

21 May 2013

Australian Prudential Regulation Authority
Policy, Research and Statistics
GPO BOX 9836
Sydney NSW 2001

Attn: Mr Neil Grummitt, General Manager, Policy Development

Via email: exemptiondp@apra.gov.au

Dear Sir

RE: BANKING ACT EXEMPTIONS AND SECTION 66 GUIDELINES DISCUSSION PAPER

We would like to offer comments for your consideration in relation to the proposals set out in the abovementioned Discussion Paper.

Introduction

It appears from the Discussion Paper, that your proposals have arisen out of failures which have occurred in the 'non-prudentially regulated financial sector'. The collapse of Banksia Securities Limited, a Registered Financial Corporation (RFC), has been noted in particular. Accordingly, it is both logical and appropriate that prudential measures be considered for such organisations.

However, Religious Charitable Development Funds (RCDFs) have been operating in Australia for many decades, through numerous periods of financial turmoil including the most recent prolonged financial crisis, and yet there has not been a single failure in this sector. There are currently 61 RCDFs according to the Australian Prudential Regulation Authority (APRA) website, and these organisations operate vastly differently from RFCs, in all key respects, notably in terms of structure, philosophy and customer base.

Accordingly, we do not believe similar measures are required in respect of RCDFs given (a) the lack of a single instance of failure should, on the face of it, indicate that the current framework and exemptions are suitable and operating effectively; and (b) RCDFs and RFCs are such different styles of organisations, that imposition of the same or similar measures for both, are inherently unlikely to achieve the same outcomes for both.

The original exemption for RCDFs arose out of the 1997 Wallis Report recommendations, and there has been no adverse occurrence in the years since which would suggest that such approach requires change.

The products offered by RCDFs have enjoyed far greater capital protection benefits than RFCs in reality, due to the structure of RCDFs and the unique and conservative nature of these organisations. As opposed to RFCs, and any other financial services organisation, RCDFs provide a highly unique and specialised offering to their clients. Investors utilise or invest in the products offered by RCDFs because they wish to contribute to, and participate in, the relevant church community.

Unlike with RFC investments/investors, a decision to invest with an RCDF is not solely based on normal investment criteria such as yield and marketing to the non-financially aware, or profit-making, risk profile and asset allocation considerations.

Church affiliated investors clearly understand that RCDFs are neither banks nor Approved Deposit-Taking Institutions (ADIs), and that the money they invest with an RCDF does not have capital protection and may not provide profit or income to them. This is partly due to the fact that the current mandatory disclosures are actually clear and prominent, and hence effective. Church affiliated investors do not disregard risk or a proper evaluation of their investment with RCDFs, however the primary purpose motivating their investment is to contribute resources as a reflection of their personal faith and commitment to the church community. This often results in the establishment of additional services to meet needs in the wider demographic community, such as Aged Care services, Schools, Child Care Services, Marriage & Family Counselling.

Accordingly, we do not consider there is any evidence to suggest that RCDFs have failed or are likely to fail, and hence no indication that the current exemption is failing to protect church affiliated investors and achieve prudential oversight objectives. The old adage 'if it ain't broke, don't fix it' strongly applies to RCDFs in this instance.

The approach proposed by APRA in combining prudential measures for RCDFs and RFCs does not recognise a fundamental difference between these structures. By treating such very different organisations in the same way, the practical outcomes for RCDFs will be ill-fitted and ultimately disadvantageous for church affiliated investors, and will have major adverse social and economic consequences for RCDFs and the Church sector.

The Proposals

We do not understand why RCDFs who offer products via debentures are distinguished from those who provide essentially the same products, through managed investment schemes. We note that both offerings currently enjoy the same registration and disclosure exemptions from the Australian Securities & Investments Commission (ASIC) via Regulatory Guide 87 and Class Order 02/184, and will be treated similarly in the course of implementing the proposed recommendations published by ASIC in Consultation Paper 207 released this month. ASIC are adopting a separate review and proposal process in relation to charitable entities than they have adopted towards debenture issuers or operators of managed investment schemes, and the distinction is important.

1. The rationale employed by APRA seems to suggest that that it is not appropriate to continue to exempt RCDFs from the need to be authorised under the Banking Act where products are offered to retail clients, because an RFC investor may have considered their investments with RFCs to have equivalent protections to those of an ADI deposit. Given the significant differences between RCDFs and RFCs and their respective investors, we do not accept that there is any nexus between the RCDF exemption and RFC investor complaints.
2. APRA appears to have developed these proposals in response to RFC failures, such as Banksia, but is nevertheless seeking to apply such failures to the RCDF sector which has historically managed funds much more conservatively and responsibly, as demonstrated by the lack of a single failure in this sector in the 90 or so years they have been operating.
3. There is no clarity at this stage around what a "retail-type product" is exactly. Typically in the financial services/Corporations Act world, it is the investors, not the products, which are classified as retail, and accordingly for consistency, this should remain the approach in all terminology.

4. APRA proposes that, unless registered as an RFC, an ADI or a registered scheme operator, RCDFs will no longer be able to accept funds from retail investors. Firstly, we note that many of the funds invested in RCDFs are then loaned to church entities and affiliates for the purposes of charitable enterprises, such as schools and community programmes. The loan book extends out to 15-20 years in some cases, and accordingly a curbing or restricting of investment funds will seriously and immediately impact the liquidity of RCDFs, the charitable works of the RCDFs, and by extension, the very clients APRA is seeking to protect.
5. APRA's proposed restructuring of the investment funds of RCDFs will result in the necessary rapid depletion of current liquidity reserves from the withdrawal of funds by affected clients, possibly beyond the minimum levels of liquidity which RCDFs are regulated to maintain. Any affected clients may be key leaders within the Church, and this could have a possible flow-on effect that may also result in the withdrawal of some of our Church funds as well. This indicates that proposals which address the problems identified with RFCs, will actually seriously harm RCDFs and their Church affiliated investors, despite the lack of problems and concerns raised in relation to the latter.
6. The restriction on accepting funds from 'retail investors' adds a further complication for RCDFs, due to the unique nature of their investors, and the difficulty in categorising them as retail or wholesale in relation to the traditional Corporations Act definitions. The more logical and successful approach would be for APRA to develop the current exemption to clearly designate the range of Church affiliated clients to whom RCDF can provide products and services ie essentially to enable the provision of products and services to any person/body/entity who utilises such products or services to support the charitable works of the RCDF. This approach would enable recognition of the unique reality for RCDFs in that investors participate in their Church community both as investors and also as participants in the lending services offered to Churches, whereby they often underwrite loan repayments. This is one of many fundamental and significant differences between RCDFs and RFCs.
7. APRA proposes to restrict the use of the word deposit and its derivatives. We believe there is no evidence to suggest that any RCDF investors are confused about the nature of the deposit products offered by RCDFs. The mandatory disclosures are clear and prominent, and we are not aware of any complaints or confusion expressed by clients in relation to the distinction between an ADI bank deposit, and an RCDF account. Such accounts are offered predominantly to two types of RCDF 'client' – the first is to what are often retail investors ie individuals who wish to support the church community and the RCDF in its charitable works; and the second is to individuals and entities who are affiliates of the church in some capacity and utilise the products to operate their church bodies or charitable works on a day-to-day basis. Regardless of categorisation under the Corporations Act, none of the persons/entities investing with RCDFs can be equated with traditional retail investors, because the unique nature of RCDFs means that Church affiliated investors do NOT solely invest for the purposes of personal gain. Nevertheless whilst we do not consider the restriction on using the word 'deposit' to be beneficial to investors in any way, nor necessary to further protections, we have no objection in revising the terminology used accordingly, and have already taken steps some years ago in this respect.
8. APRA proposes to restrict the use of BPAY facilities, although no explanation or evidence has been provided as to what problem has been identified and hence must be rectified by APRA in proposing this restriction. As noted above, a key client base of RCDFs are the church affiliates who operate churches, schools and other community works. An important service offering of RCDFs is the provision of treasury-style support in the shape of transactional accounts which allow day-to-day operation, and BPAY facilities in conjunction therewith.

To restrict RCDFs from providing such services would require such affiliates to source such services elsewhere at far greater expense, and generally impact the benefits that RCDFs were created to provide to their community. In 2006, the BPAY Management Committee invited and accepted RCDFs to become BPAY members where sponsored by an ADI.

This approach has been operating successfully since, with appropriate oversight provided by the sponsoring ADI. Given APCA's conclusion that cheque usage is in steady decline, with the reasonable expectation of obsolescence in due course, removal of RCDFs' ability to offer our affiliates BPAY services to facilitate their operations will have serious repercussions.

We do not accept that APRA's proposals offer a workable solution to RCDFs. APRA proposes that in order to continue offering products to retail investors, RCDFs must become one of three things – (i) an ADI - APRA has previously indicated it is not prepared to authorise an RCDF as an ADI, and in any case, this is not feasible for most RCDFs due to the ownership and other prudential requirements (ii) an RFC - the RFC model is totally unsuitable for any Church based treasury function as we will incur significant restrictions on the provision of at-call type products, which will severely and inappropriately impact the treasury-style services RCDFs currently provide to church affiliated persons in the operation of their churches, schools and community programs. This will further cause liquidity problems for such affiliates in their day-to-day operations which necessitate access to at-call funds (iii) a scheme operator - becoming a scheme operator will actually bring significantly less protection to investors, as combining all investments into a fund structure will ensure that any losses during times like the GFC are crystallised and passed onto investors. With the current debenture structure, church resources and capital can be, and have been, used to protect investors from losses, to their significant benefit. The systematic failure and/or closure of mortgage funds for this very reason, is compelling evidence of our concerns.

Our alternate proposals

1. That RCDFs be separated completely from the current APRA proposals in relation to RFCs given their unique purpose and successful history;
2. That all RCDFs be brought within the ASIC financial services licensing regime, given the successful oversight of such licensed RCDFs by ASIC to date, and the proposed continuity of such oversight as per Option 2 of the proposals under ASIC Consultation Paper 207;
3. That acknowledgment of the specific and intrinsic purpose of RCDFs and their investors/affiliates in relation to the continuing need for at-call money availability and BPAY facilities be considered by APRA in contemplation of any prudential oversight changes proposed going forward;
4. That the proposal to apply the Corporations Act definition of retail client be set aside in favour of a clarification of the definition of church affiliate within a retained exemption (please refer to the Attachment hereto for our suggested wording), in recognition of the special purpose and operation of RCDFs; and
5. Compliance with risk-weighted capital and liquidity requirements, in line with ASIC Consultation Paper 207, as a condition to continued operation by RCDFs under the current exemption.

As always, RCDFs are extremely willing to engage in full and frank discussions with APRA and ASIC in relation to any problems identified within our unique sector, to ensure the best outcome for our church community and all of its affiliates. We trust that APRA will find this submission informative and helpful in ensuring that regulation of RCDFs is carefully and constructively facilitated, for the sake of our investors.

Yours sincerely



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Attachment – Banking exemption No.1 of 2011 – Schedule 2

Current wording:

4. *The Fund or its controlling entity must not offer via the Fund:*
- (a) *cheque account facilities unless the account holder 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, benefit 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 Fund; or*
- (b) *Electronic Funds Transfer at Point Of Sale (EFTPOS) facilities; or*
- (c) *Automatic Teller Machine (ATM) facilities.*

Proposed wording (with changes marked in yellow):

4. *The Fund or its controlling entity must not offer via the Fund:*
- (a) *cheque account, BPay or other investment facilities unless the account holder is:*
- (i) *a body recognised by or constituted by or under the authority of a decision of the central governing body of a related religious organisation including an entity which is affiliated or operated under the effective control (whether direct or indirect) of that constituted body; 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) *an entity that is exempt from income tax under Subdivision 50-A or 50-B of the Income Tax Assessment Act 1997 and is also a Charity registered with the Australian Charities and Not-for-profits Commission established as a Church or to advance the Christian faith; or*
 - (iv) *an individual who is an adherent of a body recognised by or constituted by or under the authority of a decision of the central governing body of a related religious organisation; or*
 - (v) *a person acting as a trustee of a trust for or for the use, benefit or purposes of a related religious organisation; or*
 - (vi) *an employee of a body mentioned in subparagraphs (i) to (iii) above who receives their stipend or remuneration via an account of the Fund.*
- (b) *Electronic Funds Transfer at Point Of Sale (EFTPOS) facilities; or*
- (c) *Automatic Teller Machine (ATM) facilities.*