17 December 2021

Committee Secretariat
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

By email: economics.sen@aph.gov.au

Dear Secretariat

Inquiry into the Financial Accountability Regime Bill 2021 [Provisions] and Financial Services Compensation Scheme of Last Resort Levy Bill 2021 [Provisions] and related bills

COBA appreciates the opportunity to contribute to the Senate Economics Committee's inquiry into the Financial Accountability Regime Bill 2021 (the FAR Bill) and Financial Services Compensation Scheme of Last Resort Levy Bill 2021 and related bills (the CSLR Bills).

COBA is the industry association for Australia's customer owned banking institutions (mutual banks, credit unions and building societies).

Collectively, our sector has $153 billion in assets and more than 4.5 million customers. Customer owned banking institutions account for around two thirds of the total number of domestic Authorised Deposit-taking Institutions (ADIs) and deliver competition and market leading levels of customer satisfaction in the retail banking market.

Key points

- **Commencement of the FAR should be no earlier than six months after all elements of the regime (Ministerial rules, regulations, guidance) are finalised.**
- **The threshold in the FAR for enhanced compliance entities should be increased to $20 billion in total assets, to align with other regulatory thresholds imposed on ADIs.**
- **On the CSLR, COBA does not support the inclusion of ADI credit providers within the scope of the CSLR regime. Given the prudential regulatory framework, the likelihood of an unpaid AFCA determination by an ADI is extremely remote.**
- **In relation to CSLR funding, COBA requests the Committee's support for a levy-setting process that allows levied entities time to anticipate and plan for potential costs.**

COBA's position on the FAR Bill

Key elements of the FAR not contained in the primary legislation

Key elements of the FAR, i.e. Ministerial rules, regulations and other guidance material, are not yet available. Until they are available, regulated entities do not have clarity and certainty and about the

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new regime. This factor is accentuated by the fact the FAR has not one but two regulators: APRA and ASIC.

Development of these key elements should be subject to appropriate consideration and consultation.

While COBA appreciates efforts to provide additional details on the proposed prescribed responsibilities, enhanced notification threshold and regulator coordination in Treasury's earlier consultation, the lack of certainty on the final position for these key elements poses considerable challenges for industry in understanding the full extent of the obligations they face.

Most challenging for COBA members is the absence of the Ministerial rules. The FAR Bill allows the Ministerial rules to prescribe responsibilities and positions for individuals within accountable entities.[1]

Prescribed responsibilities and positions within ADIs are critical elements of the FAR for COBA members and will require adequate time and preparation to implement.

The new responsibilities under the FAR compared to the Banking Executive Accountability Regime (BEAR) are likely to require that existing contracts of employment will have to be reviewed and updated to make clear who has responsibility for each of these prescribed responsibilities. Implementation considerations will include dealing with cases of overlapping responsibilities.

For example, we understand that the prescribed list of responsibilities and positions will contain a new end-to-end product responsibility.[2] Once the detail on the new end-to-end product responsibility becomes available in the Ministerial rules, regulated entities will need to conduct significant internal review processes to ensure all products are properly assigned and reconciled. In the absence of certainty around the new responsibility, regulated entities are unable to properly prepare for its commencement.

The FAR Bill also provides the power for the Minister to make rules to determine when an accountable entity meets the enhanced notification threshold.[3]

The threshold for enhanced notification requirements is a significant issue for our sector. Earlier proposals[4] from Treasury indicated that the threshold for ADIs may be set at "total assets > $10 billion". We note that the threshold for "small ADIs" under the BEAR is also $10 billion. A number of COBA members are clustered around the $10 billion mark in terms of their asset size.

This raises two issues:

- the appropriateness of the $10 billion threshold (discussed below), and
- the need for certainty as soon as possible about the threshold for planning and transition purposes, i.e. entities need to understand whether they will be subject to the core versus enhanced compliance obligations and obligations for accountability maps and statements to be produced to APRA and ASIC.

COBA members have recently executed a massive regulatory change implementation program where significant elements of the new regimes were finalised just months or even weeks ahead of commencement.

[1] Financial Accountability Regime Bill 2021, Section 10(4)

[2] https://treasury.gov.au/sites/default/files/2021-07/c2021-169627-policy-paper.pdf

[3] Financial Accountability Regime Bill 2021, Section 31(3)

[4] https://treasury.gov.au/sites/default/files/2021-07/c2021-169627_questionsandanswers_2.pdf

In October 2021, COBA members simultaneously implemented design and distribution obligations and new anti-hawking, breach reporting, internal dispute resolution and insurance selling requirements. As ASIC noted, these reforms "require significant changes to businesses' systems and processes."[5]

Key decisions about the scope and applications of these reforms were finalised at a very late stage, magnifying the complexity of the implementation process for regulated entities.

COBA urges policymakers to prioritise certainty and adequate implementation periods when introducing regulatory change.

Threshold for enhanced notification requirements should be increased

COBA supports the tiered approach for the 'core' and 'enhanced' compliance model. This will reduce the regulatory burden on smaller ADIs without creating any material accountability risks.

COBA requests that the Committee support an increase in the proposed threshold for enhanced notification obligations from $10 billion to $20 billion in total assets for ADIs.

This would align with APRA's $20 billion threshold for its simplified capital framework for smaller, less complex ADIs and align with APRA's $20 billion threshold for significant financial institution status under the new remuneration standard, CPS 511.

Commencement date

The currently proposed commencement settings for the FAR should be revised. COBA requests that FAR commencement should be no earlier than six months from the date of finalisations of all rules, regulations and guidance materials.

The FAR legislation is set to commence on 1 July 2022 or six months after Royal Assent. Given the Bill will not pass before 31 December 2021, the 1 July 2022 commencement date is no longer applicable and regulated entities will have six months from the date of the Bill's Assent to prepare for the regime.

COBA does not consider six months from the Bill's commencement as adequate time to prepare for the commencement of the FAR, given the extent of uncertainties around the regime in the absence of finalised Ministerial rules, regulations and other guidance materials.

It is crucial that development of these elements is subject to appropriate consideration and consultation. Once finalised, regulated entities will need adequate time to understand the full scope of the regime and allocate responsibilities, update accountability maps and statements, review the entity's risk position, update reporting systems and obtain board approvals.

This means commencement of the FAR should be no earlier than six months after the full extent of the regulatory regime has been finalised, including any rules, regulations or guidance.

Ideally, FAR commencement should align with the commencement of APRA's prudential standard on remuneration, CPS 511. For ADIs that are significant financial institutions, CPS 511 will commence from 1 January 2023, and for other APRA-related entities from 1 January 2024.

[5] https://asic.gov.au/about-asic/news-centre/find-a-media-release/2021-releases/21-213mr-asic-s-approach-to-new-laws-reforming-financial-services-sector/

COBA's position on the CSLR Bills

CSLR regime should not include ADI credit providers

COBA encourages the Committee to reconsider the inclusion of credit provision by authorised deposit-taking institutions (ADIs) within the scope of the CSLR. COBA supports a safety net for consumers who are victims of unpaid AFCA determinations but we are unaware of any evidence of unpaid AFCA determinations by ADI credit providers.

COBA notes that the set of sub-sectors of AFCA determinations previously proposed for inclusion in the CSLR has changed since earlier consultation.

Section 1065(2) of the Financial Sector Reform (Hayne Royal Commission Response No. 3) Bill 2021[6] allows AFCA determinations relating to the provision of credit to be captured in the CSLR's remit. While not yet confirmed in the regulation, COBA understands that credit providers will be responsible for paying levies to fund the CSLR's operation.

COBA questions inclusion of credit provision in the CSLR regime to the extent that it captures credit provision by ADIs. As APRA-regulated entities, COBA members are subject to prudential regulation, close supervision and capital requirements to protect against insolvency. The risk of an unpaid AFCA determination from an ADI is significantly lower than that from a non-ADI credit provider (i.e. an entity which is not subject to prudential regulation and capital requirements).

As noted above, we are unaware of any evidence of unpaid AFCA determinations against ADIs relating to credit provision.

The CSLR Bills and Explanatory Memorandum do not provide sufficient explanation on the reason for including credit provision within the scope of the CSLR. Instead, the Explanatory Memorandum provides a brief reference to the extension of the regime beyond personal financial advice, stating:

> *"In its response to the Royal Commission, the Government committed to improving consumer and small business access to redress, including by implementing an industry-funded, forward-looking CSLR that extends beyond personal financial advice failures."*[7]

Treasury's Discussion Paper in 2019 recognised that there is no evidence of unpaid determinations in Australia relating to the provision of prudentially regulated services:

> *"Over recent years, there is no evidence of unpaid determinations in Australia relating to the provision of prudentially regulated banking, insurance and superannuation services to consumers and small businesses."*[8]

While we understand that the CSLR deliberately carves out prudentially regulated activities (e.g. deposit taking) from sectors where not all participants are prudentially regulated (e.g. the provision of credit), there is no evidence to demonstrate that ADI credit providers are causing the harm intended to be addressed by the creation of the CSLR.

The extension of the CSLR regime to capture ADI credit providers may create unfair outcomes, by requiring ADI credit providers, who are meeting their obligations under AFCA, to cover the costs of non-ADI credit providers who have not paid AFCA determinations against them.

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[6] Financial Sector Reform (Hayne Royal Commission Response No. 3) Bill 2021

[7] FAR and CSLR Bills – Explanatory Memorandum

[8] CSLR Discussion Paper 2019

Entities should have more certainty about costs under the CSLR

Regulations and a legislative instrument will determine the levy framework for the CSLR and hence the costs for relevant entities.

COBA notes the Government intends to fund the establishment of the scheme and its operation in the first year.

However, our members are concerned about the uncertainty surrounding the funding arrangements for the CSLR in subsequent years, given the absence of finalised regulations and legislative instrument which provides many of the details.

In Division 1 of the Financial Services Compensation Scheme of Last Resort Levy Bill 2021,[9] a levy will be imposed "*if a person is a member of a sub-sector of a kind prescribed by the regulations*."

While COBA understands that the sub-sectors prescribed in the regulations are intended to mirror the sub-sectors of claims payable under the CSLR, the uncertainty around who will be funding the regime is undesirable. It is important to our members to have clarity on whether credit providers will be included.

In addition, members have expressed concern about limited visibility on how the levy will be calculated. The Explanatory Memorandum gives some indication of levy calculation, without providing the level of detail that would allow levied entities an understanding about the potential costs they may incur:

> *"The total amount of annual levy payable is determined by the CSLR operator in a legislative instrument. Amounts payable by individual firms in a sub-sector will be worked out in accordance with a method to be prescribed in the regulations – drawing on concepts in place for the similar calculations for ASIC supervisory cost recovery levy framework."*[10]

More visibility of the anticipated costs for the CSLR regime would afford our members more time to plan and budget for any additional costs.

I hope this submission assists the Committee in assessing the Bills. Please do not hesitate to contact Maryanna Vasilareas (mvasilareas@coba.asn.au) if COBA can be of any further assistance to the Committee.

Yours sincerely

MICHAEL LAWRENCE
Chief Executive Officer

[9] https://www.legislation.gov.au/Details/C2021B00171

[10] FAR and CSLR Bills – Explanatory Memorandum