23 May 2013

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

Sent via email: exemptiondp@apra.gov.au

Dear Mr Grummitt

Banking Act Exemption: Religious Charitable Development Funds (RCDFs)

Anglican Funds South Australia ("AFSA") welcomes the opportunity to comment on the Discussion Paper. This letter sets out our submissions on the proposals in the Discussion Paper which relate to the RCDF Exemption Order.

AFSA is an RCDF operating as an activity of the Synod of the Diocese of Adelaide of the Anglican Church of Australia Incorporated ("Synod"), through the Anglican Funds South Australia Ordinance (as amended 2010) passed by an act of Synod. The Synod is a trust established through an Act of the South Australian Parliament.

AFSA funding provided to parishes and other diocesan agencies, including schools, is often the enabler for social enterprises to be established, restructured or to continue to operate. AFSA 'retail' investors support AFSA, and these investments in turn are a means to support these social enterprises.

1 Background

1.1 Anglican Funds South Australia

AFSA was established as a means for parishes and other Anglican affiliated organisations to invest and access stable funding for church and charitable projects, and also to invest their endowment and every-day funds. AFSA is governed by an independent Board of Directors appointed by the Diocesan Council, which is an organ of the Synod.

AFSA's Board and Management are professionals who predominantly originate from the banking, funds management, or mutual sectors.

Though the present-day activities of AFSA have existed since inception, in 2008 it was divided into two distinct activities the first being the Endowment Fund, which administers a market linked investment fund governed in the Yale-style Endowment Model. This fund is closed to all but the Synod, Parishes and Anglican corporations, and the activities of the Endowment Fund are not the subject of this submission.

The second activity is the Community Fund ("the Fund"), which is specifically a Religious Charitable Development Fund (RCDF). The Fund has separate reserves, and has operated profitably since inception, with profits either withheld as reserves or paid out as grants. During the restructure, AFSA voluntarily adopted a (simplified) prudential governance framework, which included capital adequacy guidelines as the appropriate standard for maintaining and increasing reserves each year and this reserve element was encapsulated in AFSA's Board Policies. Reserves are invested in order to further support investors' funds. Today the Fund has grown to have $20.1m in total assets and is backed by reserves in excess of 10% of Risk Weighted Assets. In addition to the Fund's own reserves, the Fund is also guaranteed by the assets of the Synod. At the time of writing, the investments of individuals comprise 9% of our liabilities.

AFSA's core purpose of being a strong and significant supporter of local parishes, including their community activities and buildings, aligns with the investors' desires of supporting their own Anglican community.

Provided that they are an Anglican affiliate, the Fund welcomes all investor types affiliated with the Anglican Church - including individuals, partnerships, businesses, charities/community associations, NFP entities and trusts. AFSA provides fee free accounts, including at-call and term investments. Profits surplus to the capital needs of the Fund are returned to Parishes and Anglican Affiliated Organisations through a Participant Distribution, which is allocated on the basis of the nominations of investors combined with the proportion of the nominators' investment balances as compared to all other nominators.

AFSA offers secure online transaction functionality including BPAY, Cemtex (bulk clearing files) and third party payment functionality. The system provider is Data Action, which has many clients in the Credit Union sector. AFSA also participates in the Bulk Electronic Clearing System (BECS), through Indue, with AFSA's BSB being [redacted] online use).

In the past year, AFSA's Community Fund, with the assistance of parishioner investors, made an economic contribution to the church community, and to other Anglican Affiliated charitable organisations, such as Anglicare-SA of over $1.3m in interest paid, discounts on loan rates compared to commercial lending rates at the time, and Participant Distributions.

1.2 The important role of RCDFs

As a result of the specialised nature and requirements of Church financing, Religious Charitable Development Funds have been long established in Australian Churches. Features of these RCDFs include:

1. Funding sources regularly involving not only monies from lay parishioners but also funding from commercial sources
2. Specialised lending on terms not usually available through commercial sources
3. Personalised customer (individual or parish) relationships
4. Coverage of 'pockets of market failure' in the ADI market due to development, social nature (breakeven/Charity/NFP), small regional community or reputational concerns.

RCDFs are, as described, focused on charitable social development work. Many of these works and programmes are delivered in conjunction with government, and the funding we contribute relieves the government from financial burden.

2 Submissions on proposed changes to the RCDF Exemption Order

2.1 Conflation of RFCs with RCDFs

APRA appears to conflate RFCs with RCDFs in their discussion paper. The paper specifically mentions failure in the RFC market, and we submit that to date, and to our current knowledge, no RCDF has failed to make good on its liabilities to investors over the decades that they have been allowed to operate under the banking exemption, including during the many recessions and market failures which have occurred over that time.

The vehicles are different in many ways:

RFC	RCDF
Participate in an open market.	Are restricted to investors affiliated with the religious order, and currently to individuals connected to the same.
Have a goal of profit for the benefit of shareholders.	Have a goal of producing long-term financial outcomes that generate funds to provide for religious and charitable works.
Investor primary motive is return on investment.	Investor primary motive is promoting the religious and charitable works of the diocese, and their local church community.
Funds invested for return.	Funds invested ethically.
Sales made through financial advisers.	Investors attracted through their affiliation with the Church.

We 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 that 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."

AFSA is not a major global institution, and we would like to highlight that any benefits that accrue to the Anglican Diocese of Adelaide from the placement of funds by retail investors with AFSA, are to support our mission activities in community services, social welfare, aged care, and education.

AFSA is concerned that the losses suffered by imprudent, and poorly advised investors of a failed RFC, a structure patently different to an RCDF, are being conflated as also being a problem with RCDFs, which history suggests is an incorrect proposition. We submit that due to the closed nature of our addressable market, stability and prudent management of our investors' funds is paramount, as a failure to do so would cause irreparable reputational damage to our Church.

2.2 Prohibition on the use of the word "Deposit"

AFSA already operates under the understanding that the word "deposit" is a prohibited descriptor of the investments of an RCDF. AFSA supports that using the word "investment" underscores that the investor is not making a deposit with an ADI, and as such does not enjoy the support of the government deposit guarantee. In AFSA's view, this is consistent with the disclaimer that RCDFs are required to give investors.

2.3 Demarking ADIs and RCDFs

AFSA accepts APRAs position that if an investor believes that they have made a deposit with an ADI, it would be reasonable that they would expect the level of protection afforded under the Banking Act. AFSA also agrees that investors in RCDFs should not be under the impression that they are dealing with an ADI.

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.

AFSA submits that if APRA maintains that these arrangements are insufficient, then the path forward could be to require under the Banking Exemption Act that the RCDF be subject to added conditions, such as maintaining 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 is has obtained that confirmation, and maintains those records.

In any instance, AFSA submits that a general prohibition on taking retail investments, rather than a considered exploration of other possible alternatives, is not in the best interests of our Church, our charitable organisations, our parishes, and would not reflect the interests and wishes of our parishioner stakeholders.

2.4 Call to clarify "At Call" prohibition

AFSA would like to clarify that APRA's intention was not to prohibit "at-call" funds for non-personal investors, ie in the circumstances where AFSA was operating in the capacity of an internal treasury.

Despite our call for clarification on this matter, AFSA submits that, as with all financial institutions, the ability to access "at-call" investments is an important factor in reducing overall cost of funds. This enhances surpluses available for use in our religious and charitable works.

The proposal that RCDFs could only offer investments on a minimum 31-day term, would severely impact AFSA's ability to attract deposits, including from non-personal investors.

We submit that if the concern of APRA is one of form of language, then APRA considers alternative terms for use by RCDFs.

2.5 Restrictions on transaction settlement schemes such as BPAY

The purpose of restricting BPAY for RCDFs is unclear. For corporate treasury entities this functionality continues to be of value and is provided through an ADI, not directly by the RCDF. There has been considerable investment by RCDFs in becoming PIM's. Having access to BPAY is consistent with the Australian Payments Clearing Association (APCA) approach in reducing cheque fraud, and the need for and number of cheques.

The implications of removing the availability of these settlement methods reach beyond parishioner investors, they would impact upon the ability of AFSA to service parishes and affiliated organisations with internal treasury operations. Settlement funds currently held in low-interest bearing accounts could be lost resulting in at best a higher cost of funds, and at worst loss of business opportunity, as affiliates may choose not to deal with AFSA altogether. AFSA believes this outcome is not the intention of APRA, and seeks clarification of this matter.

2.6 Prohibition on taking investments from individuals

AFSA already operates in a market restricted to those who are affiliated with the Anglican Church. In relation to individual investors, those would typically be parishioners of our churches. We submit that APRA's approach of prohibiting all investments from individuals misses the crucial point that parishioners are highly involved stakeholders.

Since time immemorial, the church has been built by the efforts of parishioners, whether they volunteer skills and energy, or contribute resources such as money or donated goods and services. Churches would not be built without the contribution of parishioners, nor would those assets be extended beyond the parish to the conduct of the charitable works of the wider diocese and its entities. Parishioners control their churches through parish councils and vestry meetings in which they are afforded official positions in the hierarchy of their local church management through election by their peers in the parish.

Lay representatives from each parish are nominated to vote at our Synod (the AGM of the diocese) which provides the right of the laity to vote, creating a significant voice exercising control of the diocese. Laity are also elected to represent the Synod on Diocesan Council which is the board of management of the diocese.

Parishioners have been baptised in the church, been confirmed, and taken their first communion. Steps along a path of engagement, recorded in official registers at the Church Office, and given to parishioners on official certificates. The specific affiliation of each individual investor is recorded at time of investment, as they need to nominate the affiliated organisation they wish to receive the Fund's Participant Distribution.

Anglican parishes are directly funded by their congregations. Parishioners not only paid to build the church buildings, they directly pay the stipend of their clergy, and pay the operational expenses of their parish.

We submit that it is not possible to reasonably argue that parishioners are disinterested bystanders, instead their passion and commitment to their faith and to their parish community is expressed through direct involvement, through giving to their church collection, the making of bequests, and also through their investments with AFSA on the understanding that by investing they are directly benefiting their Anglican community, and providing another means by which it can fulfil its mission.

We submit that the same could be said of parents who choose to send their children to Anglican Schools, many of whom are also parishioners at their local Anglican church.

AFSA submits that instead of prohibiting investments from individuals, APRA considers strengthening the definition of affiliate to also include those individuals who are directly connected as parishioners of the Church or parents and children attending our schools.

3 Reform Impacts

3.1 Losses to the community will mean the government will shoulder more burden

AFSA sees no benefit to the community from the current APRA approach. AFSA considers that the impact on the 'not for profit sector' would be more than minor and that a full Regulatory Impact Statement (RIS) should be completed.

The obvious impact is the loss of $1.1 Billion in estimated retail investments (refer to discussion paper page 11). These funds are often the catalyst that provides the ability for RCDFs to raise funds from the commercial ADI market or other sources (including internal parish accounts) estimated by APRA at a further $6.3B.

In total this $7.4B is spread over at least 42 and up to 50 separate entities across Australia. These monies are lent to support various internal entities and programs. They are often the source of funds that enable these entities to continue operating, redevelop to become a commercial proposition, or restructure, rather than close. As a result the $7.4B is only the obvious amount, the impact and total involved is many multiples thereof. By way of example a diocesan entity may use this finance to attract a commercial lender to a community project, to attract a government grant that has a co-contribution funding requirement, or to maintain quick start up capacities during quiet periods.

The community projects themselves have considerable value beyond the multiple of $7.4B described above. These include real assets (improved building market value and community utility), real services (including education) and the ‘outcomes’ sought after by government grant programs (eg at home care of the elderly etc).

By removing the retail (lay parishioner) investments, a thread from the fabric of society is being pulled. In many cases, particularly in regional and under privileged communities, that fabric has already worn very thin with the Churches being the last institutions available. RCDFs often continue or step in to operate where there are pockets of market failure, where ADIs have long since left communities and commercial financing is not available.

The direct annual cost impact on RCDFs could be estimated by comparing the retail (lay parishioner) cost of funds to long term commercial market funding costs. The difficulty with this approach is that it varies over the interest rate cycle and as there is currently unusually high competition for deposits, the margin is narrower than would otherwise be the case.

The direct costs are however irrelevant if the quantum is likely to force RCDFs to change their operations across the economic cycle.

3.2 Deterioration of the risk profile of RCDFs

The proposed changes to the funding structure of RCDFs could mean that those with a higher reliance on parishioner investors will move from a funding structure comprised of many smaller investors to one of larger institutional investors and/or lines of bank funding. This may have the effect of concentrating risk in the liquidity structure of RCDFs. AFSA submit that this would work against the objects of APRA.

4 Next Steps

We trust that our submission has been helpful to APRA. AFSA requests that APRA contact us to discuss our submission further. You may do this by contacting our Jamie Anderson who is the manager of the Community Fund, at either [redacted] or by telephone [redacted].

Yours sincerely

Allan Perryman
Chairman of the Board
Anglican Funds South Australia