



RESPONSE TO SUBMISSIONS

Licensing: A phased approach to authorising
new entrants to the banking industry

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Contents

Glossary	4
Executive summary	5
Chapter 1 - Introduction	6
Background	6
Consultation	6
Submissions received	6
Restricted ADI framework	7
Chapter 2 - Response to submissions	8
Introduction of a phased approach for licensing ADIs	8
Balance of APRA's mandate	8
Eligibility	9
Restricted phase	11
Minimum requirements	12
Licence restrictions	14
Financial Claims Scheme	16
Further refinement	17
Alternative approaches	19
Next steps	20

Glossary

ADI	Authorised deposit-taking institution within the meaning of the Banking Act.
ADI licence	Authorisation under section 9 of the Banking Act, to conduct banking business, with or without conditions.
APRA	Australian Prudential Regulation Authority.
Banking Act	<i>Banking Act 1959.</i>
Banking business	Banking business is defined in section 5 of the Banking Act.
FCS	The Financial Claims Scheme (FCS) is an Australian Government scheme that provides protection to deposits with ADIs and policies with general insurers in the unlikely event that one of these financial institutions fails. In the case of ADIs, the FCS only covers protected accounts held with institutions that are incorporated in Australia and recorded in Australian currency. The FCS can only be activated by the Australian Government. APRA is responsible for administering the scheme.
Fintech	Fintech refers to technology-enabled innovation in financial services.
Licensing	Licensing refers to the process by which APRA grants an ADI licence to an institution.
Protected Account	Has the meaning in section 5 of the Banking Act.
Prudential framework	Prudential framework refers to the legislation, including prudential standards and associated guidance material, which applies to the prudential regulation of ADIs.
Restricted ADI framework	As set out in the Information Paper <i>ADI Licensing: Restricted ADI Framework</i> .
Restricted ADI licence	Authorisation under section 9 of the Banking Act to conduct banking business for a limited period with specific requirements and restrictions

Executive summary

The Australian Prudential Regulation Authority (APRA) is an independent statutory authority established for the purposes of prudential supervision of financial institutions and for promoting financial system stability in Australia. APRA is responsible for, in particular, protecting the interests of depositors, insurance policyholders and most superannuation fund members¹ – collectively referred to as APRA's beneficiaries. Protecting the financial interests of these beneficiaries lies at the centre of APRA's mission.

In undertaking its role, APRA seeks to not unduly hinder other desired objectives of promoting efficiency, competition, contestability and competitive neutrality in the financial system. In licensing new entrants to the prudentially-regulated segments of the financial system, APRA aims to achieve an appropriate balance between financial safety and these other considerations.

APRA has reviewed its approach to licensing new entrants to the banking industry, with a view to making it easier for potential applicants to understand and navigate the licensing process while at the same time not materially lessening entry standards that serve as important protections for the Australian community.

To this end, APRA released a Discussion Paper *Licensing: A phased approach to authorising new entrants to the banking industry* on 15 August 2017. The Discussion Paper laid out proposals for a new licensing approach featuring the introduction of a Restricted ADI licence. The Discussion Paper, among other matters, set out the proposed eligibility criteria, timeframe, initial requirements and ongoing requirements for prospective applicants.

APRA sought submissions on the proposals and the framework was broadly supported, with some specific areas suggested for adjustment or clarification.

This paper sets out and responds to the feedback received, indicating enhancements to the Restricted ADI framework following the consultation period. The framework remains broadly consistent with the proposal set out in the Discussion Paper, with the most significant clarifications in the areas of eligibility for authorisation, nature of business for Restricted ADIs during the restricted phase, and a change to wind-up costs, which have been replaced with a resolution reserve.

Accompanying this paper is an Information Paper describing the Restricted ADI framework which is available on APRA's website at <http://www.apra.gov.au>.

APRA will refresh its ADI Authorisation Guidelines in due course to provide further clarity to potential applicants in preparing their licence applications.

¹ APRA does not supervise self-managed superannuation funds as these are regulated by the Australian Taxation Office.

Chapter 1 - Introduction

Background

In July 2017 APRA established a centralised Licensing Unit to administer the licensing of new entrants to APRA-regulated industries. APRA's Licensing Unit manages licensing applications, partnering with frontline supervisors and risk specialists to fulfil this responsibility. This is expected to deliver enhancements to the licensing approach over time.

On 15 August 2017 APRA released a Discussion Paper *Licensing: A phased approach to authorising new entrants to the banking industry*.

The Discussion Paper outlined proposals to introduce a phased approach to the ADI licensing process for certain applicants seeking to become ADIs. The approach sought to facilitate competition in the banking sector by providing eligible new entrants time to establish the full complement of resources and systems necessary to be able to meet all aspects of the prudential framework. In doing so, the proposals sought to ensure that confidence in the safeguarding of deposits with ADIs would not be diminished. The proposals also took account of a range of competitive considerations and APRA's role of promoting financial stability.

Consultation

Written submissions on these proposals were invited from all interested parties by 30 November 2017.

APRA hosted an industry roundtable on the Restricted ADI framework on 25 October 2017. This provided a further opportunity to engage with interested parties and receive feedback. Roundtables were also held on cloud based technology services which was an area of significant focus for potential Restricted ADI applicants.

In addition, APRA engaged with interested parties through a number of events including bilateral meetings, meetups and speaking engagements.

Submissions received

APRA received 16 written submissions on its proposals. These submissions were from potential new banking industry entrants, industry associations and an academic organisation. Submissions that were not marked as confidential are available on APRA's website.

All respondents supported the introduction of a phased approach to licensing ADIs. However, some sought clarification of, or raised concerns about, particular elements of the proposed approach. The most common areas related to:

- flexibility to accommodate diverse business models;
- wind-up costs;
- the deposit limit;

- the minimum capital and liquidity requirements;
- the maximum Restricted ADI time period; and
- the adoption of cloud based technology.

APRA's response to these issues is set out in Chapter 2.

Restricted ADI framework

Accompanying this paper is an Information Paper which includes the final version of the Restricted ADI framework. This incorporates the changes made in response to feedback received during consultation. The Restricted ADI framework will be available from the date of this paper.

In due course APRA will update its ADI Authorisation Guidelines to accommodate the Restricted ADI Framework.

In the interim, potential applicants should contact APRA's Licensing Unit directly at licensing@apra.gov.au with any questions about the application process.

Chapter 2 - Response to submissions

The Discussion Paper invited submissions on all aspects of the proposals. In addition, specific areas were detailed where feedback was sought on the proposed direction.

This chapter details APRA's proposals, the feedback received and APRA's response.

Introduction of a phased approach for licensing ADIs

APRA proposed a phased approach to authorising new entrants to the banking industry. This centred on the introduction of a Restricted ADI licence for certain applicants seeking to become ADIs.

Comments received

All respondents supported the introduction of a phased approach, with several 'strongly supporting' the initiative.

Submissions reflected a view that a phased approach would lower barriers to entry, encourage innovation, and facilitate the capital raising process critical to new entrants' survival. One respondent stated that the proposals 'represent a concrete approach to providing practical support to new entrants', while many emphasised the importance of retaining stability in the banking industry.

While all were supportive of the introduction of a phased approach, feedback was provided on a number of specific areas. These are outlined in the sections below.

APRA response

APRA welcomes the positive response to the proposals, noting that there was broad support across a wide range of the financial services community, from fintech start-ups through to established corporations and industry bodies.

Balance of APRA's mandate

APRA asked if the proposals strike an appropriate balance between financial safety and considerations relating to efficiency, competition, contestability and competitive neutrality.

Comments received

Generally there was agreement that the balance was appropriate and that, in all likelihood, the proposals would reduce barriers to entry without materially compromising financial stability or creating unfair competitive advantages for new entrants over incumbents.

There was an appreciation, in particular among start-up respondents, that the public's confidence in the strength of the Restricted ADI framework was critical to its businesses. One

respondent, highlighting the failure rate of start-ups, suggested that there should be a greater consideration given to capital and liquidity management to minimise risk to financial stability, while another noted the importance of not creating a 'regulatory holiday' which might impact on existing smaller ADIs.

Other responses:

- supported the proposals, citing the facilitation of new competition as likely to improve dynamic efficiency in the banking industry, and a much needed next step in achieving the Australian government's objective to promote fintech capability and move Australia into line with international trends in banking regulation;
- felt that the proposals fell short of intentions as the framework did not provide sufficient certainty, time or ability to raise the required capital;
- suggested that the principal value of the proposed phased approach is to facilitate access to capital for potential new entrants, while simultaneously developing capabilities; and
- given the often limited resources of start-ups, highlighted the importance of the new regime being simple, clear and predictable, as well as having assistance and a point of contact with APRA along the pathway.

APRA response

The submissions generally considered the framework struck an appropriate balance of APRA's mandate, however some specific areas were highlighted for APRA to consider. These areas are discussed separately below.

APRA remains committed to striking a balance between allowing competitive opportunities for new entrants and protecting both deposit-holders during the restricted phase and confidence in the Restricted ADI sector. APRA is also mindful of maintaining appropriate competitive neutrality within the community of smaller ADIs, which over time will include Restricted ADIs that have successfully progressed to an ADI licence.

Eligibility

APRA proposed that the applicants that will be eligible for a Restricted ADI licence are those that require the time to build resources and capabilities in order to meet the prudential framework. APRA envisaged that the Restricted ADI licence would appeal more to start-ups with limited financial resources and (at least initially) a simple product set.

The Discussion Paper set an expectation that applicants would not be eligible to use the restricted phase where they possess the resources and capability to apply directly for an ADI licence. This would include well-established corporations or prudentially-regulated companies such as subsidiaries of foreign banks.

Comments received

Respondents had a range of views on the appropriateness or clarity of the proposed eligibility requirements and this area received considerable focus in submissions.

A few submissions suggested that the eligibility criteria should be wider, while another suggested a two-tier arrangement to differentiate requirements between established entities and start-ups.

Some respondents requested further clarity on eligibility, including for those entities that might not initially fit the definition of a bank under the Banking Act.

Other responses:

- outlined the merits of restricting eligibility to only innovative businesses; and
- advocated limiting eligibility further to remove those that have connections to existing ADIs or where the entity cannot demonstrate a genuine need for a transitional licence.

APRA response

Feedback in submissions on this issue was mixed. However, since the release of the Discussion Paper, APRA has also had the opportunity to engage with a large number of potential Restricted ADI applicants. This engagement has provided a useful test of a range of business models that potential applicants may wish to pursue in the banking sector. It has also highlighted that some potential applicants were most interested in the Restricted ADI licence route for the open dialogue with APRA's Licensing Unit (which they did not see as available where applying directly for an ADI licence), rather than to build resources or capabilities. This feedback has also influenced APRA's considerations on eligibility.

APRA remains of the view that the Restricted ADI framework is most suited to start-ups or smaller applicants, where a Restricted ADI licence can be used as a signal to potential investors that they have a credible plan to achieve ADI status, affording recognition while still in the development stage.

The final policy makes eligibility guidelines clearer, based around a number of principles. These are centred on capabilities, resources and limited, lower-risk business and include indicative asset and equity thresholds set out below. Where applicants with established businesses are within these thresholds they will typically be considered to be eligible for the Restricted ADI licence route, provided they are not part of an existing ADI or foreign bank group.

To provide an indicative threshold on resources:

- **Balance sheet assets** - APRA will typically expect applicants, including groups, with balance sheet assets of greater than \$100 million, to apply directly for an ADI licence. Excluding branches of foreign banks, a \$100 million balance sheet currently equates to around the 15th percentile of the ADI industry.
- **Equity** - Under the Restricted ADI framework, an entity with balance sheet of \$100 million would require approximately \$20 million of equity. Institutions that have more than \$20 million of equity, or have parent institutions that have an ability to invest equity of more than \$20 million in establishing an ADI subsidiary, would typically be expected to apply via the direct route.

These indicative thresholds keep Restricted ADI applicants at the smaller end of the industry, lessening any negative impact on competitive neutrality.

The restricted route is targeted at applicants that require time to build resources and capabilities. APRA expects Restricted ADIs to be conducting limited business during the restricted phase and would not expect Restricted ADIs to grow significantly beyond the \$100 million asset size guidance.

For those applicants that are unlikely to satisfy the eligibility guidelines for a Restricted ADI licence, APRA remains committed to providing similar open dialogue and engagement through the licensing process.

Restricted phase

APRA proposed that the restricted phase would be limited to a maximum of two years. During this period the Restricted ADI would be required to demonstrate readiness for ADI status or exit the banking industry. Restricted ADIs would be able to progress to an ADI licence at an earlier stage, where the Restricted ADI was able to demonstrate readiness.

Comments received

Respondents were generally split on this issue.

Around half of the respondents were comfortable with the hard two-year deadline as it incentivised progress. It was also acknowledged that this timeframe would reflect the speed at which businesses should move to become commercially viable and APRA would progress applicants.

Most of the remaining respondents proposed a flexible approach whereby APRA could retain the capacity to extend the timeframe by a further year on a case-by-case basis, for example with set milestones. Reasons cited for a flexible deadline included the limited funding environment in Australia for start-ups, the high expense of human capital and the impact that a hard deadline would have on negotiations with potential investors.

Two other suggestions were received:

- adopt the UK approach of a limit of one year, albeit with an option to extend by a year if it was deemed the Restricted ADI could qualify for ADI status in that time; and
- a three year, three phase approach, in which a middle phase was added to the proposed licensing framework to allow the Restricted ADI to increase its business beyond the initial restrictions. This middle phase would provide a stronger signal of viability to potential investors.

APRA response

An important part of the proposed framework is the expectation that a Restricted ADI licence holder will progress to an ADI licence in a maximum of two years.

In balancing the feedback and objectives, APRA remains of the view that a maximum two year period is appropriate. APRA believes that a fixed time period has several benefits, including certainty, transparency and facilitation of exit if needed, while also avoiding an uneven playing field.

Notwithstanding these factors, APRA will, in exceptional circumstances, be prepared to extend the restricted phase for a short period of time. All Restricted ADIs will be in regular contact with APRA and significant issues of this nature will be addressed individually where required.

Minimum requirements

The Discussion Paper outlined a number of minimum requirements that would need to be met by potential Restricted ADI applicants prior to licensing. APRA asked if the proposed minimum requirements are appropriate and if there are alternatives that should be considered.

Comments received

Fit and proper and governance

Commentary received supported the application of Prudential Standard *CPS 520 Fit and Proper* (CPS 520). One respondent strongly recommended that Restricted ADI applicants meet the requirements of the forthcoming Banking Executive Accountability Regime (BEAR) to ensure governance standards apply across the industry.

Business plan

One respondent suggested metrics be set as to what constitutes appropriate funding for the business model, including technology requirements. Another respondent added that business plans should include systems and skills to manage asset and liability portfolio mismatches.

Approach to meeting the full prudential framework

One respondent encouraged APRA to provide clear guidance on the preferred format and key acceptance criteria for required documentation, and for that guidance to be delivered early in discussions with the applicant in order to assist in the production of material that would demonstrate credible plans for progress to an ADI licence in the required timeframe.

Capital

There was broad acceptance that \$3 million plus wind-up costs as minimum regulatory capital strikes an appropriate balance between the facilitation of new entrants and financial stability, notwithstanding the need for clarification of the methodology for calculating wind-up costs.

One respondent requested that mutually owned applicants continue to be permitted to have start-up capital comprising mostly Tier 2 Capital with an agreed time frame to build up Tier 1 Capital.

Risk management

Commentary received supported the application of *Prudential Standard CPS 220 Risk Management* (CPS 220).

Exit plan

Several respondents sought clarification on the issue of calculation and methodology of wind-up costs.

One respondent suggested that the requirement to hold wind-up costs of 12 months operating expenses in addition to the minimum capital requirement would seem to be too high for a well-capitalised, more substantial operating business if applied strictly. Another respondent noted that assessment of wind-up costs should be calibrated to a wind-up scenario rather than to budgeted full operating expenses, and be specific to each applicant's circumstances.

Another respondent suggested including a 'menu of options' in the exit plan as appropriate.

APRA response

In general there were no strong objections to the approach proposed. Broadly speaking, APRA has retained its proposed approach with additional clarifications.

Governance

Prudential Standard CPS 510 Governance (CPS 510) will apply to Restricted ADIs with some exemptions. Acknowledging that some Restricted ADIs may be using the restricted phase to finalise executive appointments and staff recruitment, certain concessions will be made to specific requirements regarding board composition and committees. Restricted ADI boards will not be required to maintain a majority of independent directors, nor will they be required to establish the full set of board committees. The board can maintain responsibility for committees under CPS 510 with the exception of the remuneration committee which will be the responsibility of the non-executive directors.

The forthcoming Banking Executive Accountability Regime which is implemented through legislation will apply to all licences issued under the Banking Act and therefore will apply to Restricted ADIs from 1 July 2019.

Business plan

APRA will expect business plans to detail capital and funding plans, including best and worst case scenarios, and to ensure appropriate balance sheet management systems and skills will be available during the restricted period.

Including specific metrics for funding in the policy framework beyond minimum capital and liquidity requirements is not considered plausible because of the broad spectrum of business models that are expected to be put forward for a Restricted ADI licence. In addition, part of assessing an applicant's plans, skills and capabilities is considering the applicant's own plan to manage its business.

Approach to meeting the full prudential framework

An important aspect of the proposed framework is the expectation that a Restricted ADI will progress to an ADI licence. Having a credible path to meeting the full prudential framework is a key requirement of a Restricted ADI application. Including this in the business plan demonstrates that an applicant understands the requirements of operating as an ADI. It also

assists APRA in assessing likely progress over the restricted phase. APRA appreciates that plans might require amendment over time and is committed to working with applicants to help them navigate the licensing process.

Capital, resolution reserve and exit plans

The final restricted licensing framework will retain minimum Common Equity Tier 1 (CET1) capital requirements as the greater of \$3 million plus a resolution reserve (typically set at \$1 million) or 20 per cent of total assets. The existing concessions on the composition of capital that apply to new mutually owned ADI entrants will apply in the Restricted ADI framework.

On the basis of the feedback received, APRA recognises the need to establish clear expectations for potential applicants as well as to seek consistency and transparency in relation to wind-up costs. APRA has amended the policy relating to wind-up costs and has replaced it with a resolution reserve. This will more clearly indicate the purpose of this requirement which is intended to cover APRA's administration costs should a resolution be required. The resolution reserve will be set at \$1 million, unless an applicant's business model presents specific risks. Applicants should still consider their own wind-up costs as part of their plans.

The credibility of applicant's exit plans will be considered on a case-by-case basis depending on each applicant's complexity. APRA is able to provide guidance to applicants on this.

Licence restrictions

The Discussion Paper set out a range of licence restrictions to manage risk during the restricted phase, including a limit on deposit-taking, and ongoing capital adequacy and liquidity requirements. APRA asked if the proposed licence restrictions are appropriate and whether there are alternative or other restrictions that should be considered.

Comments received

Respondents submitted wide ranging and diverse views on several parts of the proposals for restrictions during the restricted phase.

Liabilities

Respondents were split between those that felt that the \$2 million aggregate deposit limit was appropriate, those that felt it was too low, and those that felt it was too high.

Among the views that it was too low, reasons cited were that it would:

- limit potential customer numbers such as to be too few to adequately test commercial viability (which may lead to incorrect assumptions given a small data set);
- that it did not take into account those applicants that are more established businesses or those with a strong capital base; and
- it did not acknowledge applicants with more developed capabilities.

These respondents sought consideration of a more flexible or discretionary approach depending on each applicant's capital position and ongoing performance during the restricted phase.

Those respondents that felt it was too high cited overseas comparisons and the concern over hot money flight².

Capital Adequacy

Some respondents felt that the proposed 20 per cent leverage ratio would penalise those applicants with a higher asset base and would result in Restricted ADIs operating at a significant disparity to smaller ADIs.

Other responses included:

- a preference that capital adequacy be calculated as a percentage of risk weighted assets rather than total assets (assuming a suitable risk metric is applied) to ensure deposits are not used to fund high risk activities. Another respondent preferred a risk weighted asset measure in order to be able to build a genuine banking model, citing the importance of not just initial requirements, but ongoing requirements during and at the end of the restricted period; and
- a suggestion that the capital requirements would limit potential for growth in their existing business lines operating in other aspects of financial services.

Liquidity

Some respondents felt that the proposed Minimum Liquidity Holdings (MLH) requirements of 20 per cent were a little high and proposed taking into account MLH as part of a more flexible approach towards the deposit limit. One respondent felt MLH should begin higher and that there should be a phased approach to MLH commensurate with the entity's maturity and sophistication.

Nature of business

Respondents sought greater clarity around APRA's proposal that Restricted ADIs are 'not expected to be actively conducting banking business with the general public'. It was suggested that in order to adequately test product design and operation, a wider consumer set than staff, friends and family is required. The importance of revenue generation to attract investment was also noted, as was a proposal to allow a customer base of a few thousand consenting and fully informed early adopters.

One respondent asserted that it was essential that Restricted ADIs be able to actively conduct banking business under a strict set of conditions, suggesting that restrictions on business activity gives incumbents the opportunity to copy the Restricted ADI's technology and processes. Stringent restrictions might have the unintended consequence of certain businesses engineering themselves not to require an ADI licence which would increase the shadow banking sector.

² Hot money is money which is likely to be withdrawn hastily following small changes in market conditions.

Alternative restrictions

There was some general support for greater flexibility in approaching restrictions through the Restricted ADI period, and for a process whereby there could be a gradual easing of restrictions as the Restricted ADI proved its capabilities to develop robust systems and risk management frameworks.

APRA response

APRA will retain the deposit limit of \$2 million on the aggregate balance of all protected accounts and the deposit limit of \$250,000 on the aggregate balance of all protected accounts held by an individual account-holder. Restricted ADIs will not be required to meet the full prudential framework and are unlikely to have finalised and embedded risk management practices. Because of this, it is appropriate to limit the benefit Restricted ADIs receive from being covered by the Australian Government's Financial Claims Scheme.

It is also for this reason that Restricted ADIs should not actively conduct business. Restricted ADIs can conduct limited new business or grow existing business within the \$100 million asset threshold set out in the eligibility guidance. APRA considers Restricted ADIs should be dealing with 'friends and family' type depositors who understand the risk associated with their status as a Restricted ADI. By not actively conducting banking business, Restricted ADIs can focus their attention on demonstrating their readiness to meet the requirements of the full prudential framework and transition to an ADI licence as soon as possible. This provides applicants with greater clarity on what is permitted in terms of 'actively conducting banking business'.

APRA has retained its proposals on minimum capital and liquidity requirements. These are important safeguards for entities operating under a Restricted ADI licence.

For clarity, the limit only applies to protected accounts, and does not include pre-paid card business. APRA has amended the liquidity requirements for Restricted ADIs to ensure adequate high quality liquid assets are held against protected accounts as well as stored value i.e. pre-paid cards.

In establishing the Restricted ADI framework, APRA believes it is important that the status and framework applying to a Restricted ADI is clear to all. A gradual easing of restrictions would introduce ambiguity into what investors and depositors are dealing with. However APRA is a proportionate, risk-based regulator and will assess the applicant against the relevant prudential standards on a basis proportionate to the size and complexity of the applicant's business model.

Financial Claims Scheme

The FCS may be activated by the Government as a last resort in the event of a failure, and as such it is an important safety net and backstop to financial system stability. The Discussion Paper proposed that while applicants will be expected to have credible exit plans that protect depositors without reliance on the FCS, APRA will need confidence that the applicant is able to provide the necessary information, should the FCS be activated. APRA asked if the

proposals are appropriate in the context of the last resort protection afforded to depositors under the FCS.

Comments received

Respondents that replied to this question were unanimous in their support of the FCS reporting obligations for Restricted ADIs.

APRA response

APRA has retained its position in the final framework.

Further refinement

APRA asked if there were other refinements to the licensing process that should be considered.

Comments received

Respondents covered a range of topics under this question.

Licensing process

Some respondents sought greater certainty around the time frame for the processing of Restricted ADI applications, transparency on progress towards ADI licence, more guidance on considerations around issuing a conditional ADI licence, and encouraged a coordinated inter-agency approach given requirements of other government agencies.

Technology and innovation

Some respondents requested a flexible approach to the adoption of new technology, notably the use of cloud offerings, and early engagement with APRA to understand expectations on technology platforms. Some respondents also commented on the commitment to open data access and automated switching.

Some respondents suggested APRA allow Restricted ADIs to use cloud services to help foster innovation and so as not to put local entities at a competitive disadvantage to offshore peers.

Ongoing business

There were requests for clarity around the treatment of already established business lines both through the restricted phase and in the event of an exit from the banking industry.

Policy framework

Submissions included:

- advocating Restricted ADIs be required to use the terminology 'restricted bank' during the restricted phase;
- a suggestion that, upon gaining an ADI licence, there be transitory arrangements for up to a year to build capital conservation buffers;
- a proposal that APRA support open banking and simplified or automated switching between banks for all regulated ADIs; and
- a suggestion that the minimum requirements should include detailed capital and funding plans for adequate resourcing, balance sheet management skills, forecasts and liquidity management policies and procedures.

APRA response

Submissions in relation to the licensing process were generally accepted as outcomes APRA should strive towards. The creation of the centralised Licensing Unit at APRA will assist in achieving these outcomes over time.

In relation to setting time frames for a licence decision, however, this is not practical to achieve in the context of the APRA licensing process as time to decision will always depend on a large number of factors. These factors include the quality of the application received, the responsiveness of applicants to requests for further information, complexity of the business model (in particular where precedents may be set), and the number of licence applications being considered at any one time. Currently APRA engages with individual applicants to discuss indicative timeframes to assist with planning. Setting an arbitrary deadline is likely to see some applications rejected which might otherwise be viable.

In relation to technology and innovation, APRA remains open to engagement with all applicants on considering innovative approaches. APRA seeks to remain neutral on the approach or technology used, as long as the risks are understood and managed appropriately. APRA has recently released draft *Prudential Standard CPS 234 Information Security* for consultation, and is currently updating its guidelines on outsourcing arrangements involving shared computing services (including cloud) in response to developments over the past years. There are a range of avenues for applicants to engage with APRA on innovation and applicants are encouraged to approach APRA where they think there is benefit in engagement.

In relation to ongoing business, APRA has sought to clarify the treatment of already established business lines through its updated eligibility guidelines and confirmation of ongoing licence requirements which apply across the business. In the event of an exit from the banking industry, APRA's primary interest is the protection of depositors and minimising any impact on financial stability; once these objectives are met APRA would revoke the Restricted ADI licence (and, with it, permission to use any restricted words such as 'bank'), and any further business that the institution wished to continue or pursue would not be under the remit of APRA.

Parliament has recently passed an amendment to Section 66 of the Banking Act, such that as of 4 May 2018 any ADI, including Restricted ADIs, can use the term 'bank' unless APRA determines otherwise.

APRA has determined that requiring the use of the term 'restricted bank' is unnecessary given that only limited banking business would be conducted and deposits are still protected under the FCS as they would be with any other ADI. However, APRA will require that Restricted ADIs take all reasonable steps to ensure that it is clear to all customers and potential customers that they are Restricted ADIs. This includes requiring a disclosure statement on all promotional, marketing and disclosure material, whether in paper form, electronic form or website or social media based content.

Alternative approaches

APRA sought and received some alternative suggestions from respondents.

Comments received

Responses included:

- a suggestion to create a new classification of depositor along the lines of a 'sophisticated investor'. This would be defined as a person with a minimum \$500,000 of net assets available to invest and a minimum deposit of \$100,000. Restricted ADIs could then only take deposits from these 'sophisticated depositors', which would not be covered by FCS;
- a proposal of a framework with multiple categories of Restricted ADI with different requirements and restrictions to better cater for the diversity of applicants, the different stages of business maturity, and varying access and levels of capital; and
- a proposal to create an 'Australian Small Business Fund' based on the success of the British Business Bank established by the UK Government in partnership with a number of private companies.

APRA response

Any legislative changes to amend the definition of depositor or eligibility for the FCS are a matter for Government, not APRA. Such legislative changes would require an extensive consultation period which would delay establishment of the Restricted ADI framework. APRA has sought to provide the flexibility of the Restricted ADI framework in a timely fashion and is not proposing to pursue changes to the definition of depositor or eligibility for the FCS.

APRA notes the suggestion for multiple classes of Restricted ADI, but is of the view that this would introduce greater complexity into the licensing process and less clarity over what a Restricted ADI licence represents for those interacting with Restricted ADIs. Allowing fewer restrictions for some Restricted ADIs would also increase risk and reduce competitive neutrality, which was a concern for many respondents.

After active engagement with potential applicants and respondents, APRA is of the view that the ADI licence presents a suitable entry route for applicants with greater resources and capabilities. This approach better balances APRA's objectives than establishing multiple Restricted ADI entry routes.

Next steps

Accompanying this paper is an Information Paper describing the Restricted ADI framework. The Restricted ADI framework is available from the date of this paper. This Response Paper and the Information Paper for the Restricted ADI Framework are available on APRA's website at <http://www.apra.gov.au>

In the coming months APRA will refresh its ADI authorisation guidelines to provide further clarity to potential applicants for preparing their licence applications.



 **APRA**