Chapter 1

Introduction

1.1 On 13 June 2017, the Senate referred the provisions of the Major Bank Levy Bill 2017 and the Treasury Laws Amendment (Major Bank Levy) Bill 2017 (the bills) to the Senate Economics Legislation Committee for inquiry and report by 19 June 2017.

Overview of the bills

1.2 The Major Bank Ley Bill 2017 (Major Bank Levy Bill) will introduce a levy on authorised deposit-taking institutions (ADIs) with total liabilities of greater than $100 billion. The levy is imposed at a rate of 0.015 per cent on certain liabilities of the ADI that are reported to the Australian Prudential Regulation Authority (APRA) on a quarterly basis under a reporting standard.[1]

1.3 The amount of liabilities on which the Major Bank Levy will be payable is the total reported liabilities of the ADI for the quarter, reduced by the sum of:

- the ADI's total Additional Tier 1 Capital at the end of the quarter;
- the ADI's total holdings of deposits protected by the Financial Claims Scheme at the end of the quarter;
- an amount equal to the lesser of the derivative assets and derivative liabilities at the end of the quarter in relation to the ADI; and
- the exchange settlement account balance held with the Reserve Bank of Australia (RBA) for the quarter in relation to the ADI.[2]

1.4 Schedule 1 to the Treasury Laws Amendment (Major Bank Levy) Bill 2017 (the Treasury Laws Amendment Bill) amends the *Australian Prudential Regulation Authority Act 1998* (APRA Act), the *Financial Sector (Collection of Data) Act 2001* (Collection of Data Act), the *Income Tax Assessment Act 1997* (ITAA 1997) and the *Taxation Administration Act 1953* (TAA 1953) to specify certain administrative features relating to the Major Bank Levy, including the requirement that the levy is payable to the Commissioner of Taxation (Commissioner) quarterly.[3] In particular, the amendments:

- modify the TAA 1953 to:
  - specify that the Major Bank Levy is payable to the Commissioner;
  - ensure that the ordinary collection and recovery provisions apply in relation to the levy;

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1 Explanatory Memorandum, p. 3.

2 Explanatory Memorandum, p. 6.

3 Explanatory Memorandum, p. 3.

- introduce an anti-avoidance law for the levy; and
- allow the Commissioner to give information relating to the levy to APRA;

- modify the ITAA 1997 so that the $100 billion threshold is indexed to grow in line with nominal Gross Domestic Product;
- modify the Collection of Data Act to allow APRA reporting standards to include information relating to reporting amounts for the purposes of the Major Bank Levy; and
- modify the APRA Act to allow APRA to provide information relating to the Major Bank Levy to the Commissioner.[4]

1.5 Subject to the passage of the bill, the Major Bank Levy is due to take effect from 1 July 2017.

Financial impact

1.6 The Major Bank Levy is expected to raise $6.2 billion between 2017-18 and 2020-21 (Table 1). The implications for the underlying cash balance are $5.5 billion over the same period.[5]

Table 1: Financial impact of the Major Bank Levy over the forward estimates

2016-17	*2017-18*	*2018-19*	*2019-20*	*2020-21*
—	$1 600m	$1 500m	$1 500m	$1 600m

Source: Explanatory Memorandum, p. 3.

Conduct of the inquiry

1.7 The committee advertised the inquiry on its website. It also wrote to relevant stakeholders and interested parties inviting submissions by 15 June 2017. The committee received 21 submissions, which are listed at Appendix 1.

1.8 The committee held a public hearing in Canberra on 16 June 2017. The witnesses who appeared at the hearing are listed at Appendix 2.

1.9 The committee appreciates the efforts of all stakeholders who contributed to the inquiry.

Background

1.10 In the 2017-18 Budget, the government announced that it would introduce a levy on major banks with assessable liabilities greater than $100 billion. The levy will contribute to budget repair over the forward estimates period and contribute to strengthening the structural position of the budget for the long term—providing

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4 Explanatory Memorandum, pp. 6-7.

5 Explanatory Memorandum, p. 3.

greater fiscal capacity to accommodate shocks such as those seen in the global financial crisis.[6]

1.11 Repairing the budget and maintaining the Australian Government's AAA credit rating will also benefit the largest banks, as their credit ratings, and hence funding costs, are more closely linked to the government's credit rating.[7]

1.12 In his second reading speech, the Treasurer emphasised that:

> Our banks must be unquestionably strong, but they must also be unquestionably accountable, unquestionably fair and our banking system must be unquestionably competitive.
>
> The government is also committed to ensuring that Australia's largest banks are held to account and make a fair additional contribution to the Australian community which they serve.[8]

1.13 The bank levy will have a number of other beneficial impacts for ongoing stability and competition settings, notably:

- ensuring a fair contribution from major banks to the economy given risks to the economy arising from large leveraged banks;
- providing a more level playing field for smaller banks and non-bank competitors; and
- complementing broader prudential reforms being implemented by APRA and the government.[9]

1.14 The levy will also bring Australia's taxation arrangements for ADIs into alignment with other advanced countries.[10]

A fair contribution from major banks to the community

1.15 Australia's major banks are among the most profitable in the advanced world. Rates of return on equity for the largest banks have averaged around 15 per cent over the past five years, far exceeding peers in the United States, Europe and Japan, and matched only by Canadian banks.[11]

1.16 In the last year alone, the five banks that will be affected by the levy—Australian and New Zealand Bank (ANZ), Commonwealth Bank of Australia (CBA),

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6 Explanatory Memorandum, p. 5.

7 Explanatory Memorandum, pp. 25-26.

8 The Hon. Scott Morrison (Treasurer), Major Bank Levy Bill 2017—Second Reading Speech, *House of Representatives Hansard*, 30 May 2017, p. 1.

9 Explanatory Memorandum, p. 26.

10 Explanatory Memorandum, p. 26.

11 Explanatory Memorandum, p. 26.

National Australia Bank (NAB), Westpac and Macquarie Bank—collectively earned more than $30 billion in profit after tax.[12]

1.17 The global financial crisis demonstrated that large, leveraged banks are a major source of systemic risk. If one or more of Australia's major banks became distressed or was seen to be at risk of failing, there could be the potential for significant contagion to other financial institutions.[13]

1.18 This would impose large costs on Australia's financial system and economy. The costs of borrowing would rise, with significant flow-on effects to mortgage holders, business and government finances. Credit supply could also be disrupted, starving the economy of the capital needed for it to grow and create jobs. In essence, the levy represents a fair additional contribution from the largest banks for the risks they pose to the financial system and economy.[14]

Provide a more level playing field for smaller banks and non-bank competitors

1.19 The major banks represent 80 per cent of the bank deposit market, 80 per cent of all credit provided by the banks and around three-quarters of the credit card market.[15]

1.20 A number of factors contribute to the ongoing dominance of major banks in the market for consumer and business lending. In his second reading speech, the Treasurer noted that:

> The House of Representatives Economics Committee's review of the four major banks, commissioned by the Prime Minister and myself last year, concluded that Australia's banking sector is an oligopoly and that Australia's largest banks have significant pricing power which they have used to the detriment of everyday Australians.[16]

1.21 Further, these banks have benefited:

> …[F]rom a regulatory system that has helped to embed their dominant position in the market. For example, the major banks are accredited to use internal ratings-based models that allow them to reduce the amount of capital that they must hold, lowering their funding costs relative to the smaller banks who rely on standardised risk weights.[17]

1.22 The imposition of the levy will reduce the largest banks' funding cost advantage and contribute to a more level playing field. This will enhance the ability of

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12 Explanatory Memorandum, p. 26.

13 Explanatory Memorandum, p. 26.

14 Explanatory Memorandum, p. 27.

15 Explanatory Memorandum, p. 27.

16 The Hon. Scott Morrison (Treasurer), Major Bank Levy Bill 2017— Second Reading Speech, *House of Representatives Hansard*, 30 May 2017, p. 2.

17 The Hon. Scott Morrison (Treasurer), Major Bank Levy Bill 2017— Second Reading Speech, *House of Representatives Hansard*, 30 May 2017, p. 1.

smaller banks and non-bank lenders to compete more aggressively with the largest banks.[18]

Complement prudential reforms to strengthen the financial system

1.23 The Major Bank Levy will complement prudential reforms being implemented by the government and APRA to improve financial system resilience. These reforms include:

- setting bank capital levels such that they are 'unquestionably strong';
- strengthening APRA's crisis management powers; and
- ensuring banks have appropriate loss absorbing capacity.[19]

1.24 The design of the levy complements the 'unquestionably strong' direction of prudential policy. The levy will not apply to common equity and Additional Tier 1 capital (capital instruments that can be converted to equity or be written off in the event of distress). According to APRA, the payment of the levy will not have a material impact on the resilience of the banking system and the levy regime does not harm APRA's prudential policy objectives.[20]

1.25 As the levy excludes deposits protected by the Financial Claims Scheme, it also creates an additional incentive for affected banks to move towards more stable, deposit-based funding. In doing so, it complements prudential measures aimed at making banks more resilient to market disruptions of the sort seen in the global financial crisis.[21]

The Major Bank Levy is comparable with bank levies in other jurisdictions

1.26 A number of foreign jurisdictions have introduced bank levies that are similar in design to the Major Bank Levy.[22] A summary of these levies is provided in Table 2.

1.27 These bank balance sheet levies commonly adopt a liabilities base rather than other options such as assets or regulatory capital. Consideration of their design, in particular that of the United Kingdom, has reinforced the value of adopting a broad base/low rate approach that limits exclusions from total liabilities in setting the base.[23]

1.28 Analysis following their introduction indicates that the incidence of bank levies being passed on to consumers (in the form of higher interest rates) is not universal and is likely to depend in part on country-specific factors. There is some evidence to suggest that bank levies can promote financial stability—levies introduced

18 Explanatory Memorandum, p. 27.

19 Explanatory Memorandum, pp. 5-6.

20 Explanatory Memorandum, pp. 27-28.

21 Explanatory Memorandum, p. 28.

22 Explanatory Memorandum, p. 37.

23 Explanatory Memorandum, p. 38.

in Europe have been found to have induced large increases in bank capital levels, due to the levies increasing the cost of wholesale funding relative to equity.[24]

Table 2: International Bank Levies

Jurisdiction (introduced)	***Levy base***	***Levy rate***	***Exemptions & threshold***
Australia (proposed 2017)	Liabilities	0.06% (annualised)	Deposits protected by the FCS, AT1 capital before deductions, derivatives Threshold: $100bn
Austria (2011)	Liabilities	<€20bn: 0.09% >€20bn: 0.11%	Insured deposits Threshold: €1bn
Belgium (2012)	Liabilities	0.13231% (2016)	Levied on 'debt towards clients'
France (2011)	Minimum regulatory capital	0.5%	Threshold: €500m
Germany (2011)	Liabilities Derivatives	Liabilities: >€300m: 0.02% progressively increasing to >€300bn: 0.06% Derivatives: 0.0003%	Retail deposits, certain reserves, certain profit participation rights Threshold: €300m Maximum: 20% of annual earnings Minimum: 5% of calculated annual contribution
Hungary (2010)	Assets	<HUF50bn: 0.15% >HUF50bn: 0.24%	Interbank loans
Iceland (2011)	Total liabilities	0.376%	Threshold: ISK50mn
Netherlands (2012)	Liabilities	Long-term: 0.022% Short-term: 0.044%	Protected deposits, regulatory capital, insurance liabilities Threshold: €20bn
Poland (2016)	Assets	0.44%	Equity capital and government securities Threshold: PLN4bn
Portugal (2011)	Liabilities	0.01-0.11%	Tier 1 and 2 capital, and protected deposits
Slovakia (2012)	Liabilities	0.2%	'Own funds' and subordinated debt
Sweden (2009)	Liabilities	0.09%	Protected deposits
United Kingdom (2011)	Liabilities	Long-term and equity: 0.09% (0.05% from 2021) Short-term: 0.18% (0.1% from 2021)	Protected deposits, Tier 1 capital, sovereign repos, other selected liabilities

Source: Explanatory Memorandum, pp. 37-38.

24 Explanatory Memorandum, p. 38.

Human rights implications and other considerations

Human rights implications

1.29 The bills do not engage any of the applicable rights or freedoms.[25]

Senate Standing Committee for the Scrutiny of Bills

1.30 The Senate Standing Committee for the Scrutiny of Bills (SSCSB) commented on both bills in the *Scrutiny Digest 6 of 2017*.

1.31 In relation to both bills, the SSCSB was concerned about provisions that allow the incorporation of external materials existing from time to time:

> At a general level, the committee will have scrutiny concerns where provisions in a bill allow the incorporation of legislative provisions by reference to other documents because such an approach:
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> - raises the prospect of changes being made to the law in the absence of parliamentary scrutiny, (for example, where an external document is incorporated as in force 'from time to time' this would mean that any future changes to that document would operate to change the law without any involvement from Parliament);
> - can create uncertainty in the law; and
> - means that those obliged to obey the law may have inadequate access to its terms (in particular, the committee will be concerned where relevant information, including standards, accounting principles or industry databases, is not publicly available or is available only if a fee is paid).
>
> As a matter of general principle, any member of the public should be able to freely and readily access the terms of the law. Therefore, the committee's consistent scrutiny view is that where material is incorporated by reference into the law it should be freely and readily available to all those who may be interested in the law.[26]

1.32 The SSCSB has requested that the Treasurer provide advice as to the type of documents that it is envisaged may be applied, adopted or incorporated by reference under subclauses 5(5), 6(5) and 8(2) of the Major Bank Levy Bill 2017 subsection 13(2C) of the Treasury Laws Amendment (Major Bank Levy) Bill 2017, whether these documents will be made freely available to all persons interested in the law and why it is necessary to apply the documents as in force or existing from time to time, rather than when the document is first made.[27]

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25 Explanatory Memorandum, p. 24.

26 Senate Standing Committee for the Scrutiny of Bills, *Scrutiny Digest 6 of 2017*, 14 June 2017, p. 46.

27 Senate Standing Committee for the Scrutiny of Bills, *Scrutiny Digest 6 of 2017*, 14 June 2017, pp. 46-47 and 71-72.

1.33 In relation to the Treasury Laws Amendment (Major Bank Levy) Bill 2017, the SSCSB was concerned about provisions that reverse the evidential burden of proof:

> Section 56(2) of the Australian Prudential Regulation Authority Act 1998 makes it an offence to disclose information acquired without authorisation. The offence carries a maximum penalty of imprisonment for 2 years. Proposed subsection 56(5D) provides an exception (offence specific defence) to this offence, stating that the offence does not apply if the production by a person of a document that was given to the Australian Prudential Regulation Authority (APRA) under section 13 of the Financial Sector (Collection of Data) Act 2001 is to the Commissioner of Taxation for the purposes of the Major Bank Levy Act 2017.
>
> Subsection 13.3(3) of the Criminal Code Act 1995 provides that a defendant who wishes to rely on any exception, exemption, excuse, qualification or justification bears an evidential burden in relation to that matter.
>
> At common law, it is ordinarily the duty of the prosecution to prove all elements of an offence. This is an important aspect of the right to be presumed innocent until proven guilty. Provisions that reverse the burden of proof and require a defendant to disprove, or raise evidence to disprove, one or more elements of an offence, interferes with this common law right.[28]

1.34 The SSCSB has requested that the Treasurer provide advice as to why it is proposed to use an offence-specific defence (which reverses the evidential burden of proof) in this instance.[29]

28 Senate Standing Committee for the Scrutiny of Bills, *Scrutiny Digest 6 of 2017*, 14 June 2017, pp. 70-71.

29 Senate Standing Committee for the Scrutiny of Bills, *Scrutiny Digest 6 of 2017*, 14 June 2017, p. 71.