



2 April 2019

TO: ALL AUTHORISED DEPOSIT TAKING INSTITUTIONS, LIFE INSURANCE COMPANIES AND GENERAL INSURERS

PROPOSED *FINANCIAL SECTOR (SHAREHOLDINGS) RULES 2019*

The *Treasury Laws Amendment (Financial Sector Regulation) Act 2018* (the amending Act) amends the *Financial Sector (Shareholdings) Act 1998* (FSSA) from 1 April 2019 to introduce a streamlined approval path for applications to hold a stake of more than 20 per cent in a new or recently established domestically-incorporated financial sector company with assets below the relevant threshold¹.

Under the streamlined approval path, applicants will not be assessed against the current national interest framework. Instead, FSSA approval will be granted if the applicants are 'fit and proper'. Approvals granted under the streamlined path will require the holder of the approval to provide relevant information to APRA annually.

Who is eligible for the streamlined approval path?

The eligibility criteria for the streamlined approval path are set out in section 14A of the FSSA. In brief, the streamlined approval path is available for applications to hold a stake in a company:

- (1) that has:
 - (a) applied to be licensed by APRA as an authorised deposit-taking institution (ADI), general insurer or life company, but whose application has not yet been decided; or
 - (b) been licensed by APRA as an ADI, general insurer or life company for less than five years; and
- (2) whose total resident assets are less than:
 - (a) \$200 million, for an ADI or life company; or
 - (b) \$50 million, for a general insurer.

Applications to hold a stake in a holding company of a company to which the above applies may also be made under the streamlined approval path.

Paragraph 45A(1)(a) of the FSSA as amended provides APRA with the power to make rules by legislative instrument prescribing matters required or permitted by the FSSA. APRA has today released for consultation a draft of the *Financial Sector (Shareholdings) Rules 2019* (FSSA Rules) prescribing:

- matters that must be considered in determining whether a person is fit and proper for the purposes of the FSSA (subsection 14A(2) of the FSSA);

¹ Where 'financial sector company' means:

- (a) an authorised deposit-taking institution as defined in the *Banking Act 1959*; or
- (b) a company authorised under the *Insurance Act 1973* to carry on insurance business; or
- (c) a company registered under section 21 of the *Life Insurance Act 1995*; or
- (d) a holding company of a company covered by paragraph (a),(b) or (c).

- the meaning of ‘total resident assets’ used to determine whether a financial sector company’s assets are less than the relevant assets threshold (subsection 14A(5) of the FSSA); and
- the information to be provided to APRA annually, as a condition of approval (paragraph 16A(5)(b) of the FSSA).

A detailed explanation of the draft FSSA Rules is provided in Attachment A.

Consultation period

The draft FSSA Rules will be subject to an eight-week public consultation and are available on the APRA website at: <https://www.apra.gov.au/financial-sector-shareholdings-rules-2019>

Written submissions on the proposed FSSA Rules should be sent to licensing@apra.gov.au by 27 May 2019 and addressed to:

General Manager, Licensing
Policy and Advice Division
Australian Prudential Regulation Authority

Request for cost-benefit analysis information

APRA requests that all interested stakeholders use this consultation opportunity to provide information on the compliance impact of the proposed changes and any other substantive costs associated with the changes. Compliance costs are defined as direct costs to businesses of performing activities associated with complying with government regulation. Specifically, information is sought on any increases or decreases to the compliance costs incurred by businesses as a result of the proposed FSSA Rules.

Consistent with the Government’s approach, APRA will use the methodology behind the Regulatory Burden Measurement Tool to assess compliance costs. This tool is designed to capture the relevant costs in a structured way, including a separate assessment of upfront costs and ongoing costs. It is available at: <https://rbm.obpr.gov.au/home.aspx>.

Respondents are requested to use this methodology to estimate costs to ensure that the data supplied to APRA can be aggregated and used in an industry-wide assessment. When submitting their cost assessment to APRA, respondents are asked to include any assumptions made and, where relevant, any limitations inherent in their assessment. Feedback should address the additional costs incurred as a result of complying with APRA’s requirements, not activities that institutions would undertake regardless of regulatory requirements in their ordinary course of business.

Yours sincerely,

Pat Brennan
Executive General Manager
Policy and Advice Division

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 that is not in the public domain and that is identified as confidential will be protected by section 56 of the *Australian Prudential Regulation Authority Act 1998* and will therefore be exempt from production under the FOIA.

ATTACHMENT A

EXPLANATORY MATERIAL

Financial Sector (Shareholdings) Rules 2019 - Draft

Introduction

The introduction sets out the legislative basis for making the Rules.

Interpretation

This section sets out the definitions used in the Rules. Terms such as 'financial sector company' which are used in the instrument are defined in section 3 of the FSSA.

A brief explanation and summary of the new terms and definitions included in the instrument are set out below.

holder of an approval means a person who has been granted approval under paragraph 14(1)(b) of the FSSA to hold a stake of more than 20 per cent in a financial sector company.

relevant licensed company has the meaning given by section 3 of the FSSA.

Note: Section 3 of the FSSA provides that *relevant licensed company*, in relation to an approval under paragraph 14(1)(b), means the company to which subsection 14A(3) or (4) applied in granting the approval.

Matters that must be considered in determining whether a person is fit and proper

This section sets out the matters that must be considered in determining if an applicant is fit and proper. In drafting this section, APRA has looked internationally to other regulators that currently utilise a fit and proper test for shareholders, as well as its *Prudential Standard CPS 520 Fit and Proper*. APRA has proposed high level considerations for the fit and proper test which can be considered by the decision maker in a manner and to an extent that suits the circumstances.

A brief explanation of the matters to be considered are set out below.

Honesty, integrity and reputation

Financial sector companies occupy a unique position of trust within the community. It is important both in the interests of individual depositors or policy holders, as well as the stability of the financial sector more generally, that these types of companies only be associated with persons who are of good repute.

Competence and capability

It is important that those who have influence and control over financial sector companies have the necessary skills, knowledge, expertise, diligence and soundness of judgement to undertake and fulfil the responsibilities involved.

The relevance of a shareholder's competence and capability is proportionate to their level of influence and control over the financial sector company i.e. a person may be considered

competent and capable to hold a minority stake but not a majority stake in a financial sector company.

Financial Soundness

It is essential that those in a position of influence and control over the affairs of a financial sector company be financially sound, and that there are no financial reasons which could influence improper conduct in regards to the financial sector company.

Substantial shareholders should have the capacity to finance their proposed stake in the financial sector company and the means to maintain, for the foreseeable future, a sound financial position in respect of themselves, and the financial sector company.

Conflicts of Interest

It is fundamental that persons who have influence over, or can direct, a financial sector company do not have conflicts of interest which could improperly influence their conduct in regards to the affairs of the financial sector company.

Suspicion of Financial Crime

The consideration of suspicions of financial crime complements the integrity assessment. It is essential that financial sector companies given their position of trust in the community are not used as vehicles for money laundering, financing of terrorism or other financial crimes.

APRA's ability to supervise

The applicant must not adversely affect the financial sector company's ongoing compliance with prudential requirements. The financial sector company must be able to comply after the approval, with all prudential requirements, including capital requirements, liquidity requirements and large exposures limits, as well as with requirements related to governance arrangements, internal control, risk management and compliance.

APRA should not be prevented from:

- effectively exchanging information with other regulators; or
- fulfilling its monitoring duties by the laws, regulations or administrative provisions of another country governing a natural or legal person with close links to the financial sector company or by difficulties in the enforcement of those laws, regulations or administrative provisions.

Persons who direct the company

For an applicant that is a company, its directors, chief executive officer, or equivalent persons effectively direct the exercise of its voting power over the financial sector company or an intermediate company. It is therefore important that these individuals are also fit and proper.

Influence of other persons

As part of the assessment of the fitness and propriety of an applicant, it is necessary to look through the arrangement and consider if there is any potential for another person to direct or influence the applicant in the exercise of their voting power, such as a business partner or a

family member. In such cases, it is imperative that that person also be fit and proper to hold a stake of more than 20 per cent in the financial sector company.

These rules do not prevent the decision maker from considering other matters that may be relevant to the applicant's fitness and propriety. These could include whether the applicant has a good standing in the relevant industry sector or if the applicant is a 'politically exposed person' under anti money laundering and counter terrorism financing laws.

How will the matters determining an applicant's fitness and propriety be considered?

Applicants must satisfy the decision maker that they are a fit and proper person. APRA therefore expects the onus will be on the applicant to provide sufficient evidence to the decision maker that they are fit and proper rather than for the decision maker to show otherwise.

Honesty, integrity and reputation

APRA expects that the decision maker will take particular account of the following factors (whether in Australia or overseas) which may call into question the honesty, integrity and reputation of the applicant:

- any conviction or prosecution of a criminal offence, in particular offenses relating to laws governing financial services, fraud, financial crime, tax offenses and under legislation relating to companies, bankruptcy, insolvency or consumer protection;
- any demonstration of a lack of willingness to comply with legal obligations, regulatory requirements or professional standards, or having been obstructive, misleading or untruthful in dealing with regulatory bodies or a court;
- any perpetration of or participation in negligent, deceitful, or otherwise discreditable business or professional practices;
- any relevant enforcement actions by any other regulatory or professional bodies for non-compliance with any relevant provisions;
- whether the applicant has dealt with the decision maker in an open and co-operative way and has disclosed to the decision maker appropriately anything relating to their fitness and propriety and acquisition of the financial sector company of which the decision maker would reasonably expect notice; and
- any other information from credible sources that is relevant.

APRA expects an applicant's honesty, integrity and reputation may be demonstrated by provision of police checks, personal and professional references, independent due diligence reports, personal attestations, ASIC reports etc.

Competence and capability

APRA expects that the decision maker will consider the competence of the applicant with respect to the level of influence and control they will have over the affairs of the financial sector company and will take into account:

- previous experience in acquiring and managing holdings in companies;
- previous experience in the area of the financial activities carried out by the financial sector company;
- previous demonstration of due skill, care, diligence and compliance with relevant standards; and
- any substantial involvement in the management of a business or company which has failed, where that failure has been occasioned in part by deficiencies in that management.

APRA expects competence and capability may be demonstrated by provision of curriculum vitae, qualifications, professional references, ASIC searches, business plan etc.

Financial Soundness

APRA expects that the decision maker will take particular account of the following factors, which may call into question the financial soundness of the applicant:

- they are or have been unable to fulfil financial obligations;
- they have entered into a scheme of arrangements with creditors;
- they are subject to a judgement debt;
- they have been declared bankrupt;
- they have seriously or persistently failed to manage personal debts or financial affairs satisfactorily in circumstances where such failure caused loss to others; or
- in the case of a company, it is in the course of being wound-up, or has had a statutory manager appointed.

APRA expects this may be demonstrated by provision of credit check reports, financial reports etc.

APRA expects applicants to demonstrate their capacity to finance the proposed acquisition and maintain, for the foreseeable future, a sound financial position in respect of the financial sector company. APRA expects this may be demonstrated by provision of audited financial reports, bank statements, auditors' certificates and/or capital raising and divestment plans.

Control and influence

APRA expects the decision maker will consider the influence and control the applicant may exercise on the financial sector company in regards to (i) the intensity of their assessment, and (ii) the content of the required information, which should be proportionate to the nature of the applicant (individual or company) and of the proposed stake.

Conflicts of Interest

APRA expects an application may be refused if the decision maker has reasonable grounds to suspect a conflict of interest could improperly influence the conduct of the applicant in regards to the affairs of the financial sector company. APRA expects applicants with a conflict of interest to declare

the conflict to the decision maker and provide grounds as to how the conflict will be managed such that it does not improperly influence the conduct of the applicant.

Suspicion of Financial Crime

APRA expects the decision maker will assess information regarding the source of funds that will be/were used for the acquisition, including both the activity that generated the funds, as well as the means through which they have been transferred, to assess whether this may give rise to an increased risk of money laundering or terrorist financing.

APRA also expects the decision maker will consider the information about the applicant gathered during the assessment process, as well as other information sources such as open media searches.

APRA expects the decision maker will refuse the application if they have reasonable grounds to suspect financial crime including money laundering or terrorist financing by the applicant.

APRA's ability to supervise

APRA expects the decision maker will assess:

- the ability of the financial sector company to comply at the time of the application, and to continue to comply after approval, with all prudential requirements; and
- the applicant's intention towards the financial sector company.

APRA expects this could be demonstrated by appropriate commitments by the applicant to meet prudential requirements. These commitments could include, for example, financial support in case of liquidity or solvency problems.

If the financial sector company will be part of a group, APRA expects the decision maker to assess whether there are any impediments to APRA's ability to supervise. This assessment could include the complexity of the group structure, location of group entities, relationships with other regulators, and whether the group has clear and transparent corporate governance arrangements.

Meaning of total resident assets

This section explains how the total resident assets of a financial sector company is defined. The Explanatory Memorandum to the *Treasury Laws Amendment (Financial Sector Regulation) Bill 2018* set the expectation that APRA would define total resident assets with relation to existing methodology. APRA has therefore defined total resident assets in reference to the methodology for calculating 'total assets' under relevant reporting standards made under section 13 of the *Financial Sector (Collection of Data) Act 2001*.

- For authorised deposit taking institutions (ADI) that are banks, 'total assets' are calculated in accordance with Reporting Standard *ARS 320.0 Statement of Financial Position (Domestic Books)*.
- For ADIs that are credit unions or building societies, 'total assets' calculated in accordance with Reporting Standard *ARS 323.0 Statement of Financial Position (Licensed ADI)*.

- For General Insurers, 'total assets' are calculated in accordance with Reporting Standard *GRS 300.0 Statement of Financial Position*.
- For Life companies, 'total assets' are calculated in accordance with Reporting Standard *LRS 300.0 Statement of Financial Position*.

Although purchased payment facility providers (PPF) do not report under ARS 323.0, APRA proposes to use the methodology in this reporting standard to determine their total resident assets in the same way as this methodology is used by APRA in determining a PPF's total assets for its annual levy amount.

APRA expects the calculation of the financial sector companies 'total resident assets', in accordance with the methodology in the relevant reporting standard, be conducted no more than 30 calendar days prior to an application under the streamlined approval path being made.

Information to be contained in yearly report of prudential information

This section describes the information to be provided to APRA by the holder of the approval on an annual basis. APRA has sought to avoid making the annual reporting requirement excessively onerous by proposing to only require the information necessary for it to determine if an FSSA approval under the streamlined approach is still appropriate. APRA proposes that the holder of an approval will be required to provide:

- any information that the holder is aware of that reveals that the relevant licensed company has or is likely to exceed the assets threshold;
- the amount of the stake and direct control interest held by the holder in the financial sector company/ companies for which approval was granted as at the end of the financial year for which the report is being made;
- if the holder is a company, any changes to its directors, chief executive officer, or equivalent persons; and
- an attestation on matters related to the holder's continued fitness and propriety.

As reports are required to be provided by the holder of the approval, who in most instances will not be an APRA regulated institution, APRA is not proposing to develop an approved reporting form. It is expected the report will be provided in a freeform basis similar to the format of the Risk Management Declaration required under APRA prudential standard *CPS 220 Risk Management*. APRA expects the report to be provided electronically to the relevant licensed company's APRA Supervisor.