



Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010

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Law and Bills Digest Section

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Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010

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House: House of Representatives

Portfolio: Treasury

Commencement: Sections 1–3: on Royal Assent; Schedule 4 (item 4): on the day after Royal Assent; Schedule 1 (items 1–25; 27–46), Schedule 2 (items 1–83; 85–93), Schedule 3 (items 1–51; 53–63), Schedule 4 (items 1-3; 5–25; 27–36), Schedule 6 (items 1–64; 66–78) and Schedule 7: on the 28th day after Royal Assent; Schedule 5: on 1 July 2010; Schedule 1 (item 26), Schedule 2 (item 84), Schedule 3 (item 52), Schedule 4 (item 26), Schedule 6 (item 65): for various commencement arrangements, please refer to table at **item 2** in the Bill

Links: The [links](#) to the Bill, its Explanatory Memorandum and second reading speech can be found on the Bills page, which is at <http://www.aph.gov.au/bills/>. When Bills have been passed they can be found at ComLaw, which is at <http://www.comlaw.gov.au/>.

Purpose

The Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010 (the Bill) proposes to amend various Acts to strengthen Australia's crisis management and prudential framework.¹ These Acts include:

- *Australian Prudential Regulation Authority Act 1998* (APRA Act)
- *Banking Act 1959* (Banking Act)
- *Insurance Act 1973* (Insurance Act)
- *Life Insurance Act 1975* (Life Insurance Act)
- *Retirement Savings Account Act 1997* (RSA Act)
- *Superannuation Industry (Supervision) Act 1993* (Superannuation Supervision Act), and
- *Financial Sector (Collection of Data) Act 2001* (FSCODA Act).

1. Explanatory Memorandum, Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010, p. 1.

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In addition, the Bill proposes to amend other legislation to make changes to the levy system, most of which were recommended in the 2009 *Report of the Review of Financial Sector Levies* (see below).² These Acts include:

- *Financial Institutions Supervisory Levies Collection Act 1998* (FI Levies Collection Act)
- *Authorised Deposit-taking Institutions Supervisory Levy Imposition Act 1998* (ADI Levy Imposition Act)
- *General Insurance Supervisory Levy Imposition Act 1998* (GI Levy Imposition Act)
- *Life Insurance Supervisory Levy Imposition Act 1998* (LI Levy Imposition Act)
- *First Home Saver Account Providers Supervisory Levy Imposition Act 2008* (FHSA Levy Imposition Act)
- *Retirement Savings Account Providers Supervisory Levy Imposition Act 1998* (RSA Levy Imposition Act), and
- *Superannuation Supervisory Levy Imposition Act 1998* (Superannuation Levy Imposition Act).

Background

APRA and prudential regulation

What is APRA's role

The Australian Prudential Regulation Authority (APRA) is a Commonwealth statutory authority established in 1998 under the APRA Act and which operates under various Commonwealth Acts including those mentioned above.

APRA is the prudential regulator of the Australian financial services industry, which includes banks, credit unions, building societies, general and life insurance companies, reinsurance companies and most members of the superannuation industry.³

APRA's prudential regulation role involves the following:

- establishing prudential standards
- assessing new licence applications

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2. Ibid. For further information about the financial sector levy system, see Treasury and APRA, *Proposed financial sector levies for 2009-2010*, Consultation paper, June 2009, viewed 10 June 2010, http://www.treasury.gov.au/documents/1560/PDF/consultation_paper.pdf
 3. APRA, *About APRA*, viewed 31 May 2010, <http://www.apra.gov.au/aboutApra/>

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- assessing financial integrity of supervised institutions
- carrying out remediation, crisis response and enforcement where necessary.⁴

All deposit-taking institutions (ADIs); friendly societies; general insurance, reinsurance and life insurance companies; as well as trustees of prudentially regulated superannuation funds must be licensed to operate in Australia.⁵ Once licensed, an institution is subject to ongoing supervision by APRA, in which APRA follows a risk-based approach, where licensees with greater risks are supervised more closely.⁶

APRA's prudential standards set out minimum capital and risk-management requirements, which licensees must follow in order to maintain their licence.

Where institutions are unable or unwilling to comply with their prudential requirements, APRA is able to take remediation or enforcement action. This includes conducting investigations of and giving directions to the non-complying institutions.⁷ In certain cases, APRA may also apply to the Federal Court of Australia to disqualify a person working in the supervised institution from working in the relevant industry; appoint a statutory manager; replace a trustee or apply to the Court to appoint a judicial manager to take control of the non-complying institution.⁸

For more comprehensive information about APRA's supervisory role, see its [Supervision Blueprint](#), released in January 2010.⁹

APRA also collects information for its own purposes and acts as the national statistical agency for the financial sector.¹⁰

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4. APRA, *Australian Prudential Regulation Authority: protecting Australia's depositors, insurance policy holders and superannuation fund members*, viewed 31 May 2010, <http://www.apra.gov.au/AboutAPRA/upload/APRA-Brochure-FINAL-08Jan2010.pdf>
 5. See *ibid.*, p. 8.
 6. See *ibid.*, p. 7.
 7. See *ibid.*, p. 10.
 8. *Ibid.* The term 'ADI statutory manager' is explained in subsection 13A(2) of the Banking Act as 'the entity in control of an ADI's business under this Subdivision [Subdivision A]. That entity will be either APRA or an administrator of an ADI's business appointed by APRA'. The term 'judicial manager' is a manager appointed by the Federal Court of Australia under section 62R of the Insurance Act: section 3 of the Insurance Act. The powers of a judicial manager are set out in sections 62Y and 62Z of the Insurance Act.
 9. APRA, *APRA's Supervision Blueprint*, January 2010, viewed 31 May 2010, <http://www.apra.gov.au/AboutAPRA/upload/APRA-Supervision-Blueprint-FINAL-08Jan2010.pdf>
 10. APRA, *Australian Prudential Regulation Authority: protecting Australia's depositors, insurance policy holders and superannuation fund members*, *op. cit.*, p. 4. For further information about APRA's data collecting role, see Explanatory Memorandum, *op. cit.*, p. 77.

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Finally, APRA administers the Financial Claims Scheme (FCS) established in 2008. The aim of the FCS is to protect certain policy holders and claimants who make valid claims against a general insurer where that insurer is insolvent.¹¹

Who pays for APRA's supervision

APRA's prudential supervision is, in part, funded by industry levies determined by the Federal Government each year.¹² The levies also cover certain functions of the Australian Securities and Investments Commission (ASIC) and the Australian Tax Office (ATO) in relation to institutions regulated by APRA.¹³

A review of the methodologies used in determining financial sector levies was conducted by Treasury and APRA in 2008 and 2009, with a report published in June 2009 (the Levies Review Report).¹⁴ Recommendations made in the Levies Review Report included the following:

That the levy date for new starters should be redefined and a new starter return be introduced.

That the imposition legislation be amended to provide more flexibility so that a valuation basis other than assets can be used on a case by case basis in the annual determinations.¹⁵

Committee consideration

On 1 June 2010, the Senate Standing Committee for Economics—Legislation Committee stated that it had considered provisions in the Bill and determined that there were no substantive matters requiring examination.¹⁶

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11. For further information about the FCS, see APRA, *Financial Claims Scheme: questions and answers*, viewed 31 May 2010, <http://www.apra.gov.au/upload/FINANCIAL-CLAIMS-SCHEME-Q-and-A-for-APRA-website-for-GIs-UPDATED-22Apr10.pdf>
 12. Explanatory Memorandum, op. cit., p. 89.
 13. Ibid.
 14. Treasury and APRA, *Report of the review of financial sector levies*, June 2009, viewed 31 May 2010, http://www.treasury.gov.au/documents/1708/PDF/Review_of_Financial_Sector_Levies.pdf
 15. Ibid., pp. 2–3.
 16. Senate Standing Committee for Economics, *Consideration of time critical Bills*, 1 June 2010, viewed 7 June 2010, http://www.aph.gov.au/senate/committee/economics_ctte/timecritical_bills/report/report.pdf

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Position of significant interest groups

Treasury released an exposure draft of the Bill on 19 January 2010 for comment,¹⁷ to which various stakeholders submitted comments.¹⁸

In general, stakeholders supported the proposed amendments in the exposure draft.¹⁹

However, it is noted that the Self-Managed Super Funds Professionals Association of Australia (SPAA) expressed concern about the proposed amendments to proposed section 130BB of the exposure draft. In brief, SPAA stated that:

SPAA is concerned about the severity of the penalty that could be imposed on SMSF trustees under this section.

There is no distinction made between the trustees of large funds and the trustees of an SMSF. The former are managing the superannuation affairs of a large number of unrelated members, whereas SMSF trustees are managing affairs for themselves and their immediate family group. Therefore the consequences of a breach under section 130BB are arguably much less severe in the case of a SMSF when compared to a larger fund.

...

In short, SPAA finds it difficult to foresee a situation where the actions of a SMSF trustee under section 130BB may warrant 5 years imprisonment. SPAA therefore

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17. See C Bowen MP (Minister for Financial Services, Superannuation and Corporate Law and Minister for Human Services), 'Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010', *media release*, 19 January 2010, viewed 31 May 2010, <http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2010/005.htm&pageID=003&min=ceba&Year=&DocType=>
 18. See Treasury, *Submissions: exposure draft Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010 and explanatory material*, viewed 31 May 2010, <http://www.treasury.gov.au/contentitem.asp?ContentID=1761&NavID=037>
 19. See, for example, Australian Financial Markets Association (AFMA), *Consultation on exposure draft Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010*, 16 March 2010, p. 2, viewed 31 May 2010, <http://www.treasury.gov.au/documents/1761/PDF/AFMA.pdf>; Insurance Council of Australia, *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010*, 16 March 2010, pp. 1–2, viewed 31 May 2010, http://www.treasury.gov.au/documents/1761/PDF/Insurance_Council_of_Australia.pdf

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considers that a less onerous penalty regime should apply under this section to SMSF trustees.²⁰

The Association of Superannuation Funds of Australia (ASFA) also expressed some concern about proposed section 130BB of the exposure draft. It stated:

ASFA has two concerns with proposed section 130BB:

- The narrow class of persons that can be penalised, and
- The broadness of the term ‘reasonable steps’.

...

The offence of knowingly providing false or misleading information to an auditor is restricted to the trustee, a responsible officer of a trustee or an employee of the trustee of a superannuation entity. ASFA’s concern is that parties beyond those listed may, without risk of penalty, provide false or misleading information to a listed person for the sole purpose of covering up a breach by that other person. The person involved may be, for example, the accountant, administrator or other service provider to a superannuation fund. ASFA would argue that, unless the offence is widened to capture a broader range of persons, an auditor may be required to report interference under new section 130BA by a person in respect of whom the Regulator would be powerless to take action under section 130BB.

To avoid penalty under proposed subsection 130BB(2), the relevant person is required to demonstrate that they took ‘reasonable steps’ to ensure that information provided to the auditor was not false or misleading in a material particular or missing something that makes the information misleading in a material respect.

ASFA’s concern is that the legislation uses the term ‘reasonable steps’ while the explanatory material and the heading to the provision uses the term recklessness. ASFA is concerned that a person who considers that they have taken reasonable steps in ensuring the accuracy of the information provided could, in the regulator’s opinion, be found to not have taken reasonable steps.²¹

20. SPAA, *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010*, 16 March 2010, p. 2, viewed 31 May 2010, http://www.treasury.gov.au/documents/1761/PDF/SMSF_Professionals_Association_of_Australia_Limited.pdf

SMSF refers to self-managed super funds.

21. AFSA, *Exposure draft Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Bill 2010 and explanatory material*, 12 March 2010, p. 5, viewed 31 May 2010, <http://www.treasury.gov.au/documents/1761/PDF/ASFA.pdf>

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It is noted that proposed section 130BB of the Exposure Draft has been included in **item 35 of Schedule 4** of the Bill in the same form.²²

No stakeholder comments have been found in relation to the proposed amendments in the Bill itself.

Financial implications

The Government states that the proposed measures in the Bill would have no significant financial impact.²³

Main provisions

Due to the short timeframe between when the Bill was introduced and when it was to be debated; as well as the comprehensive information set out in the Explanatory Memorandum, this Digest will only deal with some of the proposed amendments.

Schedule 1—amendments to the Banking Act

APRA's preventive powers

Some amendments in **Schedule 1** aim to enhance APRA's powers to prevent prudential concerns arising in relation to ADIs.²⁴

One such amendment is set out in **items 5 and 8 of Schedule 1**, which propose to insert **new subsections 9(2A) and 11AA(1A)** into the Banking Act.

Section 9 currently relates to authority to carry on a banking business in Australia. Section 11AA currently relates to authority to be a non-operating holding company (an NOHC) of an ADI.²⁵

Proposed subsections 9(2A) and 11AA(1A) provide that APRA may set criteria for the granting of such authority by legislative instrument.

The Explanatory Memorandum states:

22. For further information about offences relating to auditors in the Bill, see pp. 11–13 of this Digest.

23. Explanatory Memorandum, op. cit., pp. 2–8.

24. For the meaning of 'authorised deposit taking institution' (ADI), see section 5 of the Banking Act.

25. For the meaning of 'non-operating holding company' (NOHC), see section 5 of the Banking Act.

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The amendment enhances the authorisation framework by permitting minimum standards for entry and participation in regulated financial markets to be made by legislative instrument. Currently, such criteria are set out in APRA guidelines.²⁶

Similar amendments are proposed in **Schedule 2 items 9 and 12** (inserting **proposed subsections 12(1B) and 18(2A)** into the Insurance Act) and **Schedule 3 items 2 and 4** (inserting **proposed subsections 20(2A) and 28A(2A)** into the Life Insurance Act).

Other proposed amendments relating to APRA's preventive powers are set out in **items 7 and 9 of Schedule 1**, which propose to insert **new subsections 9A(5A) and 11AB(5A)** respectively into the Banking Act.

The Banking Act currently provides APRA with power to revoke authorisations to carry on banking business in certain circumstances. However, the Banking Act does not enable APRA to continue an authorisation in effect upon revocation of that authorisation. An authorisation continuing in effect means that following a revocation of an authorisation, the authorisation is said to continue in relation to a specified matter or for a specified period of time as though the revocation of the authorisation had not occurred. This is said to have implications on APRA's ability to 'monitor an entity, or act under relevant laws, after the entity's authorisation has been revoked'.²⁷

Proposed subsections 9A(5A) and 11AB(5A) provide that the notice of revocation of an authority may state that the authority continues in effect in relation to a specified matter or period of time, as if the revocation did not happen for certain purposes. These purposes are:

- a specified provision of the Banking Act or regulations
- a specified provision of another Commonwealth law that APRA administers, or
- a specified provision of the prudential standards.

Similar amendments are proposed in **Schedule 2 items 11 and 13** (inserting **proposed sections 16A and 22A** into the Insurance Act) and **Schedule 3 items 3 and 5** (inserting **proposed sections 28 and 28E** into the Life Insurance Act).

It is noted that an existing equivalent provision is section 29GB of the Superannuation Supervision Act, which enables APRA to allow a Registrable Superannuation Entity (RSE) licence to continue in effect.²⁸

26. Explanatory Memorandum, op. cit., p. 15.

27. See *ibid.*, p. 12.

28. An RSE licence is one granted under section 29D of the Superannuation Supervision Act.

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Auditors and actuaries

Appointment of auditors and conduct of audits

Under the Banking, Insurance and Life Insurance Acts, there are various provisions relating to the appointment of auditors and conduct of audits, which vary across those Acts. Consequently, the Bill contains provisions aimed at harmonising these laws.

For example, **item 10 of Schedule 1** proposes to insert **new subsection 11AF(1AB)** into the Banking Act.

Section 11AF currently relates to APRA's powers to make prudential standards for ADIs and authorised NOHCs.

Proposed subsection 11AF(1AB) provides that such a standard may provide for matters relating to the appointment of auditors or the conduct of audits.

According to the Explanatory Memorandum, '[t]his clarifies the existing law'.²⁹

Similar amendments are proposed in **Schedule 2 item 18** (see **proposed new paragraph 32(3)(b)** - Insurance Act) and **Schedule 3 item 49** (inserting **proposed subsection 230A(1A)** into the Life Insurance Act).

Item 36 of Schedule 1 proposes to insert **new section 16AV** into the Banking Act.

Proposed section 16AV provides that if the prudential standards require an auditor to be appointed, the appointed auditor must perform the functions and duties of an auditor as set out in those standards.³⁰ Not only must the appointed auditor comply with those standards in performing such functions and duties, but the relevant ADI or authorised NOHC must make any necessary arrangements to enable the appointed auditor to perform those functions and duties.

Similar provisions in relation to compliance with prudential standards and making necessary arrangements to enable the auditor to perform functions and duties are proposed in **Schedule 3 item 11** (inserting **proposed sections 83** and **83B** into the Life Insurance Act).

Offences relating to interfering with auditors

Currently, there is nothing in the relevant financial sector legislation, being amended in the Bill, which prohibits misleading or otherwise interfering with an auditor in carrying out

29. Explanatory Memorandum, op. cit., p. 57.

30. An 'appointed auditor' is one appointed in accordance with prudential standards: see **Schedule 1 item 2** of the Bill.

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his or her functions. Yet, section 1309 of the *Corporations Act 2001* (the Corporations Act) makes it an offence for an officer or employee of a corporation to knowingly mislead an auditor of the corporation.

There is also no prohibition in such financial sector legislation requiring an auditor to advise APRA or the ATO that someone has tried to interfere with the auditor carrying out his or her duties. Again, section 311 of the Corporations Act provides for this.

As the Explanatory Memorandum states:

The present offences in the Corporations Act apply when auditors are undertaking functions or exercising duties under the Corporations Act, but not when undertaking similar functions or exercising similar duties under the prudential Acts.³¹

Item 38 of Schedule 1 proposes to insert **new sections 16D** and **16E** into the Banking Act.

Proposed section 16E makes it an offence for an employee or officer of an ADI or authorised NOHC to knowingly give, or allow to be given, false or misleading information to an auditor of the entity. The penalty imposed is five years imprisonment and/or 200 penalty units.³²

Under **proposed section 16E**, it is also an offence for an employee or officer of an ADI or authorised NOHC to give, or allow to be given, such false or misleading information to an auditor of the entity without taking reasonable steps to ensure that the information is not false or misleading. The penalty imposed is two years imprisonment and/or 100 penalty units.

Proposed section 16D provides that if an appointed auditor of an ADI or authorised NOHC is aware of circumstances amounting to the following:

- someone has tried to unduly influence, coerce, manipulate or mislead the appointed auditor in connection with the performance of that auditor's functions or duties, or
- someone has tried to otherwise interfere with the performance of that auditor's functions or duties,

the appointed auditor must notify APRA of those circumstances as soon as practicable, and no later than 28 days, after he or she becomes aware of those circumstances.

31. Explanatory Memorandum, op. cit., p. 54.

32. One penalty unit is equal to \$110: *Crimes Act 1914* section 4AA. In certain circumstances, additional pecuniary penalties — up to five times the amount of maximum pecuniary penalty imposed on a natural person convicted of the same offence — may be imposed on corporations: see *ibid.*, subsection 4B(3).

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Failure to do so is an offence punishable by 12 months imprisonment and/or 50 penalty units.

Similar amendments are proposed in **Schedule 2 item 35** (inserting **proposed sections 49D** and **49DA** into the Insurance Act); **Schedule 3 item 29** (inserting **proposed sections 90** and **91** into the Life Insurance Act); and **Schedule 4 items 20** (inserting **new Division 2A** into the FSCODA Act), **29** (inserting **proposed sections 69** and **70** into the RSA Act) and **35** (inserting **proposed sections 130BA** and **130BB** into the Superannuation Supervision Act).

APRA's corrective powers

As mentioned above, APRA has a range of enforcement powers and sanctions to respond proportionately to compliance concerns. Where APRA is unable to resolve prudential concerns by working cooperatively with the Board and management of a supervised entity, it becomes necessary for APRA to use more direct methods of enforcing compliance.

Issuing directions is one such method. The ability to issue directions enables APRA to specify how an institution should resolve compliance issues and to compel the institution to take specific action to address identified prudential risks.³³ The Banking, Insurance and Life Insurance Acts enable APRA to issue directions to regulated institutions if certain conditions are satisfied. The Bill proposes to amend such conditions.

Item 13 of Schedule 1 proposes to amend **paragraph 11CA(1)(h)** in the Banking Act.

Existing paragraph 11CA(1)(h) provides that APRA may issue directions to an ADI or an authorised NOHC if APRA has reason to believe that there has been or might be a sudden material deterioration in the body corporate's financial condition.

Proposed paragraph 11CA(1)(h) provides that APRA may issue directions to an ADI or an authorised NOHC if APRA has reason to believe that there has been or might be a material deterioration in the body corporate's financial condition, omitting the word 'sudden'.

The Explanatory Memorandum states:

This reflects that it is not the speed but the extent of the deterioration that should be relevant in determining whether the trigger is met.³⁴

Similar amendments are proposed in **Schedule 2 item 86** (amending **paragraph 104(1)(g)** of the Insurance Act) and **Schedule 3 item 54** (amending **paragraph 230B(1)(g)** of the Life Insurance Act).

33. Explanatory Memorandum, op. cit., p. 21.

34. Ibid., p. 23.

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Under existing subsections 11CA(1) and (2) of the Banking Act, APRA can direct a regulated entity to do, or cause a subsidiary to do, certain things if certain conditions are met, but the conditions themselves (subsection 11CA(1)) do not refer to subsidiaries.

Item 14 of Schedule 1 proposes to insert **new subsection 11CA(1AA)** into the Banking Act, which would enable APRA to issue directions to an ADI or authorised NOHC if particular conditions are met.

First, APRA must consider that the direction is reasonably necessary for one or more prudential matters relating to the ADI or authorised NOHC.

Second, APRA must have reason to believe that, in relation to the ADI or authorised NOHC:

- a subsidiary is or about to become unable to meet its liabilities
- there has been or might be a material risk to the security of a subsidiary's assets
- there has been or might be a material deterioration in a subsidiary's financial condition
- a subsidiary is conducting its affairs in an improper or financially unsound manner, or
- a subsidiary is conducting its affairs in a way that may cause or promote instability in the Australian financial system.

The Explanatory Memorandum states:

The amendment reflects that the conduct or circumstances of a subsidiary of a regulated body may in some instances affect prudential matters relating to the regulated body.³⁵

Similar amendments are proposed in **Schedule 2 item 87** (inserting **proposed subsection 104(1A)** into the Insurance Act) and **Schedule 3 item 55** (inserting **proposed subsection 230B(1AA)** into the Life Insurance Act).

Item 17 of Schedule 1 proposes to insert **new subsection 11CA(2B)** into the Banking Act relating to directions that APRA may issue to foreign ADIs regarding assets and liabilities.

Proposed subsection 11CA(2B) provides that APRA may direct a foreign ADI:

- to act in a way that:
 - a particular asset or class thereof of the ADI be returned to the control of the part of the ADI's banking business that is carried out in Australia, or
 - a particular liability or class thereof of the ADI cease to be the responsibility of the part of the ADI's banking business that is carried out in Australia, or

35. Ibid., p. 25.

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- to not act in a way that:
 - a particular asset or class thereof of the ADI ceases to be under the control of the part of the ADI’s banking business that is carried out in Australia, or
 - a particular liability or class thereof of the ADI becomes the responsibility of the part of the ADI’s banking business that is carried out in Australia.

The Explanatory Memorandum states:

The amendment clarifies that APRA may issue a direction to prevent inappropriate intra-entity transactions that may undermine the financial position of the ADI’s Australian operations. This may be particularly important in a situation where the foreign ADI is in financial distress and to ensure that liability holders in Australia are not disadvantaged in the winding up or other resolution of the ADI.³⁶

APRA’s investigation powers

Powers to investigate

APRA has power to investigate or appoint someone to investigate APRA regulated entities and the ATO has similar powers in relation to superannuation entities that the ATO regulates.³⁷

However, it is stated in the Explanatory Memorandum that:

... there is uncertainty as to whether APRA and the ATO may commence or continue an investigation once such an entity enters external administration or, in the case of a superannuation entity, the entity is wound up, dissolved or terminated or the trustee becomes externally-administered or insolvent under administration.

This uncertainty is undesirable. Investigation powers are important for gathering information and evidence for the purposes of administering and enforcing relevant laws.³⁸

The proposed amendments in the Bill seek to address this uncertainty.

Investigation during winding up

Items 19, 24, 43 and 44 of Schedule 1 propose to insert **new subsections 13(6), 13A(7), 61(7) and 62(3)** respectively into the Banking Act.

36. Ibid., p. 26.

37. See, for example, subsection 13(4), sections 13A and 61 of the Banking Act; sections 52 and 62A of the Insurance Act; Part 7 Division 3 of the Life Insurance Act; Part 25 Divisions 3 and 4 of the Superannuation Supervision Act.

38. Explanatory Memorandum, op. cit., p. 27.

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Section 13 enables APRA to obtain certain information from an ADI. **Proposed subsection 13(6)** generally makes it clear that section 13 applies to an ADI which is or becomes an externally-administered body corporate, in the same way as it applies to any other ADI.

Proposed subsections 13A(7), 61(7) and 62(3) would have a similar effect in relation to their respective sections. Section 13A enables APRA to investigate or appoint someone to investigate an ADI that is failing, or likely to fail, to meet its obligations or suspend payments. Section 61 enables APRA to investigate various ADIs and NOHCs (or subsidiaries thereof) in particular circumstances. Section 62 relates to APRA's ability to obtain information from ADIs and authorised NOHCs (or subsidiaries thereof) in particular circumstances.

The Explanatory Memorandum states:

The amendments clarify that APRA may commence or continue an investigation after an ADI ... enters external administration ...³⁹

Similar amendments are proposed in **Schedule 2 item 46** (inserting **proposed subsection 52(6)** into the Insurance Act) and **Schedule 3 item 40** (inserting **proposed subsection 137(3)** into the Life Insurance Act). See also **Schedule 4 item 36** (inserting **proposed subsection 263(3)** into the Superannuation Supervision Act).

Requirements to provide information etc

Item 40 of Schedule 1 proposes to insert **new section 22A** into the Banking Act.

Proposed subsection 22A(1) provides that, in any proceeding under or arising out of the Banking Act, a person may not refuse or fail to comply with any of the following requirements to:

- answer a question or give information
- produce books, accounts or other documents, or
- do any other act,

on the grounds that by doing so, there might be a chance that he or she be disqualified. This is irrespective of whether the person is a defendant in or a party to the proceeding or any other proceeding (**proposed subsection 22A(2)**).

Proposed subsection 22A(3) provides similarly in relation to statutory requirements under the Banking Act to:

- answer a question or give information

39. Ibid., p. 31.

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- produce books, accounts or other documents, or
- do any other act.

This is irrespective of whether any legal proceeding is on foot.

As the Explanatory Memorandum explains:

The relevant Acts presently contain various provisions relating to the admissibility of information or documents obtained from a person under them as evidence against that person in a criminal proceeding or a proceeding for the imposition of a penalty. The Bill provides that these provisions do not apply to a proceeding for the imposition of a penalty by way of disqualification under the respective Acts. This prevents any inconsistency arising between those present provisions and the new provisions inserted by the Bill.⁴⁰

Similar amendments are proposed in **Schedule 2 item 14** (inserting **proposed section 26A** into the Insurance Act), **Schedule 3 item 58** (inserting **proposed section 245C** into the Life Insurance Act) and **Schedule 4 items 28** (inserting **proposed section 67AA** into the RSA Act) and **34** (inserting **proposed section 126L** into the Superannuation Supervision Act).

Record-keeping requirements

The Banking Act currently has no provisions on record keeping by regulated entities.

While the Insurance, Life Insurance and Superannuation Supervision Acts do have such provisions, they are said to be:

... not consistent with respect to their accessibility by APRA. It is important that APRA can efficiently access records kept by financial institutions where required to further the administration of prudential laws.⁴¹

Consequently, the Bill proposes amendments to those Acts to make record-keeping provisions consistent across the Acts.

For example, **item 42 of Schedule 1** proposes to insert **new section 60** into the Banking Act, related to keeping financial records.

Proposed section 60 generally requires any financial records kept under the Corporations Act, to be kept in Australia or in another country as approved by APRA (approval may be subject to certain conditions). In addition, records must be in English or in a form in which they are readily accessible and easily convertible into writing in English (**proposed**

40. Ibid., p. 32.

41. Ibid., p. 28.

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subsections 60(1) and (2)). Failure to do so is an offence punishable by a penalty of 200 penalty units (**proposed subsection 60(6)**).⁴²

An ADI must notify APRA of the address where the financial records are kept, including any new address if the records have been moved, within a particular period of time (**proposed subsections 60(3)–(5)**).

Finally, both APRA's decision to refuse to give approval for records to be kept in another country and APRA's decision to approve the keeping of records in another country subject to conditions are reviewable under Part VI of the Banking Act (Reconsideration and review of decisions). This means that, under section 51B of the Banking Act, a person who is affected by and is disappointed with the decision may request that APRA reconsiders that decision, accompanied by reasons for the request, within a particular period of time. APRA must then reconsider the decision and may confirm, vary or revoke it. In addition, under section 51C of the Banking Act, an application may be made to the Administrative Appeals Tribunal (the AAT) for a review of APRA's decision to confirm or vary the initial decision.

Similar amendments are proposed in **Schedule 2 items 40 and 41** (amending **subsection 49Q(1)** and inserting **proposed subsections 49Q(1A)–(1D)** in the Insurance Act); **Schedule 3 items 9 and 57** (inserting **proposed section 76A** and **proposed paragraphs 236(1)(o)–(p)** into the Life Insurance Act) and **Schedule 4 items 30–32** (inserting **proposed paragraphs 10(1)(dp)–(dq)**, substituting **paragraph 35A(2)(b)** and inserting **proposed subsections 35A(2A)–(2D)** in the Superannuation Supervision Act).⁴³

APRA's failure management powers

Recognising that some regulated financial institutions do become at risk of experiencing financial difficulties that threaten their ongoing viability, APRA has powers to intervene in such circumstances so as to protect depositors and policyholders, as well as maintain the stability of Australia's financial system.⁴⁴

External administration powers

For example, **items 20 and 21 of Schedule 1** propose to amend **section 13A** in the Banking Act relating to the consequences of an ADI being unable or failing to meet its obligations. The proposed amendment means that APRA may investigate an ADI's affairs; or take control of an ADI's business or appoint an administrator to do so, if APRA considers that in the absence of external support:

42. See note 32.

43. For further discussion about **Schedule 3 item 57**, see pp. 28–29 of this Digest.

44. See Explanatory Memorandum, *op. cit.*, p. 35.

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- it is likely that the ADI will be unable to carry on its banking business in Australia consistently with the interests of its depositors, or
 - it is likely that the ADI will be unable to carry on its banking business in Australia consistently with the stability of the financial system in Australia,
- among other factors.

Unlike the existing provision, the proposed amendments would allow the appointment of a statutory manager when either one or both of those conditions are met.

The Explanatory Memorandum states:

This amendment reflects that the interests of depositors and the stability of the financial system are separable concepts, and that there may be circumstances where an ADI is conducting its banking business in a manner that is not in the interests of its depositors, but where this does not necessarily adversely affect the stability of the financial system. The reverse could also be the case. There is a need for APRA to be able to appoint a statutory manager in either of these situations in order to ensure prompt remedial measures are taken to address the situation.⁴⁵

Winding up and priority provisions

Item 22 of Schedule 1 proposes to amend **paragraphs 13A(3)(c) and (d)** in the Banking Act by inserting **new paragraphs 13A(3)(c)–(f)**.

Existing subsection 13A(3) provides that if an ADI becomes unable to meet its obligations or suspends payment, its assets in Australia must be made available to meet its liabilities in a particular order. However, priority is not specifically given to debts owed to the Reserve Bank of Australia (the RBA) or under industry support contracts.⁴⁶

Proposed paragraphs 13A(3)(c)–(f) addresses this gap by providing that, after two other higher priorities, if an ADI becomes unable to meet its obligations or suspends payment, its assets in Australia must be made available to meet (in descending order of priority):

- any of the ADI's liabilities in Australia in relation to protected accounts that account-holders keep with the ADI
- any of the ADI's debts to the RBA
- any of the ADI's liabilities under an industry support contract certified under section 11CB, and
- any of the ADI's other liabilities.

45. Ibid., p. 41.

46. As to the meaning of 'industry support contract', see section 5 of the Banking Act.

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Recapitalisation powers

Item 25 of Schedule 1 proposes to insert **new Subdivision AA (Recapitalisation directions by APRA)** into Division 2 (Protection of depositors) of Part II of the Banking Act. **New subdivision AA** contains **proposed sections 13D–13R**. The proposed new provisions are aimed at clarifying that APRA can direct an ADI, who is without a statutory manager, to recapitalise provided that certain conditions are met.

Proposed subsection 13E(1) provides that such conditions are:

- the ADI informing APRA that it considers that it is likely to become unable to meet obligations or is about to suspend payment, or
- APRA considers that in the absence of external support, the ADI:
 - may become unable to meet its obligations
 - may suspend payment
 - is likely to be unable to carry on its banking business in Australia consistent with the interests of its depositors
 - is likely to be unable to carry on its banking business in Australia consistent with the stability of Australia’s financial system, or
- the ADI becomes unable to meet its obligations or it suspends payment.

Proposed subsection 13E(2) provides that in deciding whether to give such a direction, APRA must consult with the Australian Competition and Consumer Commission (ACCC) unless otherwise notified by the ACCC.

Under **proposed subsection 13E(4)**, a recapitalisation direction is not a legislative instrument. According to the Explanatory Memorandum, this is because:

The provision is included to assist readers, as the instrument is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*.⁴⁷

Proposed section 13F, in general, provides that a recapitalisation direction may require the ADI to issue shares or rights to acquire shares in the ADI, or other capital instruments, as specified in the direction. Only capital instruments specified in the regulations may be included in the direction.

Proposed section 13H generally provides that APRA must obtain and consider an expert’s report on the fair value of shares or rights to acquire shares, unless doing so would detrimentally affect the ADI’s depositors or the stability of Australia’s financial system.

47. Explanatory Memorandum, op. cit., p. 49.

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Proposed sections 13J and 13K provide for the methodology that the expert must follow when determining the fair value of each share in the ADI or right to acquire thereof.

Under **proposed section 13N**, a recapitalisation direction is no grounds to deny obligations where an ADI is a party to a contract—whether the proper law of the contract is Australian law or a foreign law.

Failure to make reasonable efforts to comply with a recapitalisation direction, where contravention is not due to circumstances beyond the ADI's control, is an offence under **proposed subsections 13Q(1) and (2)**. There is a similar offence provision relating to officers of an ADI under **proposed subsection 13Q(4)**, where the penalty is 50 penalty units.

Proposed section 13R provides generally that an acquisition of shares, rights to acquire shares or other capital instruments, directly resulting from compliance with a recapitalisation direction, are authorised for the purposes of subsection 51(1) of the *Trade Practices Act 1974*. This means that the acquisition is not subject to the restrictive trade practices provisions of that Act.

Similar amendments are proposed in **Schedule 2 item 83** (inserting **proposed sections 103A–103N** into the Insurance Act) and **Schedule 3 item 51** (inserting **proposed sections 230AA–230AM** into the Life Insurance Act).

APRA's powers to require information where the ADI has a statutory manager

Item 27 of Schedule 1 proposes to insert **new section 14AD** into the Banking Act. **Proposed section 14AD** relates to APRA's ability to obtain information or documents for the purposes of protecting depositors.

Proposed subsection 14AD(1) provides that APRA may require a person, by issuing a written notice, to give information or documents relating to the business of an ADI that has a statutory manager if certain conditions are met. These conditions are:

- where the statutory manager is APRA:
 - APRA believes on reasonable grounds that the person has the requisite information or documents, and
 - APRA requires the information or documents for the purposes of protecting depositors
- where the statutory manager is not APRA:
 - the statutory manager makes a written request to APRA to require the person to give the information or documents
 - APRA believes on reasonable grounds that the person has the requisite information or documents, and

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- APRA is satisfied that the statutory manager requires the information or documents for the purposes of protecting depositors.

The notice must specify a period of time (which is reasonable in all the circumstances), as well as the form and manner, in which such information or documents must be given to APRA (**proposed subsections 14AD(2) and (3)**).

Failure to comply with such notice is an offence punishable by a penalty of imprisonment for 12 months and/or 50 penalty units (**proposed subsection 14AD(4)**).⁴⁸

It is noted that under **proposed subsection 14AD(5)**, a person is not excused from complying with such notice on the grounds that doing so would tend to incriminate the individual person or make him or her liable to a penalty.

However, the Bill affords some protection in that under **proposed subsection 14AD(6)**, in the case of an individual person, neither the information or document given; the act of complying with the notice; nor any information, document or thing obtained as a direct consequence of complying with the notice, are admissible in evidence against the person in the following types of proceedings:

- a criminal proceeding, or
- a proceeding for imposing a penalty.

That protection does not apply to those proceedings relating to the falsity of the information or document.

The Explanatory Memorandum states:

The amendment recognises that information about the financial condition of the ADI is most likely to be within the knowledge of key personnel within the ADI or with whom the ADI deals. The amendment enables APRA to require such information in a timely manner so as to maximise the chances of rehabilitation or crisis resolution.⁴⁹

Amendments to the Financial Claims Scheme (FCS)

Proposed amendments to the FCS are expected to reduce costs for consumers in facilitating FCS administration, ensuring timely payment under the FCS and clarifying certain matters related to the operation of the FCS.⁵⁰

For example, **item 29 of Schedule 1** proposes to insert **new subsections 16AF(1A) and (1B)** into the Banking Act.

Proposed subsection 16AF(1A) provides that when determining entitlements under the FCS, the interest payable on protected accounts is payable at the rate of interest payable

48. See note 32.

49. Explanatory Memorandum, *op. cit.*, p. 43.

50. *Ibid.*, p. 129 (Regulation Impact Statement).

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according to terms and conditions of the protected account. However, if APRA considers that such rate is uncertain, the rate of interest is the rate that APRA declares is payable. Such declaration is not a legislative instrument under **proposed subsection 16AF(1B)**.

Another proposed amendment relating to the FCS is **item 33** of **Schedule 1**, which proposes to insert **new subsections 16AJ(2)–(9)** into the Banking Act, relating to the requirement on a liquidator of an ADI to assist APRA in making payments under the FCS.

Existing section 16AJ enables APRA to require a liquidator, appointed in connection with the actual or proposed winding up of an ADI, among others, to give APRA reasonable assistance in the performance of APRA's performance or the exercise of its powers, in relation to the FCS.

Proposed subsection 16AJ(2) enables APRA to require a liquidator to also assist APRA in paying account holders their entitlements under Subdivision C of Division 2AA of Part II of the Act (Payment of account holders of declared ADIs). Under **proposed subsection 16AJ(4)**, the liquidator's compliance with this requirement takes precedence over other requirements associated with winding up of the ADI. In addition, under **proposed subsection 16AJ(5)**, the liquidator does not have to comply unless there is sufficient property to meet his or her costs, which are likely to be incurred in complying with the requirement or unless APRA indemnifies the liquidator for those costs.

Schedule 2—amendments to the Insurance Act

APRA's preventive powers

Apart from the proposed amendments in **Schedule 2** mentioned above, other amendments in **Schedule 2** also aim to enhance APRA's powers to prevent prudential concerns arising in relation to insurers.

Item 18 of **Schedule 2** proposes to insert **new subsection 32(3)** into the Insurance Act.

Section 32 of the Insurance Act currently enables APRA to determine prudential standards.

The Explanatory Memorandum states that the existing provision enables APRA to require the head entity and its subsidiaries to comply with prudential standards individually; but not to make prudential standards in relation to corporate groups, or parts of groups, as a whole.⁵¹

Proposed subsection 32(3) provides a prudential standard may require particular entities to ensure that its subsidiaries (or particular subsidiaries); or the entity and its subsidiaries

51. Ibid., p. 16.

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(or particular subsidiaries), collectively satisfy particular requirements in relation to prudential matters.

The Explanatory Memorandum states:

The amendment enables APRA to make prudential standards with respect to general insurance groups or parts of such groups where it is desirable to do so.⁵²

It is noted that an equivalent provision is section 11AF of the Banking Act.

Appointment of auditors

Item 28 of Schedule 2 proposes to insert **new section 40** into the Insurance Act.

Section 39 of the Act already requires a general insurer to appoint an auditor and an actuary.

Proposed subsection 40(1) enables APRA to require a general insurer, by written notice, to appoint a person specified in the notice to be an auditor for a specified purpose.

Under **proposed subsection 40(2)**, the specified person may be the principal auditor or another auditor, consequently creating a distinction between the two roles.

The Explanatory Memorandum states:

The latter term captures both the principal auditor and an auditor appointed for a specific purpose by notice from APRA.

The distinction ensures that provisions in the Insurance and Life Insurance Acts are targeted at relevant auditors. For example, the present requirements under the Acts on insurers to appoint an auditor, to notify APRA of that appointment, or for the auditor to audit the insurer's yearly statutory accounts, are not intended to apply to auditors appointed by notice from APRA for a specific purpose. As a result, such provisions are amended to refer to the 'principal auditor' rather than to 'an auditor'. Similarly, those provisions intended to apply to all auditors are amended so as to refer to 'an auditor'.⁵³

Similar amendments are proposed in **Schedule 3 item 11** (inserting **proposed section 83A** into the Life Insurance Act).

52. Ibid., p. 17.

53. Ibid., pp. 58–59. The quote from the Explanatory Memorandum includes an explanation of other proposed amendments, such as **Schedule 2 items 24–27 and 29–33** and **Schedule 3 items 10, 12–19, and 20–26**.

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Failure management powers

External administration

Currently, under section 62K of the Insurance Act, APRA is entitled to be heard in proceedings of the Federal Court of Australia, in relation to the appointment of a judicial manager.

Under section 62R of the Insurance Act, the Federal Court may cancel such appointment at any time and appoint another person as judicial manager. However, there is no provision entitling APRA to be heard in this situation.

Item 50 of Schedule 2 proposes to insert **new subsection 62R(3)** into the Insurance Act, providing that APRA is entitled to be heard in proceedings before the Federal Court for the cancelling of the appointment of the judicial manager.

The Explanatory Memorandum states:

This ensures that APRA's views are taken into account in all circumstances where the Federal Court may issue an order relating to the appointment or cancellation of the appointment of judicial management.⁵⁴

A similar provision is proposed in **Schedule 3 item 42** (inserting **proposed subsection 163(3)** into the Life Insurance Act).

An amendment proposed in **Schedule 2** relating to the powers of judicial managers is set out in **item 51**, which proposes to insert **new paragraph 62T(1)(c)** into the Insurance Act.

Proposed paragraph 62T(1)(c) provides that at the time judicial management commences, the judicial manager has all the powers and functions of the Board of directors of the general insurer. This is in addition to already existing management powers of the general insurer.

The Explanatory Memorandum states:

These amendments align the powers of a judicial manager with the powers of a statutory manager under the Banking Act. There are certain decisions that may only be taken by the Board of the insurer, which may be required to be made by a judicial manager for the purposes of fulfilling its functions.⁵⁵

A similar amendment is proposed in **Schedule 3 item 43** (inserting **proposed paragraph 165(1)(e)** into the Life Insurance Act).

54. Explanatory Memorandum, op. cit., p. 42.

55. Ibid., p. 44.

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Item 52 of Schedule 2 proposes to substitute **section 62ZD** of the Insurance Act.

Existing section 62ZD enables APRA to request information from a judicial manager of a general insurer about either the conduct of the judicial management and/or the financial position of that general insurer and it requires the judicial manager to comply with that request.

Proposed subsection 62ZD(1) provides that in addition to the above matters, APRA may also request information from the judicial manager about a matter that APRA considers would enable APRA to perform its functions under Part VC of the Insurance Act (FCS for policy-holders with insolvent general insurers).

In addition, **proposed subsections 62ZD(3) and (4)** set out fault-based and strict liability offence provisions respectively, relating to judicial managers failing to comply with APRA's requests for such information. The fault-based offence has a penalty of imprisonment for six months and/or 100 penalty units.⁵⁶ The strict liability offence has a penalty of 60 penalty units.

The Explanatory Memorandum states:

The strict nature of the latter offence reflects APRA's need to receive prompt and accurate information about the conduct of judicial management and other relevant matters.

These amendments ensure that the statutory or judicial manager has can obtain the information required to understand the affairs of a distressed ADI or general insurer.⁵⁷

A similar amendment relating to statutory managers is proposed in **Schedule 1 item 27** (Banking Act – see above).

Business transfers

Transferring a business of an entity in financial distress to one that is financially healthy may be a less expensive means of resolving financial problems than winding up.⁵⁸

Item 53 of Schedule 2 proposes to insert **new paragraph 62ZI(2)(aa)** into the Insurance Act.

Existing section 62ZI relates to a report that the judicial manager must file with the Federal Court of Australia, recommending a specified course of action that is, in his or her

56. See note 32.

57. Explanatory Memorandum, *op. cit.*, p. 44.

58. *Ibid.*, p. 36.

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opinion, most advantageous to the general interest of the policyholders of the general insurer, as well as promoting financial system stability in Australia.

Proposed paragraph 62ZI(2)(aa) adds another possible course of action: transfer of the business, or part thereof, of the company to another company under section 25 of the *Financial Sector (Business Transfer and Group Restructure) Act 1999* (FS and Group Restructure Act).

A similar amendment has been proposed in **Schedule 3 item 44** (inserting **proposed paragraph 175(2)(aa)** into the Life Insurance Act).

A related amendment is proposed in **Schedule 4 items 4 and 5** (amending **section 25(1C)** of the *Financial Sector (Business Transfer and Group Restructure) Act*—see below for details).

Recapitalisation

The Bill proposes related amendments to the Insurance Act with respect to complying with recapitalisation directions mentioned previously.

For example, **item 49** of **Schedule 2** proposes to insert **new subparagraph 62M(a)(iiia)** into the Insurance Act enabling the Federal Court of Australia to make an order for the appointment of a judicial manager to a general insurer if that insurer has failed to comply with a recapitalisation direction.

Amendments to the Financial Claims Scheme (FCS)

Items 77 and 78 of **Schedule 2** propose to amend **section 62ZZO** of the Insurance Act.

Section 62ZZO currently enables APRA to require reasonable assistance from a general insurer or a liquidator appointed in connection with the winding up, or proposed winding up of a general insurer, in relation to APRA's FCS functions and powers under Part VC of the Insurance Act (FCS for policy-holders with insolvent general insurers).

Amendments proposed in **items 77 and 78** have the effect that, in addition to those from whom APRA may already require assistance, APRA may require assistance from a judicial manager of a general insurer.

Item 81 of **Schedule 2** proposes to insert **new subsections 62ZZQ(8)–(10)** into the Insurance Act.

Section 62ZZQ currently relates to enforcing compliance with the requirement to give APRA reasonable assistance and information under section 62ZZO and subsection 62ZZP(1) of the Insurance Act, as it relates to general insurers and liquidators.

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Proposed subsections 6ZZQ(8)–(10) extends the enforcement provisions to judicial managers.

Schedule 3—amendments to the Life Insurance Act

In addition to the amendments proposed in **Schedule 3** referred to above, **Schedule 3** sets out other proposed amendments to the Life Insurance Act.

Auditors' and actuaries' duty to give information

Item 27 of **Schedule 3** proposes to insert **new section 88B** into the Life Insurance Act, relating to an auditor's duty to give information to APRA when so required.

Currently, section 88A of the Act simply gives an auditor of a life company, authorised NOHC or subsidiaries thereof, discretion as to whether to give information to APRA that the auditor considers would assist APRA in its functions under the Life Insurance or FSCODA Acts.

In contrast, **proposed subsection 88B(1)** gives APRA power to, by written notice, require a person who is or was an auditor of a life company to:

- give APRA information, or
- produce books, accounts or documents,

about the life company if APRA considers that the giving of the information or producing such books, accounts or documents, will assist APRA in performing its functions under the Life Insurance or FSCODA Acts.

The person must comply with such requirement in a way that does not involve giving false or misleading information (**proposed subsection 88B(2)**). Failure to comply with the notice, or providing false or misleading information, is an offence punishable by a penalty of either six months imprisonment and/or 100 penalty units (fault-based offence) or 60 penalty units (strict liability offence) (**proposed subsections 88B(3)–(5)**).⁵⁹

Item 30 of **Schedule 3** proposes a similar amendment in relation to actuaries by inserting **new section 98B** into the Life Insurance Act.

Reviewable decisions

Item 57 of **Schedule 3** proposes to insert **new paragraphs 236(1)(o)** and **(p)** into the Life Insurance Act.

59. See note 32.

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Section 236 of the Act relates to the review of certain decisions. Subsection 236(1) lists decisions under the Act that are subject to review. Under subsections 236(2)–(4), a person affected by such a decision may, within a certain period of time, request the Regulator to reconsider that decision and provide reasons for the request.⁶⁰ The Regulator may then confirm, revoke or vary the decision in question (subsection 236(5)). Under subsection 236(8), an application may be made to the AAT to review the Regulator’s decision to confirm or vary the initial decision.

The effect of **item 57** is that both of the following decisions will be reviewable under section 236 of the Life Insurance Act:

- a refusal to give an approval under **paragraph 76A(1)(b)**—approval to keep records in a country other than Australia, and
- a decision to give an approval subject to conditions under **paragraph 76A(1)(b)**.

A similar amendment is proposed in **Schedule 4 item 30** (inserting **proposed paragraphs 10(1)(dp)–(dq)** into the Superannuation Supervision Act), as discussed previously.

Schedule 4—amendments of other Acts

Schedule 4 contains amendments proposed to several Acts, including:

- the APRA Act
- the FS and Group Restructure Act
- the FSCODA Act
- the RSA Act, and
- the Superannuation Supervision Act.

Amendments to the APRA Act

Item 1 of **Schedule 4** proposes to repeal **paragraphs 56(1)(a)–(cc)** (definitions of ‘protected information’ and ‘protected document’), substituting them with **proposed paragraphs 56(1)(a)–(c)**.

Section 56 of the APRA Act deals with the protection and sharing of protected information and documents by APRA.

The Explanatory Memorandum states:

Currently, the definitions of protected information and documents in section 56 covers much but not all information collected under prudential laws in relation to financial sector entities (as defined in the FSCODA). All such information and

60. For the meaning of ‘Regulator’, see Dictionary in the Schedule of the Life Insurance Act.

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documents should be subject to the protection of section 56 and the information sharing regime it contains.⁶¹

Proposed paragraphs (a)–(c) of the definitions in **subsection 56(1)** of the APRA Act captures financial sector entities as defined in the FSCODA Act.

Amendments to the FS and Group Restructure Act

Items 4 and 5 of **Schedule 4** propose to amend **subsection 25(1C)** of the FS and Group Restructure Act.

Section 25(1C) of this Act currently deals with compulsory transfer of business determinations made by APRA, in relation to transfers from one life insurance company to another.

The amendment proposed in **item 4** would extend the provision to transfers from a life insurance company to another company not necessarily a life insurance company.

Item 5 proposes to insert **new subsections 25(1D)–(1F)** into the FS and Group Restructure Act in relation to the following types of transfers:

- unregulated business from a life insurance company
- business from a general insurer, and
- unregulated business from a general insurer.

In general, these new provisions would enable APRA, in certain circumstances, to make determinations for the transfer only of business that is not unregulated business from a life insurance or general insurer, to an entirely different company; as well as determinations for the transfer of business from a general insurer to another general insurer. The circumstances include APRA being satisfied that:

- the transferring body had contravened the Life insurance Act or the Insurance Act (as the case may be), any regulations or other instruments made under or any obligations imposed by the respective Act, or
- the judicial manager of the transferring body had recommended under the respective Act that the business be transferred to the other company or general insurer (as the case may be).

Certain other conditions must also be satisfied:

- APRA considering the interests of the policy owners of the transferring body (viewed as a group) and, in considering to those interests, concluding that it would be appropriate for the transfer to be made, and
- conditions set out in subsection 25(2) of the FS and Group Restructure Act, such as APRA being satisfied that:

61. Explanatory Memorandum, op. cit., p. 29.

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- the board of directors of the receiving entity consented to the transfer, and
- the transfer is appropriate, having regard to:
 - the interests of the financial sector as a whole; and
 - any other matters that APRA considers to be relevant.

For a discussion of related amendments to the Insurance and Life Insurance Acts relating to business transfers, see above.

Amendments to the FSCODA Act

Objective of the FSCODA Act

Item 7 of Schedule 4 proposes to substitute **subsection 3(1)** of the FSCODA Act.

Subsection 3(1) currently states that the objective of this Act is to enable APRA in collecting information to assist APRA in the prudential regulation and monitoring of financial sector bodies, as well as to facilitate the formulation of monetary policy by the RBA.

However, as the Explanatory Memorandum states:

The global financial crisis highlighted that the Government and other financial sector regulators may require specific data to inform decisions and monitor subsequent outcomes that cannot presently be collected by APRA under the FSCODA. This includes data from non-prudentially regulated bodies which operate in the financial sector.⁶²

Consequently, **proposed subsection 3(1)** provides that the objective of the FSCODA Act is to enable APRA to collect information to assist:

- APRA in the prudential regulation and monitoring of financial sector bodies
- another financial sector agency to perform its functions or exercise its powers, and
- the Minister to formulate monetary policy.

New definitions

‘Financial sector agency’ is defined in **item 22 of Schedule 4**, which proposes to insert the **new definition of ‘financial sector agency’** into the FSCODA Act. ‘**Financial sector agency**’ would mean:

- ASIC
- the RBA, and

62. Ibid., p. 77.

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- a Commonwealth, State or Territory authority that is prescribed by the regulations.

Item 8 of Schedule 4 proposes to amend the definition of ‘financial sector entity’ in **subsection 5(2)** of the FSCODA Act.

Currently, a ‘financial sector entity’ is a registered or regulated entity; or a corporation that is a medical indemnity entity under section 5A of the Act; or a discretionary mutual fund, as defined in subsection 5(5) of the Act.

The **proposed new definition** means that the FSCODA Act would also apply to certain persons providing financial services and persons who participate in a payment system under the relevant legislation and that reporting standards to be complied with by such person may be made.⁶³

Reporting standards and confidential information

Items 10 and 12 of Schedule 4 propose to amend **subsection 13(1)** of the FSCODA Act.

Proposed subsection 13(1) of the Act would enable APRA to determine reporting standards, in writing (as opposed to by legislative instrument), that must be complied with by financial sector entities, with respect to particular reporting documents, and to publish those standards, which are legislative instruments, in any way that APRA considers appropriate.

Item 13 of Schedule 4 proposes to insert **new subsections 13(1A)** and **(1B)** into the FSCODA Act.

Proposed subsection 13(1A) provides that a reporting standard is a legislative instrument except in particular circumstances, which are as follows:

- APRA considers, on reasonable grounds, that the standard includes confidential information, the publication of which is likely to have a detrimental effect on the stability of either the financial system or of one or more financial institutions
- APRA considers, on reasonable grounds, that APRA urgently requires the information contained in the reporting documents for any of the following purposes:
 - determining the financial or prudential condition of financial sector entities
 - determining the nature or level of exposure that financial sector entities have to risks
 - assessing potential threats to the stability of the financial system

63. As to the meaning of ‘payment system’, see *Payment Systems (Regulation) Act 1998* section 7.

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- assisting APRA, the Minister or a financial sector agency to respond to any threats to the stability of the financial system
- determining what, if any, action should be taken by or in relation to one or more financial sector entities, and
- the standard does not require such urgently required information to be given on an ongoing basis.

Under **proposed subsection 13(1B)**, where the Minister directs APRA to determine reporting standards under **proposed section 13C** (inserted by **Schedule 4 item 17**), to be complied with by proposed additional financial sector entities (see **item 8** above), APRA must determine such reporting standards by legislative instrument.

The Explanatory Memorandum states:

While a one-off data collection can be effected as a legislative instrument under the FSCODA, it may create problems insofar as it may force APRA to publically [sic] reveal the sensitive information it has sought to collect or which has led it to make the collection.

Such an outcome would be undesirable, particularly where the publication of the information is likely to have a detrimental effect on financial system stability or the stability of one or more financial institutions.⁶⁴

However, the Bill proposes to include provisions to ensure a certain degree of transparency and accountability, where reporting standards are not determined by way of legislative instrument.

For example, **item 17** of **Schedule 4** proposes to insert **new sections 13A–13C** into the FSCODA Act.

Proposed section 13A provides that if a reporting standard, determined under **proposed section 13(1)**, is not a legislative instrument, as soon as practicable after the standard is determined, APRA must give a copy of the standard to each financial sector entity that must comply with it and to the Minister. In addition, APRA must give the financial sector entity a written statement explaining the effect of **proposed section 13B** (see below) at the same time as it gives the entity a copy of the reporting standard.

Proposed subsection 13B(1) provides that if APRA gives a financial sector entity a copy of the reporting standard under **proposed subsection 13A(1)**, that entity must not disclose to any person that it had been given a copy of such standard nor any confidential information included in such standard. Failure to comply attracts a penalty of a two year imprisonment.

64. Explanatory Memorandum, op. cit., p. 83.

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However, **proposed subsection 13B(2)** provides that **proposed subsection 13B(1)** does not apply if

- disclosure is to:
 - APRA for the purposes of APRA performing its functions under the FSCODA Act or any other Commonwealth law, or
 - an employee officer or contractor of the financial sector entity for the purposes of that person performing his or her duties in relation to the reporting standard, or
- disclosure is authorised under the FSCODA Act or another law, or
- the confidential information included in the reporting standard has already been lawfully made public from other sources.

Proposed section 13C enables the Minister to direct APRA to determine reporting standards under **proposed subsection 13(1B)**, as discussed above.

It is noted that the Explanatory Memorandum states:

To ensure that relevant entities are aware of the above provisions prohibiting inappropriate disclosure, APRA must explain the effect of the provisions to any entity which receives a reporting standard to which the provisions apply.

...

the amendments provide an exception from the requirements of the Legislative Instruments Act for the relevant reporting standards. APRA is, however, required to give a copy of any such standard to the Minister as soon as practicable after it is determined and must report the number of times during a year that such a reporting standard is determined in its annual report. Under subsection 59(4) of the APRA Act, the Minister must cause a copy of APRA's annual report to be tabled in each House of Parliament within 15 sitting days after the day on which the Minister receives the report.⁶⁵

Urgent reporting standards

Item 16 of Schedule 4 proposes to substitute **subsection 13(6)** of the FSCODA Act.

Currently, subsection 13(6) provides that the requirement for APRA, when preparing reporting standards, to consult with those financial sector entities or class thereof (or their

65. Ibid., pp. 84–85. See also **Schedule 4 item 2**, which proposes to insert a **new paragraph 59(2)(ba)** into the APRA Act. Subsection 59(2) relates to the contents of the annual report that APRA must give the Minister. **Proposed paragraph 59(2)(ba)** would require APRA to include a statement of the number of times during the year that APRA determined a reporting standard, under **proposed subsection 13(1)** of the FSCODA Act, which is not a legislative instrument.

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associations or bodies representing them as the case may be), which would be affected by proposed reporting standards, does not apply if APRA is satisfied that the delay involved in holding the consultations would prejudice the interests of depositors, policy holders or members of the financial sector entity or financial sector entities concerned.

Proposed subsection 13(6) provides that, in addition to the above, APRA would also not have to consult in those circumstances where the delay in holding consultations would have a detrimental effect on the stability of the financial system.

Exemptions from having to comply with reporting standards

Item 18 of Schedule 4 proposes to substitute existing subsection 16(1) in the FSCODA Act with **new subsections 16(1)–(1B)**.

Existing section 16(1) enables APRA, by legislative instrument, to exempt a financial sector entity, or a class or kind thereof, from the requirement to comply with either:

- all requirements contained in any one or more applicable reporting standards, or
- a specific requirement(s) contained in applicable reporting standards.

Proposed subsections 16(1) and (1A) only relate to APRA exempting a single financial sector entity from having to comply with applicable standards by written notice that is not a legislative instrument.

The Explanatory Memorandum states:

The amendment reflects that a decision to so exempt a single entity is of an administrative nature rather than of a legislative nature.⁶⁶

However, under **proposed subsection 16(1B)**, exemptions for a class or kind of financial sector entities would be by legislative instruments.

Appointment of auditors and conduct of audits

As the Explanatory Memorandum states:

There are currently no provisions in the FSCODA relating to the appointment of auditors and the conduct of audits. APRA may require much of the data collected under the Act to be audited via its existing powers in the Banking, Insurance, Life Insurance and Superannuation Industry (Supervision) Acts. However, these provisions do not extend to all data collected under the FSCODA.⁶⁷

Amendments proposed in Schedule 4 seek to address that situation.

66. Explanatory Memorandum, op. cit., p. 86.

67. Ibid., p. 59.

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For example, **items 14 and 15 of Schedule 4** propose to amend **subsection 13(2)** of the FSCODA, which deals with the kind of matters that reporting standards may include. These amendments have the effect that reporting standards may include matters relating to the audit of reporting documents (as defined in subsection 13(1)) and that information contained in reporting documents may relate to information that APRA requires to perform its functions under:

- Division 2AA of Part II of the Banking Act (FCS for account holders with insolvent ADIs), or
- Part VC of the Insurance Act (FCS for account holders with insolvent general insurers).

In addition, **item 20 of Schedule 4** proposes to insert a **new Division 2A (Auditing of documents)** in Part 3 of the FSCODA Act containing several new provisions—being **new sections 17A–17D**.

In particular, under **proposed section 17B**, the auditor must perform the functions and duties of an auditor set out in the reporting standards and comply with the reporting standards in performing their functions and duties. Also, the financial sector entity must make any arrangements necessary to enable the auditor to perform their functions and duties. This is similar to amendments proposed to the Banking and Life Insurance Acts (see above).

Schedule 5—amendments relating to levies

Amendments across several Acts

Changing the valuation basis for determining levies

Amendments are proposed to various Acts changing the valuation basis for determining levies. This is done by replacing the references to ‘asset value’ in those Acts with references to ‘levy base’. See, for example, **items 1–4, 7–21, and 23–28 of Schedule 5**.

These proposed amendments are not expected to impose costs.⁶⁸

Additional amendments to the Superannuation Levy Imposition Act

Regulated levy component for new starters

This Act imposes a levy on trustees of certain superannuation entities. A ‘superannuation entity’ is defined in section 5 of the Act as an entity that:

- is a superannuation entity, and

68. Ibid., p. 135 (Regulation Impact Statement).

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- is not a self-managed superannuation fund, under the Superannuation Supervision Act.

Item 30 of Schedule 5 proposes to substitute **subparagraph 7(1A)(a)(ii)** in the Act.

Currently, section 7 provides for calculating the amount of levy to be paid. Existing subparagraph 7(1A)(a)(ii) provides that where the superannuation entity was an unregulated entity on 30 June of the previous financial year (a ‘new starter’), the restricted levy component is generally the amount that is the restricted levy percentage of the entity’s asset value on that date.

The Explanatory Memorandum states:

This method of calculating the restricted levy component is not appropriate for new starters. For example, under the present arrangements if a fund becomes a regulated superannuation fund on 1 October of a particular financial year, its restricted levy component is to be worked out by applying the restricted levy percentage to its asset value as at 30 June in the previous financial year. However, as the fund is a new starter it is unlikely to have had any assets, or have been in existence, on 30 June of the previous financial year. As a result, the fund is likely to pay only the minimum amount for this component, which could be less than commensurate with the costs of APRA’s supervisory resources.⁶⁹

Proposed subparagraph 7(1A)(a)(ii) would change the restricted levy percentage to that of the entity’s levy base on the day that the entity became a superannuation entity.

According to the Explanatory Memorandum:

The amendments bring the levy arrangements for superannuation entities into line with those applicable to ADIs, general insurers, life insurers, retirement savings account providers and leviable first home saver account providers. The respective levy imposition Acts in relation to those entities presently provide that the valuation day for a new starter is the day that it becomes regulated.⁷⁰

There is a similar amendment proposed by **item 32 of Schedule 5** in the Bill (substituting subsection 7(1B) of the Superannuation Levy Imposition Act), relating to the unrestricted levy component.

Concluding comment

The Bill does propose largely technical amendments, making the various Acts relating to the financial sector more consistent with each other.

69. Ibid., pp. 92–93.

70. Ibid., p. 93.

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It is noted that the Bill proposes several offence provisions, which address a number of gaps and inconsistencies in existing financial sector legislation. Stakeholder concerns about **proposed section 130BB**, as mentioned above, should also be considered.

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