Banking exemption No. 1 of 2008

<u>EXPLANATORY STATEMENT</u>

Prepared by the Australian Prudential Regulation Authority

Banking Act 1959 subsections 11(1)

Acts Interpretation Act subsection 33(3A)

Under subsection 11(1) of the *Banking Act 1959* (**the Act**), APRA has power to determine, by order published in the *Gazette* or on the Federal Register of Legislative Instruments[1], that all or specified provisions of the Act (other than section 63) do not apply to a person during the period while the order continues in force. Paragraph 11(2)(b) provides that an order may specify the period during which it remains in force.

Under subsection 33(3A) of the *Acts Interpretation Act 1959*, where an Act confers a power to make an instrument with respect to particular matters (however the matters are described), the power shall be construed as including a power to make such an instrument with respect to a particular class of those matters.

Banking exemption No. 4 of 2006 (**the existing instrument**) exempts authorised deposit-taking institutions (**ADI**s) within the meaning of section 5 of the Act, that have taken farm management deposits (**FMDs**), from having to treat that class of deposits as unclaimed moneys under section 69 of the Act. Accordingly, ADIs are not required to include FMDs in a statement of unclaimed moneys to the Treasurer and pay them to the Commonwealth. However, this does not affect an ADI's obligation to deal with other classes of unclaimed moneys (i.e. unclaimed moneys that are not FMDs) in accordance with section 69.

The existing instrument will remain in force until 31 December 2008. APRA had anticipated that, prior to 31 December 2008, there would be a high level policy review which would explore other possible solutions regarding the interaction of FMDs and section 69 of the Act. Such a review, which was foreshadowed in the Explanatory Statement accompanying the existing instrument, did not take place because key resources were directed to work on policy responses to the global financial crisis. The Department of the Treasury intends to address this issue in the course of 2009 on a more permanent and definitive basis through suitable legislative changes. However, in the interim, APRA has made Banking exemption No. 1 of 2008 (the new instrument) to replace the existing instrument. The new instrument will remain in force until 31 December 2009.

1. Background

Section 69 of the Act

Subsections 69(1) and (2) of the Act define 'unclaimed moneys'. Subsection (1) provides that for the purposes of section 69 'unclaimed moneys' means all principal,

---

[1] Publication on the register is required where the instrument is a legislative instruments, and will satisfy the requirement to gazette the instrument: see section 56 of the *Legislative Instruments Act 2003*.

interest, dividends, bonuses, profits and sums of money legally payable by an ADI but in respect of which the time within which proceedings may be taken for the recovery thereof has expired, and includes moneys to the credit of an account that has not been operated on either by deposit or withdrawal for a period of not less than 7 years. Subsection (2) provides that, for the purposes of subsection (1), the debiting of a fee to an account shall be deemed not to be a withdrawal and the crediting to an account of interest payable by an ADI on that account shall not be a deposit.

Subsection 69(3) of the Act provides that an ADI shall, within 3 months after 31 December in each year, deliver to the Treasurer a statement, which must comply with certain requirements, of sums of unclaimed moneys, other than unclaimed moneys held by RSAs, of not less than $100 or the prescribed amount. Subsection 69(3AA) provides that an ADI is guilty of an offence if the ADI does not give the Treasurer such a statement and there is no order in force under section 11 of the Act determining that subsection (3AA) does not apply to the ADI. Subsections 69(3A) and (4) make provision in respect of the medium upon which a statement is submitted, and content of the statement.

Subsection 69(5) provides that the total amount shown in the statement shall be paid by the ADI to the Commonwealth at the time of the delivery of the statement. Subsection 69(5A) provides that an ADI is guilty of an offence if it does not pay, at the time of the delivery of the statement, the amount specified in the statement, as required by subsection (5) and there is no order in force under section 11 determining that subsection (5A) does not apply to the ADI.

Farm Management Deposits

The requirements of section 69 have the potential to affect FMDs in a way that is inconsistent with the policy intention.

FMDs were introduced into the *Income Tax Assessment Act 1936* by way of Schedule 2G.

An FMD is a tax-linked, financial risk management tool for primary producers. The scheme is implemented commercially through participating financial institutions, including ADIs.

An FMD is designed to allow primary production income from profitable years to be set aside for subsequent ‘draw-down’ in low-income years, thereby reducing the risk to primary producers of income variability owing to factors such as drought. Primary producers are able to claim tax deductions for FMDs in the year of deposit and, when an amount is withdrawn from the account, that amount is included in the primary producer’s assessable income.

FMDs were introduced in 1999 and it would appear that many of the depositors in the FMDs choose to leave their funds in those accounts untouched for lengthy periods of time.

It would appear that money to the credit of an FMD would be considered to be unclaimed moneys as defined in section 69 once the 7 year period has elapsed. ADIs are required to inform the Treasurer of unclaimed moneys within three months after 31 December each year and, as such, time is a significant factor.

The existing instrument was made to avoid an outcome where, from 31 December 2006, ADIs might have been required by section 69 to transfer substantial FMD moneys to the Commonwealth potentially for the first time since FMDs were set up in 1999.

The application of section 69 to FMDs would frustrate their purpose, and is unlikely to have been intended by Parliament. In relation to tax, if the FMD monies are transferred to unclaimed monies, there is a risk that the provisions would operate so as to require the ATO to treat the transfer as a withdrawal and to treat such funds as taxable income for the primary producer. Further, it is problematic for primary producers to avoid the application of section 69 since:

- if the primary producer tries to increase the balance of the FMD in order that the 7 year rule in section 69 does not apply, there is a risk that the ATO will consider the whole amount to be withdrawn and redeposited;

- the taxpayer/primary producer will have to indicate in its tax return that a withdrawal and deposit were made in the same income year. However, FMDs must not be withdrawn within 12 months to retain the tax benefit. By forcing the taxpayer to change the balance, the 12 month period will be reset. It will be seen as unfair to force a taxpayer who has had an FMD for 7 years to have to go through another 12-month waiting period; and

- alternatively, the taxpayer could withdraw part of the FMD that has been held. However this withdrawal would be considered taxable income. The taxpayer would be forced to withdraw the FMD at a time when it need not do so. This would run counter to the policy intent of FMDs.

2. Purpose of the new instrument

The purpose of the new instrument is to extend the exemption provided for in the existing instrument whereby ADIs that hold FMDs are exempted from the requirement to report FMDs in their statement of unclaimed moneys to the Treasurer under subsection 69(3). For the avoidance of doubt, the new instrument repeats the exemption in the existing instrument that exempts such ADIs from the obligation to remit amounts representing FMDs to the Commonwealth under subsection 69(5), and exempts ADIs from certain criminal penalty and procedural provisions supporting subsections 69(3) and (5).

As with the existing instrument, the new instrument does not exempt a relevant ADI from any of these subsections other than in relation to the class of deposits constituting FMDs. In exempting only the class of deposits comprising FMDs, the new instrument also relies on subsection 33(3A) of the Acts Interpretation Act.

Accordingly, the new instrument does not exempt any ADI from its obligation to report other classes of unclaimed moneys and pay them to the Commonwealth, or exempt an ADI from any criminal offence provision if an ADI fails to comply with section 69 in relation to a non-FMD deposit.

3. Operation of the new instrument

The new instrument applies from the later of (a) the first moment of the day after it is registered on the Federal Register of Legislative Instruments and (b) 1 January 2009 (when the existing instrument expires) and ends on 31 December 2009.

4. Consultation

APRA has not undertaken formal consultation on this issue. In APRA's view, no new issues arise with respect to the new instrument and a further order under section 11 (extending for a period the existing exemption in respect of FMDs as a class from relevant provisions section 69 of the Act) will, pending a policy review during 2009 of other possible solutions regarding the interaction of FMDs and section 69 of the Act:

- continue to have beneficial consequences for primary producers;
- continue to overcome an unintended consequence of section 69 of the Act; and
- have no adverse consequences for industry.