



20 September 2017

Wayne Poels
Executive Director
Office of Best Practice Regulation
Department of Prime Minister and Cabinet

Dear Mr Poels

STRENGTHENING APRA'S CRISIS MANAGEMENT POWERS – REGULATION IMPACT STATEMENT (RIS)

This letter certifies that previous public reports have involved processes and a level of analysis equivalent to a final assessment Regulatory Impact Statement (RIS) as set out in the Australian Government Guide to Regulation March 2014 (the Guide).

The reports will support the introduction of the Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017 (the Bill) in the 2017 Spring Sitting of Parliament.

Overview

The Bill provides the Australian Prudential Regulation Authority (APRA) with an enhanced suite of crisis resolution powers applicable to prudentially regulated authorised deposit-taking institutions (ADIs), general insurers and life insurance companies (insurers), and certain group entities. It also provides APRA with clear powers to set appropriate prudential requirements for resolution planning, and to address potential barriers to the orderly resolution of regulated institutions and groups, prior to any crisis occurring.

Independent Review and Consultation Papers used for Self-Certification

Treasury considers that the matters which must be covered in a final assessment RIS have been addressed through the:

1. Financial System Inquiry Final Report (Murray Inquiry) (<http://fsi.gov.au/publications/final-report/>);
2. 2012 consultation paper 'Strengthening APRA's Crisis Management Powers' (Crisis Management Consultation Paper) (<https://static.treasury.gov.au/uploads/sites/1/2017/06/Discussion-Paper-1.pdf>); and
3. 2011 consultation paper 'Financial Claims Scheme' (FCS Consultation Paper) (https://archive.treasury.gov.au/documents/2025/PDF/CP_Financial_Claims_Scheme.pdf).

These papers examine gaps in the existing regulatory crisis management toolkit and other regulatory frameworks relevant to the resolution of a distressed entity, and make recommendations to address these gaps. In particular, the Murray Inquiry noted that Council of Financial Regulators (CFR) agencies reviewed the existing crisis management legislative provisions for prudentially regulated institution with particular reference to international standards and developments. The CFR agencies found that although Australia has a strong framework, there are gaps in powers that could be strengthened.

There has also been consultation with key stakeholders on the matters covered in the Bill.

Addressing the RIS questions

Question 1 and 2 – the problem and why government action is needed

The experience of other countries during the global financial crisis demonstrated that, when complex financial groups enter distress, failure to resolve these entities in an orderly fashion can lead to severe adverse economic consequences. To achieve effective resolution, it is essential for regulators to have access to flexible, timely and robust resolution powers.

In Australia, financial institutions play a key role in providing a range of functions essential to individuals, businesses and the day-to-day operation of the Australian economy. The disorderly failure of a significant financial institution could have severe impacts on the financial system and the community more broadly.

The Inquiry highlighted the need for regulators to have a range of resolution options which maximize the likelihood that an orderly resolution can be achieved.

While APRA currently has crisis management powers, the CFR agencies' review of these powers identified gaps and areas that could be strengthened. Gaps identified include: powers to address a distressed foreign bank branch in Australia; the ability to require restructuring of a regulated entity to facilitate resolution; and deficiencies in powers to resolve group distress. The Crisis Management Consultation Paper canvassed a large number of proposals to address these gaps, and to enhance the range and strength of tools available to APRA in situations of crisis.

Government intervention is required to implement these proposals in legislation so that APRA has effective powers to resolve a failing entity expeditiously in such a way as to protect the interests of depositors and policyholders, and to maintain financial system stability.

Question 3 and 4 – the policy options, and the costs and benefits of each option

The Murray Inquiry considered the following policy options, and discussed their costs and benefits, in relation to APRA's crisis management powers:

- *Strengthening regulators' resolution powers for financial institutions:* While many of the gaps identified are relatively minor in isolation, the cumulative effect of addressing them in full would enhance APRA's crisis management powers and more closely align Australia with international standards and best practice. It was noted that many of the proposed powers would have limited regulatory burden in normal times.
- *Investing more in pre-planning and pre-positioning for financial failure:* Pre-planning is necessary to support viable crisis management options and that it increases the consistency of Government approaches to crises. It was noted that pre-planning could be resource intensive for regulators and impose a burden on industry, but compared to other options, would likely be relatively low cost.
- *No change to current arrangements for either or both of the above options:* The Murray Inquiry noted that there are high costs associated with the disorderly failure of an institution, particularly where this creates financial system instability or the need for Government support. These costs would be exacerbated should the above policy options not proceed.

These options were included in the Murray Inquiry Interim Report released in July 2014.

Question 5 – who will be consulted and how?

The Murray Inquiry took initial submissions on the issues set out in its terms of reference and a second round of submissions in response to its Interim Report. In developing the Government's response to the Murray Inquiry, Treasury received submissions on the recommendations in the Final Report.

The Murray Inquiry was preceded by consultation on the FCS Consultation Paper (released in May 2011) which received 54 submissions from industry and other interested parties and the Crisis Management Consultation Paper (released in September 2012) which received 25 submissions from the industry and other interested parties.

Prior to the release of the exposure draft legislation, Treasury conducted targeted consultation with key industry representative bodies and law firms. During this period, Treasury also consulted with a number of financial institutions, including the major four banks. Following the release of the draft Bill for consultation on 18 August 2017, Treasury continued to engage with key industry stakeholders on the main issues.

Question 6 – what is the best option from those considered?

The Murray Inquiry recommended the completion of existing processes for strengthening crisis management powers (Recommendation 5). These processes included the implementation of the package of proposals in the Crisis Management Consultation Paper which built on the proposals in FCS Consultation Paper. The Inquiry strongly supported enhancing crisis management toolkits for regulators, emphasising the importance of putting in place arrangements to ensure regulators have comprehensive powers to manage crises and minimise negative spill-overs to the financial system, the broader economy and taxpayers.

On 20 October 2015, as part of its response to the Murray Inquiry, the Government agreed with the recommendation that regulatory settings should provide regulators with clear powers in the event a prudentially regulated financial entity fails. A more comprehensive toolkit of crisis management powers will enhance the tools available to APRA to manage and prepare for the effective resolution of a prudentially regulated entity that fails.

This Bill is primarily focused on the proposals from the Crisis Management Consultation Paper and the FCS Consultation Paper that relate to crisis management. This includes proposals that:

- enhance APRA's statutory and judicial management regimes to ensure their effectiveness in a crisis;
- enhance of the scope and efficacy of APRA's existing directions powers;
- improve APRA's ability to implement a transfer of business;
- ensure the effective conversion and write-off of capital instruments to which the conversion and write-off provisions in APRA's prudential standards apply;
- enhance stay provisions and ensure that the exercise of APRA's powers does not trigger certain rights in the contracts of entities within the same group;
- provide APRA with powers to resolve branches of foreign banks;
- enhance the efficiency and operation of the FCS and ensure that it supports the crisis resolution framework;
- strengthens APRA's ability to wind up an entity and monitor external administration processes; and
- provide APRA with clear resolution planning powers, to ensure banks and insurers are better prepared for a crisis.

This package of reforms will strengthen APRA's powers to facilitate the orderly resolution of an institution so as to protect the interests of depositors and policyholders, and to protect the stability of the financial system.

The other proposals in the Crisis Management Consultation Paper will be implemented at a later date.

The regulatory costing for this reform package has been prepared, consistent with the Government's Regulatory Burden Measurement Framework. These costs of the package are summarised in Table 1.

Table 1: Regulatory burden estimate (RBE) table

Average annual regulatory costs (from business as usual)				
Change in costs (\$million)	Business	Community organisations	Individuals	Total change in costs
Total, by sector	\$1.3	\$0	\$0	\$1.3

A regulatory offset has not been identified. However, Treasury is seeking to pursue net reductions in compliance costs and will work with affected stakeholders and across Government to identify regulatory burden reductions where appropriate.

Question 7 – how will you evaluate and implement your chosen option?

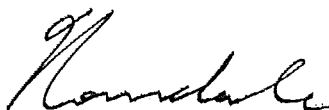
The Government will implement these reforms by introducing the Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017 to strengthen APRA's crisis management powers in the 2017 Spring Parliamentary Sitting Period.

The Bill will make amendments to legislation including the *Banking Act 1959*, *Insurance Act 1973*, *Life Insurance Act 1995*, *Australian Prudential Regulation Authority Act 1998*, *Payment Systems and Netting Act 1998*, *Financial Sector (Business Transfer and Group Restructure) Act 1999*, *Corporations Act 2001* and the *Income Tax Assessment 1997*.

The CFR will continue to review and test the effectiveness and efficiency of the crisis management powers every year. These crisis management powers will be independently assessed as part of the International Monetary Fund's Financial System Assessment Program in 2018. The CFR will also continue to monitor international developments in financial regulation and approaches to crisis resolution in other jurisdictions to ensure that APRA's crisis management powers keep pace with advancements resolution techniques.

Should the OBPR have any queries in relation to this matter please contact [REDACTED] on [REDACTED] or [REDACTED]

Yours sincerely



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Deputy Secretary
Markets Group