



Response to Submissions

Religious charitable development funds

30 March 2016

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Preamble

In order to undertake banking business in Australia, a body must be incorporated and authorised by APRA as a deposit-taking institution. Under the *Banking Act 1959* (Banking Act), APRA may give an exemption from the need to be authorised, although an exemption will generally only be provided in limited circumstances and subject to certain conditions.

In April 2013, APRA released a discussion paper on the future operation of the exemption orders made under the Banking Act. That paper set out APRA's proposals to amend existing exemptions, including the exemption order for religious charitable development funds (RCDFs).

In August 2013, APRA released a response to submissions paper that set out the key matters raised in relation to APRA's proposed changes to the RCDF exemption order and, following consideration of submissions received, APRA's proposed revisions to the April 2013 proposals. Subsequently, APRA delayed the finalisation of the future operation of the exemption order pending the outcome of the Financial System Inquiry and the Government's consideration of possible legislative approaches. In the interim, APRA has provided a number of extensions to the exemption order, with the current exemption due to expire on 31 December 2016.

This paper details the expected future operation and conditions of the exemption order as well as proposed transition arrangements. APRA seeks comments from interested parties on its proposals relating to transition matters set out in Chapter 2 and the definition of affiliates set out in Chapter 3 of this response paper. Submissions should be forwarded, preferably by email, to

exemptiondp@apra.gov.au by 13 May 2016 and addressed to:

Mr Pat Brennan
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Australian Prudential Regulation Authority
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SYDNEY NSW 2001

Important Disclosure Notice - Publication of Submissions

All information in submissions will be made available to the public on the APRA website unless a respondent expressly requests that all or part of the submission is to remain in confidence. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain in confidence should provide this information marked as confidential in a separate attachment.

Submissions may be the subject of a request for access made under the *Freedom of Information Act 1982* (FOIA). APRA will determine such requests, if any, in accordance with the provisions of the FOIA. Information in the submission about any APRA regulated entity which is not in the public domain and which is identified as confidential will be protected by section 56 of the *Australian Prudential Regulation Authority Act 1998* and therefore will ordinarily be exempt from production under the FOIA.

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Glossary

Term	Definition
ADI	Authorised deposit-taking institution as defined in the <i>Banking Act 1959</i>
APRA	Australian Prudential Regulation Authority
April 2013 discussion paper	<i>Banking Act exemptions and section 66 guidelines</i> , APRA, April 2013
August 2013 response paper	<i>Response to Submissions - Religious charitable development funds</i> , APRA, August 2013
ATM	Automatic Teller Machine
Banking Act	<i>Banking Act 1959</i>
BPAY	BPAY facility offered by BPAY Pty Limited ACN 079 137 518
Corporations Act	<i>Corporations Act 2001</i>
EFTPOS	Electronic Funds Transfer at Point of Sale
Exemption Order	Banking exemption No.2 of 2015
FCS	Financial Claims Scheme
FSI	Financial System Inquiry
RCDF	Religious charitable development fund
Retail investor	A person who would be a retail client under section 761G of the <i>Corporations Act 2001</i>
Retail product	Securities, a financial product or any other arrangement involving the taking of money on deposit offered to a retail investor
RFC	Registered Financial Corporation
Term investment	An investment with a stated term until the investment matures
Wholesale investor	An investor other than a retail investor

Chapter 1 – Introduction

In April 2013, APRA released a discussion paper, *Banking Act exemptions and section 66 guidelines* (April 2013 discussion paper), that set out, amongst other matters, proposals for the future operation of the order that exempts religious charitable development funds (RCDFs) from the need to be authorised as authorised deposit-taking institutions (ADIs) under the *Banking Act 1959* (Banking Act).

The intention of APRA in amending the operation of the order relating to RCDFs was to reduce the likelihood that an investor in an RCDF may confuse such an investment with an ADI deposit. This is consistent with the relevant global principles governing permissible activities of banking institutions - that is, that the taking of deposits be reserved for institutions that are authorised and prudentially supervised as deposit-taking institutions - as well as being aligned with reforms to the fund-raising activities of Registered Financial Corporations (RFCs).

In August 2013, APRA released *Response to Submissions - Religious charitable development funds* (August 2013 response paper) that responded to issues raised in submissions to the April 2013 discussion paper. In that response paper, APRA also set out a number of amendments to its earlier proposals in recognition of issues raised by RCDFs regarding the potential impact of APRA's original proposals on their activities. Central to these changes was the proposal to allow RCDFs to continue to accept funding from retail investors provided all such investments have a minimum stated term or call period of 31 days. That is, an investor would be required to provide 31 days' notice before they could redeem their funds. APRA also provided clarification on matters relating to the definitions of key terms, the restrictions on the use of transaction facilities and the prudential warning that RCDFs are required to include in any advertising and marketing material given to retail investors.

APRA received eight submissions on its August 2013 proposals. Submissions were generally supportive of APRA's revised proposals that would allow RCDFs to continue to accept retail investor funding

subject to conditions. Nevertheless, RCDFs continued to express a preference for being able to offer at-call products to retail investors. Submissions did not, however, raise any new issues or comments that had not been previously made in relation to proposals to restrict product offerings to retail investors.

After consideration of submissions from the August 2013 consultation, APRA considers that its amended proposals set out at that time remain appropriate. Notably, and consistent with the principle governing the boundaries between the prudentially regulated and non-prudentially regulated banking sector, APRA remains of the view that unauthorised entities should not offer at-call deposit products or other transactional banking functionality that is typically associated with the product offerings of ADIs. APRA is of the view that its revised conditions provide an appropriate balance between managing and enforcing the prudential boundary and not unduly impeding the fund-raising undertaken by RCDFs.

Chapter 2 of this paper summarises the new conditions and the proposed transition arrangements that will apply to the Exemption Order from 1 January 2017. This Chapter notes APRA's position on the future operation of the Exemption Order and seeks comments on the transition arrangements and their appropriateness to allow an orderly transition to the new arrangements.

Chapter 3 of this response paper sets out APRA's responses to a number of matters that were raised in submissions to the August 2013 response paper, including a revised definition of affiliates to address concerns raised in submissions by RCDFs on this matter. APRA is also seeking comment on the revised definition of affiliates.

In addition, a copy of the intended wording of the Schedule of conditions to the revised Exemption Order is attached to this response paper.

Subject to submissions received, APRA intends to amend the Exemption Order in accordance with the proposals set out in the August 2013 response

paper, incorporating the relevant clarifications set out in Chapter 3, with effect from 1 January 2017.

Chapter 2 – New conditions and transition arrangements

2.1 New RCDF exemption order

The current Exemption Order will expire on 31 December 2016. APRA proposes to remake the order, with effect from 1 January 2017, and incorporate the conditions as set out in the August 2013 response paper along with relevant clarifications set out in Chapter 3 of this response paper. Notably, APRA will modify the definition of affiliates as noted in item 3.2 of this paper so that an RCDF will still be able to transact with an affiliate that is a retail investor, including staff and clergy.

The new conditions are proposed to take effect from 1 January 2017 for new retail investors, and from 1 January 2018 for existing retail investors of an RCDF at 31 December 2016. These conditions, reproduced below, are consistent with those as set out in the August 2013 response paper.

2.1.1 Retail investments

An account offered to a retail investor without a stated term will be required to have a minimum 31-day notice period prior to any withdrawal. Any account offered to a retail investor with a stated term, that is a term investment, would need to commence with a stated term of at least 31 days. On maturity of a term investment, an RCDF may, where the investor has requested repayment, repay the funds via cash, cheque or direct credit to an account at an ADI. Where the investor has not requested repayment, the funds would be rolled over into a new investment with a minimum term or notice period of 31 days.

Notwithstanding the minimum term and notice period, RCDFs would not be precluded from releasing funds from retail investments in cases of an investor's exceptional circumstances that may lead to hardship. RCDFs will need to develop their own procedures for determining genuine investor hardship.

These conditions do not relate to funding from wholesale investors or affiliates of the RCDF.

2.1.2 Terminology

The use of the terms 'deposit' and 'at-call' and derivatives of these terms will not be permitted. RCDFs will not be able to use such terminology in relation to retail products or in marketing to retail investors.

2.1.3 BPAY and other transactional facilities

RCDFs will be prohibited from offering BPAY payment functionality for products offered to retail investors. However, RCDFs will be able to continue to make or receive payments, including new retail investments, via BPAY. An RCDF will also be able to continue to use BPAY to transact between affiliates of the RCDF.

2.1.4 Prudential warning

RCDFs will continue to be required to provide a prudential warning to retail investors. The existing prudential warning will be expanded to include a statement to the effect that an investment in an RCDF is not covered by the Financial Claims Scheme (FCS). The wording of the prudential warning to be included in the Exemption Order is set out below:

{Insert name of Fund} (the Fund) is not prudentially supervised by the Australian Prudential Regulation Authority. Therefore, an investor in the Fund will not receive the benefit of the financial claims scheme (FCS) or the depositor protection provisions in the *Banking Act 1959*. Investments in the Fund are intended to be a means for investors to support the charitable purposes of the Fund.'

2.2 Transition arrangements

APRA is seeking comments from RCDFs on the proposed transition arrangements, in relation to the new conditions that will be included in the Exemption Order from 1 January 2017.

APRA proposes that RCDFs listed on the Exemption Order at 31 December 2016 will continue to operate under the new Exemption Order with effect from 1 January 2017, and will have up to twelve months to transition to the new conditions under the Exemption Order. That is, existing accounts of retail investors of an RCDF at 31 December 2016 could continue to operate, without change, until 1 January 2018, after which all such accounts would need to comply with the new conditions on the Exemption Order. All retail products offered to retail investors from 1 January 2017 onwards would need to comply with the new conditions on the Exemption Order immediately from that date.

2.3 Future operation of the Exemption Order

In the August 2013 response paper, APRA set out its position on the future operation of the Exemption Order. After consideration of submissions received, APRA considers that its amended proposals set out at that time remain

appropriate. APRA's considerations in this regard are set out in Chapter 3 of this response paper. Taking account of the proposed transition arrangements outlined in this Discussion Paper, APRA proposes that RCDFs listed on the Exemption Order at 31 December 2016 will be allowed to continue to receive an exemption from the need to be authorised by APRA as an ADI should they wish to continue to conduct banking business, provided they meet the new conditions that will take effect from 1 January 2017. There will be no exemption for RCDFs or individual accounts should they not be compliant with the new requirements.

In addition, APRA may review the Exemption Order from time to time should circumstances warrant a review.

Other religious and charitable entities that wish to accept funds from retail investors but do not wish to comply with the new conditions of the Exemption Order or seek authorisation as an ADI will have the options of registering as an RFC or seeking to operate a Managed Investment Scheme.

Chapter 3 – Response to August 2013 submissions

This chapter sets out APRA's response to issues raised in submissions to the August 2013 response paper.

3.1 Retail investments

In the August 2013 response paper, APRA set out revised proposals for retail investor funding such that RCDFs would be able to continue to accept such funding, but not on an at-call basis. APRA proposed to allow RCDFs to accept retail investor funding provided that any such accounts had a minimum 31-day call period or term before an investor could redeem their funds. On maturity of the investment, an RCDF could, where an investor has requested repayment, repay the funds via cash, cheque or direct credit to an account at an ADI. Where the investor has not requested repayment, the funds would have to be rolled into a new investment with a minimum term or call period of 31 days.

Comments received

Whilst acknowledging APRA's revised position on this matter, submissions argued that RCDFs should be able to continue to accept at-call retail investor funding. Submissions expressed concerns about the impact of the restrictions on certain types of RCDF business models, and the potential inability to continue to offer the same level of services if there was any loss of funding as a result of the new limitations.

APRA's response

The potential impact on RCDFs arising from a prohibition on offering or accepting at-call products to retail investors mainly arises through a combination of a potentially reduced level of retail investor funding and the potential for ongoing increased interest expenses. APRA's position has sought to achieve a compromise whereby RCDFs are able to continue to accept funds from retail investors, but with product features that clearly differentiate this activity from transactional banking. APRA maintains the view that this distinction is important given the additional protections associated with ADI deposits compared

to other investments, including investments with RCDFs. It also prevents existing ADIs, who meet the full range of prudential requirements, from having to deal with competitors offering essentially identical products without the need to meet the same prudential requirements.

APRA's view is that an appropriate balance is achieved by allowing RCDFs to accept retail investor funding with a minimum 31-day call such that the works of RCDFs are not unduly impacted, and that the clear differentiation between products offered by RCDFs and transactional banking products offered by ADIs is achieved. As noted in the August 2013 response paper, in cases of customer hardship RCDFs will be able to release funds earlier than 31 days should there be a need.

3.2 Definition of affiliates

In the August 2013 response paper, APRA clarified the definition of *affiliates* as it applies to RCDFs. The definition provided in that paper was:

- (i) a body constituted by or under the authority of a decision of the central governing body of a related religious organisation; or
- (ii) a body in relation to which the central governing body of a related religious organisation is empowered to make ordinances or other binding rules; or
- (iii) a person acting as a trustee of a trust for or for the use, benefits or purposes of a related religious organisation; or
- (iv) an employee of a body mentioned in subparagraphs (i) to (iii) above who receives their stipend or remuneration via an account of the RCDF,

but not including retail investors, lay persons, clergy, staff or other natural persons.

Comments received

Some submissions raised concerns that the definition, as set out, would prevent an RCDF from

operating at-call accounts for affiliates who are not natural persons but are captured by the definition of retail investor. Examples provided included smaller churches and ministry organisations who would be classified as a 'retail investor' under section 761G of the *Corporations Act 2001* (Corporations Act). In addition, subsequent submissions have further questioned the purpose of precluding staff and clergy from being recognised as affiliates.

APRA's response

It is not APRA's intention to exclude RCDFs from offering at-call or BPAY transactional banking functionality to affiliates, including affiliates who are retail investors and could reasonably be expected to have a clear understanding of the nature and operations of the RCDF with whom they have an affiliation. APRA therefore proposes to widen the definition of affiliates to include staff of the RCDF and its affiliates, clergy and other retail investors who are not natural persons as set out below.

An affiliate is:

(i) a body constituted by or under the authority of a decision of the central governing body of a related religious organisation; or

(ii) a body in relation to which the central governing body of a related religious organisation is empowered to make ordinances or other binding rules; or

(iii) a person acting as a trustee of a trust for or for the use, benefits or purposes of a related religious organisation; or

(iv) an employee or voluntary staff member of a body mentioned in subparagraphs (i) to (iii) above; or

(v) a person ordained within a related religious organisation; or

(vi) a person undertaking training or education for the purpose of seeking ordination within a related religious organisation.

3.3 Non-traditional products

APRA has previously proposed that all products offered to retail investors other than affiliates have a minimum 31-day call period or term for the redemption of funds.

Comments received

One submission indicated that some of its products could not be confused with traditional banking products in that an investor could only redeem their funds contingent on the occurrence of a trigger event. An example of such a product is a funeral fund whereby an investor pays money in order to have funds available to cover funeral and other expenses in the event of death. The submission expressed the view that requiring such products to have a 31-day call before a person can redeem their funds is not reasonable.

APRA's response

APRA notes the comments concerning products which for all intent and purposes are not typical banking-like products and are not designed for transactional purposes. It would be difficult to deal with such cases under the Exemption Order on a case-by-case basis. However, as indicated in the August 2013 response paper, RCDFs will not be precluded from releasing funds from retail investments in cases of exceptional circumstances that may lead to hardship. RCDFs will be free to develop their own procedures in this regard as long as such procedures are reasonable and do not allow retail investors to routinely overcome the 31-day minimum term or call period. Considering the case of a funeral fund in this context, the release of funds to cover funeral expenses would, in APRA's view, be reasonable grounds for releasing funds immediately.

Appendix 1 - Revised Schedule of Conditions (DRAFT ONLY)

1. The Fund must be and continue to be:

(a) recognised at law as being formed for religious and charitable purposes stated in a trust deed, ordinance or other foundation document governing the Fund (Fund constitution);

(b) limited to the purposes stated in the Fund constitution; and

(c) operated not-for-profit.

2. The Fund's retail products must have the sole or dominant intention of furthering the religious and charitable purposes of the Fund.

3. A copy of the Fund constitution setting out the Fund's religious and charitable purposes must be available for inspection on request by APRA.

Minimum term or call period for products offered to retail investors

4. Subject to Condition 5, where a Fund offers, issues or sells a retail product to a retail investor on or after 1 January 2017:

(a) the retail product must have a minimum term or call period of 31 days; and

(b) subject to Condition 7, the retail investor must not be able to redeem any funds for 31 days from the date they are invested in the retail product.

Transitional Arrangements

5. A Fund may continue to make available to a retail investor, a retail product that:

(a) was offered, issued or sold to the investor prior to 1 January 2017; and

(b) which does not meet the requirements in Condition 4;

until 1 January 2018.

Rollovers and repayments to retail investors

6. When money held in a retail product that is issued or sold by a Fund to a retail investor reaches its 31 day maturity, the Fund must:

(a) roll over the retail investor's funds for a further period of at least 31 days; or

(b) if the retail investor requests that the funds not be rolled over, repay the retail investor's funds in the form of cash, cheque or direct credit to an account held at an authorised deposit-taking institution (ADI) as defined in the *Banking Act 1959*.

Early release of funds to a retail investor

7. A Fund may, upon written request from a retail investor at any time, pay to the investor some or all of the funds invested in a retail product, provided that the Fund is satisfied that the investor has demonstrated that he or she is subject to exceptional circumstances that may lead to hardship and that it is appropriate to release the funds.

8. A Fund may only release funds under Condition 7 if the release complies with a written procedure prepared by the Fund. The procedure must set out the basis upon which the Fund will determine whether exceptional circumstances that may lead to hardship exist that would warrant the early release of an investor's funds.

9. The Fund must not offer to retail investors:

(a) cheque account facilities; or

(b) BPAY facilities,

in relation to retail products.

10. The Fund must not offer to retail investors or affiliates:

(a) Electronic Funds Transfer at Point Of Sale (EFTPOS) facilities; or

(b) Automatic Teller Machine (ATM) facilities,

in relation to retail products.

11. Condition 9 does not preclude a Fund from making or receiving payments to or from a retail investor using such facilities.

Disclosures

12. The Fund or its controlling entity must in all cases ensure that advertising and marketing material of the Fund contains, at a minimum, the following disclosure:

{Insert name of Fund} (the Fund) is not prudentially supervised by the Australian Prudential Regulation Authority. Therefore, an investor in the Fund will not receive the benefit of the financial claims scheme or the depositor protection provisions in the Banking Act 1959. Investments in the Fund are intended to be a means for investors to support the charitable purposes of the Fund.

13. The Fund or its controlling entity may advertise and market the Fund on-line or in print produced by or under the auspices of the controlling entity (or the religious institution that established the Fund). All advertising and marketing material of the Fund must contain the disclosure required under Condition 12.

Restriction on use of certain words and expressions

14. A Fund must not use or assume the words or expressions deposit or at-call, or any other word or expression (whether or not in English) of like import, in relation to a retail product offered, issued or sold to a retail investor.

15. A reference to a word or expression being used or assumed includes a reference to the word or expression being used or assumed:

- (a) as part of another word or expression; or
- (b) in combination with other words, letters or other symbols.

Definitions

16. In this Schedule:

affiliate means:

- (a) a body constituted by or under the authority of a decision of the central governing body of a related religious organisation; or
- (b) a body in relation to which the central governing body of a related religious organisation is empowered to make ordinances or other binding rules; or
- (c) a person acting as a trustee of a trust for or for the use, benefits or purposes of a related religious organisation; or
- (d) an employee or voluntary staff member of a body mentioned in sub-paragraphs (a) to (c) above; or
- (e) a person ordained within a related religious organisation; or
- (f) a person undertaking training or education for the purpose of seeking ordination within a related religious organisation.

controlling entity means a person or body corporate who or which is a trustee of, or otherwise concerned in the management of, a Fund.

retail investor means a person who would be a retail client under section 761G of the *Corporations Act 2001*, but excludes affiliates.

retail product means securities, a financial product or any other arrangement involving the taking of money on deposit offered to a retail investor.



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