 328-110 of the *Income Tax Assessment Act 1997*;
- Australian-based not-for-profit organisations; and
- family trusts established to hold property for private residential purposes.

Insurance policies held by medium and large businesses will not be covered by the FCS unless the claim is under \$5,000, in which case all policyholders and other claimants with valid claims are covered.

What protection does the Financial Claims Scheme provide?

The FCS covers eligible policyholders and other claimants for the amount payable by the insurer in respect of a valid claim. The FCS applies to all valid claims by eligible policyholders and other claimants lodged with the insurer within a specified period after the commencement of FCS. Eligible policyholders and other claimants will be given a specified period within which to make a claim on an insurer after its failure. This period is 12 months from the time that the insurer is brought under the FCS.

FCS does not apply to the unexpired insurance premium paid to the insurer before its failure. However, policyholders may receive some or all of the unexpired premiums from the liquidator of the general insurer, depending on the amount of assets in the insurer upon winding up.

How is the FCS amount payable determined?

APRA will determine the amount payable to eligible policyholders and claimants. This will be done on the basis of a standard claims assessment process. Claims will be assessed by a party appointed by APRA. This could be the failed insurance company, another designated insurance company or an agency appointed to process the claims. Policyholders and claimants will be advised of how claims should be made under the FCS.

If the insurance claim is under \$5,000, APRA will pay the amount that the policyholder or claimant would have been able to claim from the failed company under a valid claim.

If the insurance claim is over \$5,000, APRA will first determine whether the policyholder or claimant is eligible under the FCS. In the case of eligible policyholders and other claimants, the amount paid will be the full amount that the policyholder or claimant would have been entitled to for a valid claim under the insurance policy. If the policyholder or claimant is not eligible to be covered by the FCS (eg if the policyholder is a large corporation), they would need to establish with the liquidator that they have a valid claim against the insurer and may then be eligible to rank with other unsecured creditors in the liquidation of the insurer.

Claimants under the FCS do not have to be policyholders at the failed insurance company. They only need to have a valid claim under an insurance contract with that company issued by the insurance company before FCS was declared. For instance, individuals making a claim under their company's employer's liability insurance policy with the failed insurance company would be eligible for payment under the FCS.

Will policyholders be given time to find alternative insurance cover?

Yes. It is recognised that policyholders will need some time to find alternative insurance cover. The FCS will continue to cover policyholders and claimants for valid claims for 28 days following the declaration of FCS for a general insurer. After this time policyholders will be expected to establish alternative insurance cover.