



Response to Submissions

Religious charitable development funds


August 2013

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Preamble

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

In April 2013, APRA released a consultation package on the future operation of certain exemption orders made under the Banking Act. The package comprised a discussion paper, *Banking Act exemptions and section 66 guidelines*, as well as revised draft *Guidelines on Implementation of section 66 of the Banking Act 1959*.

The paper set out APRA's proposals to amend existing exemptions, including Banking exemption No. 1 of 2011 for religious charitable development funds (RCDFs).

This response paper sets out the key matters raised in submissions on the RCDF Exemption Order and APRA's response to those submissions. APRA has revised its original proposals in important respects, details of which are set out in this paper. The RCDF Exemption Order was recently remade, unchanged, and will now expire on 30 June 2014. The future operation of the order will depend on the final decisions made after APRA has considered submissions on its revised proposals.

APRA is seeking comments from interested parties on its revised proposals. Submissions should be sent to exemptiondp@apra.gov.au not later than 4 October 2013 and addressed to:

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Policy, Research and Statistics
Australian Prudential Regulation Authority
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SYDNEY NSW 2001

Important disclosure notice – publication of submissions

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

Submissions may be the subject of a request for access made under the *Freedom of Information Act 1982* (FOIA). APRA will determine such requests, if any, in accordance with the provisions of the FOIA. Information in the submission about any APRA regulated entity 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.

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Glossary

ADI	Authorised deposit-taking institution as defined in the <i>Banking Act 1959</i> .
Affiliates	The classes of persons set out in paragraph 4(a), Schedule 2 of Banking exemption No. 1 of 2013, but not including retail investors, lay persons, clergy, staff or other natural persons
APRA	Australian Prudential Regulation Authority
April discussion paper	<i>Banking Act exemptions and section 66 guidelines</i>
ASIC	Australian Securities and Investments Commission
ATM	Automatic Teller Machine
Banking Act	<i>Banking Act 1959</i>
BCC	Business cost calculator
BPAY	BPAY facility offered by BPAY Pty Limited ACN 079 137 518
Corporations Act	<i>Corporations Act 2001</i>
Debenture	Has the meaning given in section 9 of the Corporations Act
EFTPOS	Electronic Funds Transfer at Point of Sale
FCS	Financial Claims Scheme
MIS	Managed Investment Scheme, being a scheme that has the meaning given in section 9 of the Corporations Act
RCDF	Religious charitable development fund
RCDF Exemption Order	Banking exemption order No. 1 of 2013
Retail investor	A person who would be a retail client under section 761G of the Corporations Act
Retail product	Securities, a financial product or any other arrangement involving the taking of money on deposit offered to a retail investor
RFC	Registered Financial Corporation
Wholesale investor	A person other than a retail investor

Chapter 1 – Introduction

In April 2013, APRA released a discussion paper, *Banking Act exemptions and section 66 guidelines* (the April discussion paper) that set out, amongst other matters, proposals for the future operation of the order that exempts religious charitable development funds (RCDFs) from the need to be authorised under the Banking Act. That order, previously Banking exemption No. 1 of 2011, was remade unchanged in June as Banking exemption No. 1 of 2013 (RCDF Exemption Order). The order expires on 30 June 2014.

APRA's proposals for RCDFs took into account the global principle governing the permissible activities of banking institutions, as set out in the Core Principles for Effective Banking Supervision.¹ The principle requires, *inter alia*, that the taking of deposits from the public be reserved for institutions that are authorised and prudentially regulated as banking institutions. At the same time, APRA acknowledged that the RCDF Exemption Order had been a long-standing one and that many RCDFs have structured aspects of their religious and charitable operations in a manner that relies on funds from retail investors.

In the April discussion paper, APRA proposed to withdraw the current RCDF Exemption Order for RCDFs accepting investments from retail investors as from end June 2014. An RCDF wishing to offer retail-type products would have to seek authorisation to become an ADI, register as a Registered Financial Corporation (RFC) or operate a registered managed investment scheme (MIS).

APRA's objective with these proposals was to minimise the risk that investors in RCDFs form the impression that an RCDF is the same as an authorised deposit-taking institution (ADI) and that the products it offers are the same as an ADI product. RCDFs accepting retail deposits do so without the prudential oversight that applies to deposits held at ADIs; APRA has no responsibility for the prudential oversight of RCDFs or their activities. Accordingly, the existing RCDF

Exemption Order requires an RCDF to disclose that it is not prudentially supervised by APRA and that contributions do not obtain the benefit of depositor protection. However, the public response to recent RFC failures has demonstrated that, even with such disclosures, investors may still consider that the security of their investment in entities granted an explicit exemption by APRA and offering ADI-type products is equivalent to a deposit with an ADI.

APRA received a total of 22 submissions on its proposals relating to RCDFs. Although there was support for some aspects of the proposals, general concern was expressed about the key proposal to require RCDFs that wished to continue to accept funds from retail investors to do so under another regulatory regime. Concerns centred around the cost of restructuring under the proposed alternative regimes and the impact of restrictions on retail funding on the future operation of RCDFs. Many RCDFs argued that they would need to curtail or abandon some of their religious and charitable activities if APRA were to proceed with the proposals.

After consideration of submissions, the gathering of further information about RCDF business models, and discussions with RCDFs, APRA has decided to revise its original proposals. APRA is no longer proposing that an RCDF wishing to offer products to retail investors would need to operate under a different regulatory regime. However, consistent with the global principle governing the boundaries between prudentially regulated institutions and shadow banking, APRA remains of the view that unauthorised entities should not be able to offer deposit products or products with features and characteristics that are clearly associated with product offerings of ADIs. Accordingly, APRA is proposing to apply additional conditions to the existing RCDF Exemption Order, consistent with those proposed for RFCs.

¹ For further details refer to the Bank of International Settlements website, Core Principles for Effective Supervision at <http://www.bis.org/publ/bcbs230.htm>

APRA is mindful that the Australian Securities and Investments Commission (ASIC) has recently consulted on proposals to amend its exemptions currently available to charitable investment fundraisers, which include a significant number of RCDFs, under *ASIC Regulatory Guide 87 Charities*.

APRA's revised proposals, set out in Chapter 2, will achieve its overall objective of ensuring that retail investors in RCDFs do not confuse their investment with deposit or transactional banking accounts provided by ADIs, while recognising the importance of the fundraising activities undertaken by RCDFs and the absence of failures in this sector historically.

The revised proposals will have their main impact on retail funding raised by RCDFs on an at-call basis. Data provided to APRA suggest that around 17 per cent of the total funding of RCDFs is sourced from retail investors and, of this, around half is at-call. APRA would expect that a significant proportion of retail at-call funding could and would switch to 31-day or longer funding, during the transition period APRA intends to provide for the new exemption arrangements. If so, the ultimate impact of the proposals on total RCDF funding is likely to be small.

Chapter 2 – Response to submissions

This chapter sets out APRA's response to submissions on issues that were set out in the April discussion paper.

2.1 Retail funding

In the April discussion paper, APRA proposed to withdraw the current RCDF Exemption Order for RCDFs accepting investments from retail investors as from end June 2014. An RCDF wishing to offer retail-type products would have to do so under an alternative regulatory regime.

Comments received

Generally, submissions were not supportive of this proposal. Concerns centred around the impact of the proposal on the religious and charitable work undertaken by RCDFs using retail funding. Submissions argued that requiring RCDFs to operate under an alternative regulatory regime would have a detrimental impact on the provision of services including schools, hospitals, aged care and social welfare programmes, amongst others. They argued that alternative regimes – seeking authorisation to become an ADI, register as an RFC or operate a registered MIS – would be administratively burdensome and the associated costs would impede the religious and charitable works of RCDFs.

Some submissions suggested they be allowed to continue to accept funds from retail investors but with additional conditions on the RCDF Exemption Order, such as requiring an investor to provide a signed declaration stating that they understand that their investment is not equivalent to a deposit with an ADI and does not enjoy the benefit of depositor protection.

APRA's response

Further analysis by APRA has suggested that it can achieve its objective of minimising the risk that investors in RCDFs confuse their investments with products provided by ADIs, at a lower cost to RCDFs than would have arisen from APRA's original proposal. Additional information from RCDFs has shown that the administrative costs and lost net interest income associated with APRA's original proposal would be higher than APRA had presumed. Accordingly, APRA has decided to revise its original proposal, in a way

that would materially reduce the administrative and lost interest income costs for RCDFs without compromising APRA's objective.

Under the revised proposal, APRA would not require RCDFs wishing to offer products to retail investors to operate under an alternative regulatory regime. Rather, APRA would extend the RCDF Exemption Order from 1 July 2014, but subject to additional conditions. RCDFs will continue to be able to raise funds from retail investors, but not on an at-call basis. At-call products could be easily misconstrued by retail investors since such products are associated with transactional accounts offered by ADIs.

The proposed additional conditions would require that any account offered to a retail investor lacking a stated maturity date have at least a 31-day notice period prior to any withdrawal. Any term investment would need to commence with a stated term of at least 31 days. On maturity of a term investment, an RCDF could, where the investor has requested repayment, repay the funds via cash, cheque or direct credit to an account at an ADI. Where the investor has not requested repayment, the funds would have to be rolled over into a new investment with a minimum term of 31 days.

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

These proposed conditions would not relate to funding from wholesale investors. RCDFs may continue to offer at-call products to wholesale investors.

2.2 Terminology

Currently, there are no restrictions on the use of the terms 'deposit' and 'at-call' by RCDFs. In the April discussion paper, APRA proposed restricting the use of these terms.

Comments received

Generally, submissions accepted this proposal.

APRA's response

On remaking the RCDF Exemption Order, APRA will restrict the use of terms 'deposit' and 'at-call' and derivatives of these terms. RCDFs will no longer be allowed to use such terminology in relation to retail products or in marketing to retail investors.

2.3 Transaction facilities including BPAY

In the April discussion paper, APRA proposed to restrict RCDFs from offering BPAY facilities. This was in addition to existing restrictions under the RCDF Exemption Order that prevents RCDFs from offering ATM, EFTPOS and cheque account facilities, other than to affiliates of the RCDF.

Comments received

The proposal to limit BPAY generated a considerable level of comment in submissions. RCDFs were generally not supportive of the proposal and questioned whether it also covered the use of BPAY between affiliates of an RCDF.

APRA's response

On remaking the RCDF Exemption Order, APRA will restrict RCDFs from offering BPAY payment functionality in relation to products offered to retail investors, as such facilities are associated with ADI transaction accounts. This approach is consistent with the current Exemption Order, which does not allow ATM, EFTPOS and cheque functionality to be offered for RCDF retail accounts. However, RCDFs themselves will be able to continue to make or receive payments, including new retail investments, via BPAY. An RCDF will also be able to continue to use BPAY to transact between affiliates of the RCDF.

2.4 Prudential warning

Currently, RCDFs must ensure that advertising and marketing material of the RCDF contains clear and prominent disclosures to the effect that:

- neither the controlling entity or the Fund is prudentially supervised by APRA;
- contributions to the RCDF do not obtain the benefit of the depositor protection provisions of the Banking Act; and
- the Fund is designed for investors who wish to promote the charitable purposes of the Fund.

As part of its review of the RCDF Exemption Order, APRA has noted instances where RCDFs are putting such disclosures in the fine print of documents or in other places where it is questionable that the disclosure is clear and prominent to a person considering investing in the RCDF. APRA reiterates that all such disclosures must be in a clear and prominent place on all advertising and marketing material. In addition, APRA is proposing that the existing disclosure be expanded to include a statement to the effect that an investment in an RCDF is not covered by the Financial Claims Scheme.

APRA considers such disclosures are important in clarifying to retail investors the nature of the investment they are undertaking and that the RCDF is neither authorised nor prudentially supervised by APRA.

2.5 Clarification of meaning of key terms

Comments received

A number of terms were used in the April discussion paper for which definitions were not explicitly provided. APRA considered that the meaning of such terms was generally understood but some submissions requested clarifications.

APRA's response

For the purposes of clarification, APRA confirms the meaning of the following terms:

'affiliates' means the classes of persons set out in paragraph 4(a), Schedule 2 of Banking exemption No. 1 of 2013, but not including retail investors, lay persons, clergy, staff or other natural persons;

'debenture' has the meaning given in section 9 of the *Corporations Act 2001* (Corporations Act);

'retail investor' is a person who would be a retail client under section 761G of the Corporations Act; and

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

Chapter 3 – Future operation of RCDF Exemption Order

3.1 Transition arrangements

Under APRA's revised proposals, RCDFs listed on the current RCDF Exemption Order at 30 June 2014 will be allowed to continue to operate under that Order. This recognises the long-standing nature of APRA's exemption regime for many of these RCDFs. Listed RCDFs will have a period of six months from that date to transition to the new Exemption Order. That is, RCDFs would need to comply with the additional conditions from 1 January 2015. There will be no grandfathering of existing accounts if those accounts do not meet the conditions in the new Exemption Order.

APRA will continue to review the RCDF Exemption Order on a periodic basis and seek to amend conditions where circumstances warrant.

Other religious and charitable entities that wish to accept funds from retail investors but do not seek authorisation as an ADI will have the option of registering an RFC or an MIS. APRA's proposed exemption order for RFCs, as set out in the April discussion paper, will allow a body to accept term funding from retail investors provided it meets the conditions under the exemption order, and conditions imposed by ASIC on retail debenture issuers.

3.2 Notifying APRA of changes to contact details

To ensure that contact details are kept up-to-date, APRA will from time to time seek information from RCDFs. Contact details for this purpose include the contact person and their telephone number and email address; and general contact details of the RCDF including name, address, email, and telephone number. To assist in this process, APRA encourages RCDFs to notify it as soon as practicable of any changes to their contact details.

Chapter 4 – Request for cost-benefit analysis information

To improve the quality of regulation, the Australian Government requires all proposals to undergo a preliminary assessment to establish whether it is likely that there will be business compliance costs. In order to perform a comprehensive cost-benefit analysis, APRA welcomes information from interested parties.

As part of the consultation process, APRA requests respondents to provide an assessment of the impact of the proposed changes and, specifically, the marginal compliance costs entities are likely to face. Given that APRA's proposed requirements may impose some compliance costs, respondents may also indicate whether there are any other requirements relating to them that should be improved or removed to reduce compliance costs. In doing so, please explain what they are and why they need to be improved or removed.

Respondents are requested to use the Business Cost Calculator (BCC) to estimate costs to ensure that the data supplied to APRA can be aggregated and used in an industry-wide assessment. APRA would appreciate being provided with the input to the BCC as well as the final result. The BCC can be accessed at www.finance.gov.au/obpr/bcc/index.html.



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