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HOUSE OF REPRESENTATIVES

FINANCIAL SECTOR LEGISLATION AMENDMENT (CRISIS RESOLUTION
POWERS AND OTHER MEASURES) BILL 2017

EXPLANATORY MEMORANDUM

(Circulated by authority of the
Treasurer, the Hon Scott Morrison MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
ADI	Authorised deposit-taking institution
Administrator	A person appointed by APRA to take control of an entity as statutory manager under section 13A of the Banking Act, new section 62ZOA of the Insurance Act or new section 179AA of the Life Insurance Act, where APRA itself does not take over control of the entity under those sections.
APRA	Australian Prudential Regulation Authority
APRA Act	<i>Australian Prudential Regulation Authority Act 1998</i>
AT1	Additional Tier 1
ATO	Australian Tax Office
Authorised NOHC	A non-operating holding company that is authorised either under the <i>Banking Act 1959</i> or <i>Insurance Act 1973</i> , or registered under the <i>Life Insurance Act 1995</i>
Banking Act	<i>Banking Act 1959</i>
BCBS	Basel Committee on Banking Supervision
Bill	Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017
CET1	Common Equity Tier 1
Commencement time	The day the Bill receives the Royal Assent
CFR	Council of Financial Regulators
Corporations Act	<i>Corporations Act 2001</i>
Court	Federal Court of Australia
FCS	Financial Claims Scheme
FSB	Financial Stability Board
Foreign ADI	A foreign ADI as defined in subsection 5(1) of the <i>Banking Act 1959</i>

<i>Abbreviation</i>	<i>Definition</i>
Foreign general insurer	A foreign general insurer as defined in subsection 3(1) of the <i>Insurance Act 1973</i>
Foreign insurer	A foreign general insurer or foreign life insurer
Foreign life insurer	An eligible foreign life insurance company as defined in the Schedule Dictionary of the <i>Life Insurance Act 1995</i>
Foreign regulated entity	A foreign ADI, foreign general insurer, or foreign life insurer
FSCODA	<i>Financial Sector (Collection of Data) Act 2001</i>
Holding company	In relation to a body corporate, refers to another body corporate of which the first body corporate is a subsidiary
IADI	International Association of Deposit Insurers
IAIS	International Association of Insurance Supervisors
Industry Acts	Refers collectively to the <i>Banking Act 1959</i> , <i>Insurance Act 1973</i> , and <i>Life Insurance Act 1995</i> but does not include the <i>Superannuation Industry (Supervision) Act 1993</i> or the <i>Private Health Insurance (Prudential Supervision) Act 2015</i> .
Insurance Act	<i>Insurance Act 1973</i>
Insurer	Refers collectively to general and life insurers
Key Attributes	Financial Stability Board, 'Key Attributes of Effective Resolution Regimes for Financial Institutions' (15 October 2014)
Life Insurance Act	<i>Life Insurance Act 1995</i>
NOHC	Non-operating holding company
PGPA Act	<i>Public Governance, Performance and Accountability Act 2013</i>
Policyholder	Means a 'policyholder' as per the <i>Insurance Act 1973</i> and a 'policy owner' as per the <i>Life Insurance Act 1995</i>
PSN Act	<i>Payment Systems and Netting Act 1998</i>
Regulated entity	An ADI, general insurer, or life insurer

<i>Abbreviation</i>	<i>Definition</i>
Relevant group of bodies corporate	A group of bodies corporate comprising a regulated entity and all of its subsidiaries or an authorised NOHC and all of its subsidiaries
Statutory manager	Refers to APRA, or an administrator appointed by APRA, when it takes control of an entity under section 13A of the Banking Act, new section 62ZOA of the Insurance Act or new section 179AA of the Life Insurance Act.
Target body corporate	A body corporate that is an authorised NOHC, subsidiary of a regulated entity or a subsidiary of an authorised NOHC.
Transfer Act	<i>Financial Sector (Business Transfer and Group Restructure) Act 1999</i> (the Bill amends the title of this Act to the <i>Financial Sector (Transfer and Restructure Act) 1999</i>)
T2	Tier 2
2012 Consultation Paper	'Strengthening APRA's Crisis Management Powers' Consultation Paper (September 2012)

General outline and financial impact

Crisis management powers

Schedules 1 to 7 to the Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017 (the Bill) makes amendments to the *Banking Act 1959*, *Insurance Act 1973*, *Life Insurance Act 1995*, *Australian Prudential Regulation Authority Act 1998*, *Payment Systems and Netting Act 1998*, *Financial Sector (Business Transfer and Group Restructure) Act 1999*, *Corporations Act 2001* and the *Income Tax Assessment 1997*.

The Bill strengthens the powers of the Australian Prudential Regulation Authority (APRA) to facilitate the orderly resolution of an authorised deposit-taking institution (ADI) or insurer so as to protect the interests of depositors and policyholders, and to protect the stability of the financial system.

The Bill also ensures that APRA has powers to set appropriate prudential requirements and take action in relation to resolution planning so that ADIs and insurers are better prepared for resolution.

Date of effect: The amendments will commence on the day the Bill receives Royal Assent.

Proposal announced: The Government announced on 20 October 2015 its intention to provide regulators with clear powers in the event a prudentially regulated financial entity fails as part of its response to the Financial System Inquiry (FSI).

Financial impact: Nil.

Human rights implications: This Bill does not raise any human rights issues. See Statement of Compatibility with Human Rights — Chapter 12.

Compliance cost impact: \$1.3 million annually.

Summary of regulation impact statement

Impact: The amendments to the above listed Acts impact ADIs, insurers and related group entities as well as their respective depositors and policyholders.

Main points:

- The Government considered the regulatory impacts of various reform options through three papers (and their associated consultation processes) – the Financial System Inquiry (Murray Inquiry) Final Report, the 2012 consultation paper ‘Strengthening APRA’s Crisis Management Powers’, and the 2011 consultation paper ‘Financial Claims Scheme’ – as well as through extensive consultation with industry stakeholders.
- The Murray Inquiry noted that CFR agencies reviewed Australia’s existing crisis management toolkit and found that although Australia has a strong framework, there are gaps in powers that could be strengthened.
- The Murray Inquiry also noted that there are high costs associated with the disorderly failure of an institution, particularly where this creates financial system instability or the need for Government support. These costs would be exacerbated should reforms to strengthen resolution powers and support pre-planning for financial failure not proceed.
- The CFR will continue to review and test the effectiveness and efficiency of the crisis management powers every year. These crisis management powers will also be independently assessed as part of the International Monetary Fund’s Financial System Assessment Program in 2018.

Chapter 1

Overview of crisis management

Outline of explanatory memorandum

1.1 The Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017 (the Bill) provides the Australian Prudential Regulation Authority (APRA) with an enhanced suite of crisis resolution powers applicable to prudentially regulated authorised deposit-taking institutions (ADIs), general insurers and life insurance companies (insurers), and certain group entities.

1.2 Chapters 2 to 9 deal with amendments to powers relevant to the resolution of a regulated entity in distress. These are specifically APRA's powers in relation to:

- statutory and judicial management (Chapter 2);
- directions powers (Chapter 3);
- transfer powers (Chapter 4);
- conversion and write-off of capital instruments (Chapter 5);
- stay provisions (Chapter 6);
- foreign branches (Chapter 7);
- Financial Claims Scheme (Chapter 8); and
- wind-up and other matters (Chapter 9).

1.3 Chapter 10 deals with amendments that relate to crisis resolution planning, to provide APRA with clear powers to ensure that regulated entities are better prepared for a resolution prior to such an event arising.

Context of the Bill

1.4 The global financial crisis demonstrated that, when complex financial groups enter distress, failure to resolve these entities in an orderly fashion can lead to severe adverse economic consequences. To achieve effective resolution, it is essential for regulators to have access to

flexible, timely and robust resolution powers. When dealing with complex groups, it is often not sufficient to apply powers to the regulated entity alone. Critical services (such as information technology, financial positions or essential staff) may be located in other group entities and contagion effects can occur within groups. Regulators need to be able to move swiftly to safeguard the critical operations of these entities where the need arises.

1.5 Just as important as the adequacy of the powers is the legislative context in which those powers are exercised. Regulators and key stakeholders such as directors, senior managers and administrators need to be confident that actions taken in good faith in pursuit of a resolution cannot be unwound, and that the stakeholders implementing said actions will be protected from adverse consequences.

1.6 Likewise, depositors, policyholders, taxpayers, shareholders and creditors require a legislative framework for resolution that meets the objectives of regulators and preserves value in distressed institutions, whilst maintaining to the extent possible the structure of commercial bargains struck prior to resolution. However, to achieve this, regulators and government will sometimes require space in which to properly understand the nature and extent of the problems facing a distressed institution, and time in which to fashion a solution. As such, regulators need to be able to conduct their work confidentially (where appropriate) and without being frustrated by pre-emptive actions by counterparties of the distressed institution. Where resolution has an adverse impact on counterparties such as creditors (relative, for instance, to ordinary insolvency), those counterparties ought to be confident that they will be compensated appropriately.

1.7 As well as flexible, timely and robust resolution powers, it is important regulators have clear powers to set appropriate prudential requirements for resolution planning, and to address potential barriers to the orderly resolution of regulated institutions and groups, prior to any crisis occurring.

1.8 Following the global financial crisis, from 2008 to 2010, the then Government introduced a series of legislative reforms to enhance prudential regulation and consumer protections, including the Financial Claims Scheme (FCS).

1.9 In 2012, the then Government issued a consultation paper, 'Strengthening APRA's Crisis Management Powers' (2012 Consultation Paper), which canvassed a large number of proposals as part of an ongoing review of APRA's crisis management powers. These proposals sought to address the identified gaps and areas that could be strengthened with reference to domestic and international developments at the time.

1.10 The 2012 consultation process was put on hold pending the outcome of the 2014 Financial System Inquiry (FSI).

1.11 The Final Report of the FSI, delivered in December 2014, recommended that the Government complete the process for strengthening APRA's crisis management powers (Recommendation 5). In its response to the FSI, the Government agreed that regulatory settings should provide regulators with clear powers in the event that a prudentially regulated financial entity or any part of the financial market infrastructure (FMI) fails¹.

1.12 The Government has prioritised the implementation of the crisis-oriented proposals in the 2012 Consultation Paper for APRA in relation to prudentially regulated ADIs and insurers. The Government has also prioritised the implementation of key proposals from consultations on the contractual loss absorption provisions in regulatory capital instruments in 2014 and on the FCS in 2011.

1.13 The proposals in the 2012 Consultation Paper were prepared to reflect international developments in financial regulation following the global financial crisis, particularly the work in the G20 and by the Financial Stability Board (FSB) to promote resilient financial systems and frameworks to resolve financial distress.

1.14 Since 2012, the G20 and FSB have continued to progress this work, including updating the FSB's Key Attributes on Effective Resolution Regimes (Key Attributes) in 2014 to address sector-specific considerations for insurance and FMI. The Basel Committee on Banking Supervision (BCBS) and the International Association of Insurance Supervisors (IAIS) have also taken steps to further address crisis preparedness in their core principles for the supervision of banks and insurers. The proposals in the Bill help to provide a framework for resolution that is consistent with these international developments, in a manner that is appropriate for the Australian financial system. In a cross-border context, the proposals in the Bill help ensure APRA has resolution powers which could be applied in a coordinated manner with authorities in other jurisdictions, where relevant, consistent with the Key Attributes.

1.15 Other proposals in the 2012 Consultation Paper that were less resolution-centric and those relating to FMI will be progressed separately. Similarly, while the Government has also agreed to consider other

¹ In this context, FMI refers to critical FMI in the form of market operators and clearing and settlement facilities

important crisis-related reforms, such as the implementation of a requirement for additional loss absorbing capacity (Recommendation 3 of the FSI's Final Report), that work is being progressed separately to these reforms.

Summary of new law

1.16 The Bill amends the *Banking Act 1959* (Banking Act), *Insurance Act 1973* (Insurance Act), *Life Insurance Act 1995* (Life Insurance Act), *Australian Prudential Regulation Authority Act 1998* (APRA Act), *Payment Systems and Netting Act 1998* (PSN Act), *Financial Sector (Business Transfer and Group Restructure) Act 1999* (Transfer Act), *Corporations Act 2001* (Corporations Act) and *Income Tax Assessment Act 1997*.

1.17 For the purposes of this Bill, the Banking Act, Insurance Act and Life Insurance Act are collectively referred to as the Industry Acts.

1.18 The Schedules to this Bill make amendments in relation to crisis resolution to:

- enhance APRA's statutory and judicial management regimes to ensure their effective operation in a crisis;
- enhance the scope and efficacy of APRA's existing directions powers;
- improve APRA's ability to implement a transfer under the Transfer Act;
- ensure the effective conversion and write-off of capital instruments to which the conversion and write-off provisions in APRA's prudential standards apply;
- enhance stay provisions and ensure that the exercise of APRA's powers does not trigger certain rights in the contracts of relevant entities within the same group;
- enhance APRA's ability to respond when an Australian branch of a foreign regulated entity (foreign branch) may be in distress;
- enhance the efficiency and operation of the FCS and ensure that it supports the crisis resolution framework; and

- enhance and simplify APRA's powers in relation to the wind-up or external administration of regulated entities under the Industry Acts, and other related matters.

1.19 Schedules 1 to 3 to this Bill also make amendments to the Industry Acts to ensure that APRA has clear powers to make appropriate prudential standards on resolution planning and ensure that regulated entities and their groups put in place measures to improve their preparedness for resolution.

Detailed explanation of new law

1.20 The Bill gives APRA an enhanced set of powers for crisis resolution and resolution planning in relation to regulated entities.

Crisis resolution

Statutory and judicial management

1.21 The existing statutory and judicial management regimes in the Industry Acts represent important powers for dealing with a financial institution in acute distress. APRA may need to use these tools to take control of an entity in cases where it does not have confidence that the board and management is capable of resolving a crisis satisfactorily, or where the board and management are mismanaging the entity, including where it is insolvent or near insolvent. Given the importance of these powers, particularly as a measure of last resort, certain key enhancements are proposed to ensure their effective operation in all relevant situations.

1.22 These enhancements include ensuring the statutory management tool can be applied in a group context where necessary. The structures of financial groups can be complex, involving numerous business lines and support services linked through different ownership and contractual arrangements. In the absence of effective group resolution powers, it may be particularly difficult to resolve a distressed regulated entity or group quickly and effectively.

1.23 A further enhancement is to extend the statutory management regime to insurers in certain defined circumstances. In most situations, applying to the Court for the appointment of a judicial manager is likely to remain the appropriate resolution tool for a failing insurer. However, there may be specific situations where APRA needs the ability to appoint a statutory manager to an insurer. In particular, this could be the case where the insurer is large or part of a complex financial group, or its distress poses a risk to the financial system or economy.

1.24 This Bill enhances APRA's capacity to take control of a distressed ADI or insurer and/or relevant parts of its group, subject to certain pre-conditions and safeguards, including amendments to:

- enhance APRA's statutory management powers in respect of ADIs, including new statutory management powers in relation to foreign ADIs;
- provide APRA with new statutory management powers in respect of insurers;
- provide APRA with new statutory management powers in respect of authorised non-operating holding companies (NOHCs) of regulated entities, and domestically incorporated subsidiaries of authorised NOHCs or regulated entities;
- enhance the moratorium provisions with respect to the statutory and judicial management provisions of the Industry Acts; and
- enhance the statutory immunity provisions applying to statutory and judicial managers.

Directions powers

1.25 Directions powers enable APRA to compel a regulated entity to take specific action to address particular prudential issues that have been identified. Directions powers may also be necessary to limit further deterioration in the financial condition of a regulated entity in a period of emerging stress, and to facilitate the resolution of a distressed regulated entity.

1.26 Refining and, where appropriate, enhancing the triggers that allow the issue of directions will help ensure that APRA can respond in a more timely and decisive way to emerging prudential concerns that affect an entity. Equally, broadening the scope of the directions powers, both in respect of the matters on which directions may be given and the entities to which directions may be given, will assist APRA to respond effectively and promptly to resolve a distressed regulated entity.

1.27 It is important that an entity, its directors or other officers are able to implement a direction from APRA without potential conflicts of duties that may give rise to delay, or impede the effectiveness of the direction, particularly in a crisis. Introducing a specific immunity provision for an entity, its directors and management when complying with an APRA direction will help address this issue.

1.28 This Bill enhances the scope and efficacy of APRA's existing directions powers, including amendments to:

- extend APRA's ability to issue directions to subsidiaries of authorised NOHCs and subsidiaries of regulated entities;
- clarify the scope of APRA's 'catch-all' directions power;
- clarify that APRA may issue directions requiring entities to take specified actions to facilitate resolution, whether in normal times or during a crisis;
- clarify that APRA may give directions despite external support being in place;
- extend APRA's ability to issue a recapitalisation direction to a regulated entity's authorised NOHC and certain other holding companies;
- harmonise recapitalisation directions powers with general directions powers;
- ensure that complying with an APRA direction will not be grounds for an entity, its directors or management to be held liable under any other law (subject to a good faith and reasonableness test);
- harmonise the protection from liability provisions in the Industry Acts; and
- provide for APRA to determine that the giving of a direction should be confidential in certain circumstances.

Transfer powers

1.29 The compulsory transfer of business powers in the Transfer Act are an important tool in APRA's crisis resolution toolkit. The Transfer Act enables some or all of the business of a regulated entity (including assets, liabilities, legal rights and obligations, data and systems) to be transferred to another regulated entity in the same category.

1.30 By international standards, the existing Transfer Act provides a comprehensive framework for compulsory transfers of business in resolution. However, there are certain areas in which the provisions could be enhanced to provide APRA with greater flexibility and certainty when arranging a compulsory transfer. For example, in some situations, rather than transferring all of the assets and liabilities comprising the business of

a regulated entity, it may be more expedient to transfer ownership in the shares of the failed entity.

1.31 The Bill improves APRA's ability to implement a transfer under the Transfer Act, including amendments to:

- enable APRA to compulsorily transfer the shares in a failing regulated entity to another body corporate;
- widen the scope of Part 4 of the Transfer Act to apply to related entities of insurers; and
- remove the requirement for complementary State or Territory legislation to be in place in relation to transfers of business.

Conversion and write-off of capital instruments

1.32 APRA's prudential standards require regulated entities to maintain minimum levels of regulatory capital. The prudential standards currently establish three categories of regulatory capital – Common Equity Tier 1 (CET1), Additional Tier 1 (AT1) and Tier 2 (T2) capital. AT1 and T2 capital instruments comprise securities (for example, preference shares and subordinated notes) that satisfy the eligibility criteria for AT1 and T2 capital set out in APRA's prudential standards.

1.33 APRA's prudential framework provides for two mechanisms by which AT1 and T2 capital instruments may absorb losses: conversion of those instruments into ordinary shares (or equivalent for mutually-owned ADIs), or the write-off of the instruments.

1.34 The amendments summarised below ensure that these conversion and write-off provisions operate as intended, notwithstanding any legal impediments. These proposals were developed following consultation on the Government's 2014 consultation paper 'Providing Certainty for Contractual Loss Absorption Provisions in Regulatory Capital'.

1.35 The Bill amends the Industry Acts to provide increased certainty in relation to the conversion and write-off of capital instruments, including amendments to provide that:

- conversion or write-off can happen despite any impediment there may be in:
- any domestic or foreign law (other than, for conversion, any laws specified in the amendments or regulations made for that purpose, including laws applying to holdings in

companies under Chapter 6 of the Corporations Act or under the *Financial Sector (Shareholdings) Act 1998*);

- the constitution of the entity that has issued the instrument or of an entity that is a party to the instrument and, for conversion, the constitution of the entity into whose shares the instrument converts (if different);
- any contract or arrangement to which the issuing entity, or an entity that is a party to the instrument, is a party and (for conversion) to which the entity into whose shares the instrument converts (if different) is a party;
- any listing rules or operating rules of a financial market in whose official list the issuing entity, an entity that is a party to the instrument, or (for conversion), the entity into whose shares the instrument converts (if different), is included;
- any operating rules of a clearing and settlement facility through which the instrument is traded; and
- a stay provision applies to contractual close-out rights that may arise as a result of the conversion or write-off of a capital instrument or the making of a determination by APRA that results in a requirement for the conversion or write-off of a capital instrument.

Stay provisions

1.36 An important aspect of the resolution regime is the operation of the stay provisions located in the Industry Acts and the Transfer Act. These provisions prevent counterparties of a failing entity from taking action on the grounds of APRA exercising its powers (including directions, recapitalisation directions, statutory and judicial management and transfer powers) in respect of the entity. This is important in ensuring that pre-emptive actions by counterparties do not impede the ability for APRA to implement an orderly resolution.

1.37 Given the amendments noted above to extend the scope of certain powers to group entities, the Bill enhances the stay provisions to ensure that the exercise of crisis powers by APRA does not give rise to termination or other legal rights in contracts of entities within the same relevant group of bodies corporate (a group comprising an ADI/insurer and its subsidiaries or an authorised NOHC and its subsidiaries).

1.38 A further important element of the resolution regime is the interaction of the stay provisions with the PSN Act. The PSN Act

overrides a range of laws in order to ensure the validity of certain provisions relating to netting and the payments systems covered by the PSN Act. Consequential amendments are made to the PSN Act to take into account enhancements to the stay provisions, the moratorium provisions for statutory and judicial management, and the extension of certain powers to group entities. This is intended to ensure that current protections under the PSN Act are retained and the rights of counterparties to close-out netting contracts, and other arrangements covered by the PSN Act, are clear.

1.39 The Bill enhances the stay provisions, and makes consequential amendments to the PSN Act, including amendments to:

- ensure that an exercise of a power in relation to an entity does not give rise to termination rights or other rights (that is, denying an obligation, accelerating a debt, closing-out on a transaction, or enforcing a security) in contracts of entities within the same relevant group of bodies corporate (that is, any group comprising the ADI or insurer and its subsidiaries or an authorised NOHC and its subsidiaries);
- ensure that the current protections afforded to counterparties to certain close-out netting contracts under the PSN Act are retained (with appropriate amendments to take into account stays applying to cross-default rights); and
- set out the relationship between the enhanced moratorium provisions for statutory and judicial management and the PSN Act, as appropriate.

Foreign branches

1.40 Foreign ADIs in Australia provide a range of important services, such as corporate lending, trade finance, wholesale lending, the provision of risk hedging to ADIs and corporate clients, and securities trading.²

1.41 Foreign insurers also provide important services in the Australian financial system, including providing a significant amount of reinsurance capacity to the Australian general insurance market.

1.42 While some of APRA's existing crisis powers do apply to Australian branches of foreign regulated entities (for example, APRA can

² Foreign ADIs are not permitted to accept retail deposits in Australia, which generally prevents them from accepting initial deposits smaller than \$250,000 from individuals.

apply to the Court for a judicial manager to be appointed to a foreign insurer), certain important powers, including statutory management and transfer powers, either do not apply or their application to foreign branches is currently unclear.

1.43 Given the risks that a distressed foreign regulated entity could pose to depositors or policyholders, or to financial system stability in Australia, the Bill enhances APRA's crisis management powers with respect to foreign ADIs and foreign insurers operating in Australia.

1.44 These enhancements are consistent with the Key Attributes which note that authorities should have resolution powers over local branches of foreign firms and the capacity to use the powers either to support a resolution carried out by a foreign home authority or, in exceptional cases, to take measures on its own initiative.

1.45 In a cross-border context, cooperation between relevant authorities in different jurisdictions will be important in ensuring that powers are applied in an effective and coordinated manner where necessary. Without this, it is possible that powers applied in one jurisdiction will not be recognised in other jurisdictions, leading to uncertainty for relevant stakeholders and a greater risk of disorderly outcomes. APRA will continue to develop its coordination of resolution plans with relevant authorities in other jurisdictions as part of resolution planning where relevant (see 1.58).

1.46 The Bill enhances APRA's ability to respond when a foreign branch may be in distress, including amendments to:

- provide APRA with powers to appoint a statutory manager to the Australian branch of a foreign regulated entity;
- clarify APRA's powers to apply to wind up the Australian branch of a foreign regulated entity;
- harmonise the power to direct a foreign regulated entity not to transfer assets out of Australia across the Industry Acts;
- clarify APRA's powers to implement a voluntary or compulsory transfer of business of the Australian branch of a foreign regulated entity; and
- provide APRA with an explicit power to revoke the authorisation of a foreign regulated entity in Australia if the entity's authorisation is revoked in a foreign country.

Financial Claims Scheme

1.47 The FCS provides an important backstop within Australia's resolution regime. It protects retail depositors and policyholders by providing prompt access to their funds which, in turn, contributes to financial stability, by limiting the propensity for a destabilising 'run' on deposits in the case of ADIs, and more generally by promoting confidence in the financial system.

1.48 The FCS for ADIs provides depositors with a guarantee of their deposits up to a pre-determined cap, which is currently set at \$250,000 per account-holder, per ADI. In the case of general insurers, the FCS provides compensation for most claims up to \$5,000 against a failed general insurer, with claims above \$5,000 also covered for eligible policyholders and certain third parties.

1.49 While the legislative framework for the FCS is broadly consistent with international standards, some of the provisions would benefit from further enhancements. Some of these enhancements were developed following consultation on the then Government's 2011 consultation paper 'Financial Claims Scheme', while others were set out in the 2012 Consultation Paper.

1.50 The Bill makes certain enhancements to the FCS framework, including amendments to:

- establish an additional payment mechanism to enable FCS entitlements to be satisfied when there has been a transfer of deposits to another ADI or policyholder claims to another general insurer;
- enable APRA to obtain information from third parties in relation to the FCS;
- facilitate the effective payout of FCS entitlements to third party claimants of a policyholder of a failed general insurer where the policyholder is in liquidation;
- enable APRA to make interim payments to claimants under the FCS applicable to general insurers;
- grant the Treasurer the discretion to declare the FCS at an earlier time, upon appointment of a statutory manager; and
- reduce the reporting burden regarding withholding tax in relation to interest on amounts paid under the FCS.

Wind-up and other matters

1.51 APRA's winding up powers in the Industry Acts are another important part of the crisis management toolkit, enabling it to act in situations where a regulated entity is insolvent or about to become insolvent. The ability to initiate the winding up of a regulated entity in a timely manner may assist to prevent further financial deterioration, improve outcomes for depositors and policyholders, and minimise impacts on the financial system more broadly.

1.52 While these provisions operate satisfactorily, the application of them in the past has identified areas for enhancement, and there is a lack of uniformity in APRA's powers relating to provisional liquidators and certain external administrators. The Bill therefore strengthens and simplifies APRA's powers in relation to the winding up and external administration of regulated entities under the Industry Acts.

1.53 There are also gaps and a lack of consistency between the Industry Acts in relation to APRA's ability to impose conditions on, or to revoke, an entity's authorisation. The Bill makes amendments to ensure that APRA has appropriate powers to impose conditions and revoke authorisations if certain grounds are met.

1.54 The Bill makes certain enhancements to APRA's winding up powers and powers to impose conditions on, or revoke, authorisations, including amendments to:

- harmonise the Industry Acts with regard to APRA's involvement in external administration of regulated entities;
- ensure that APRA's existing powers in the winding up of a regulated entity extend to where a provisional liquidator is appointed;
- enable APRA to apply for the winding up of an ADI without the ADI having first been placed in statutory management;
- provide APRA with notice of proposed applications for external administration of regulated entities;
- ensure that the institution of offence proceedings is no bar to judicial management or winding up of a regulated entity;
- enhance APRA's ability to impose, vary and revoke conditions of authorisation in certain circumstances; and

- enable APRA to revoke authorisations on certain additional grounds under the Industry Acts.

Resolution planning

1.55 In addition to having a wide and flexible set of powers through which to intervene in a crisis, it is important APRA has clear powers to set appropriate prudential requirements for resolution planning, and to address potential barriers to the orderly resolution of a regulated entity, during normal times.

1.56 An important lesson from the global financial crisis was that effective resolution requires an advanced level of preparedness through contingency planning, before a failure or crisis event materialises. This has been reflected in the increased international focus on recovery and resolution planning, including in the Key Attributes and in BCBS and IAIS core principles.

1.57 The Bill clarifies the legislative framework for resolution planning by incorporating appropriate references within APRA's prudential standard-making powers (and matters for which regulations may be made) under the Industry Acts. It also includes amendments to clarify APRA's ability to require regulated entities and their groups to take actions to address potential barriers to orderly resolution (see 1.25 to 1.28).

1.58 In a cross-border context, resolution planning will include working with authorities in other jurisdictions to enable resolution actions to be applied in a coordinated manner where appropriate. Without this, there is a risk that APRA's resolution powers (and other related provisions in the Bill) may have reduced effectiveness on a cross-border basis or may conflict with the actions or requirements of authorities in other jurisdictions. Such coordination is consistent with APRA's current approach of working closely with supervisors in other jurisdictions where relevant.

1.59 The Bill makes amendments to strengthen the legislative framework for resolution planning, including amendments to:

- refine and harmonise the definition of 'prudential matters' in the Industry Acts (which includes inserting a definition of this term in the Life Insurance Act for the first time);
- clarify which entities must comply with prudential standards; and

- enable APRA to require a holding company to ensure a regulated entity has an authorised NOHC, where appropriate.

Application and transitional provisions

1.60 The provisions of this Bill will generally apply from the date of Royal Assent. In some cases there are special application provisions which are identified where relevant.

Chapter 2

Statutory and judicial management

Outline of chapter

2.1 Schedules 1-3, 5 and 6 to this Bill amend the Industry Acts, the PSN Act and the APRA Act to enhance APRA's powers related to the statutory and judicial management of regulated entities, authorised NOHCs, and subsidiaries thereof.

Context of amendments

2.2 Statutory and judicial management are existing powers in APRA's crisis resolution toolkit. APRA can appoint itself or a third party to take control of an ADI under statutory management, and can apply to the Court for the appointment of a judicial manager to take control of an insurer. Where a statutory or judicial manager is appointed to an entity, it replaces the board of directors and takes control of the entity.

2.3 Statutory and judicial management are important tools for dealing with a financial institution in acute distress. APRA may need to use these powers to take control of an entity in cases where it does not have confidence that the board and management is capable of resolving a crisis satisfactorily, or where the board and management are mismanaging the entity, including where it is insolvent or near insolvent.

2.4 The appointment of a statutory or judicial manager can help stabilise a failing entity, so that steps can be taken to implement an orderly resolution in a way that protects the interests of depositors and policyholders, and maintains financial system stability. Depending on the circumstances, this could include maintaining some or all of the entity as a going concern, recapitalising the entity, facilitating the transfer of some or all of the business to another entity, or putting the entity into partial or complete wind-up (with declaration of the FCS where relevant).

2.5 Given the high level of intervention which it involves, statutory and judicial management would generally be used as a measure of last resort. To date, no statutory manager has been appointed to an ADI, reflecting the long period of financial stability that Australia has enjoyed. In the case of insurers, the Court has only appointed a judicial manager on

APRA's application on two occasions. Both instances involved small general insurers that had been in run-off for many years (that is, they were unable to write any new insurance business).

2.6 This Bill enhances the legislative framework underpinning the statutory and judicial management regimes to ensure their effective operation in a crisis situation, including providing for the appointment of a statutory manager to an insurer in certain special circumstances, and extending the scope of statutory management to authorised NOHCs of a regulated entity and domestically incorporated subsidiaries of an authorised NOHC or regulated entity, to address the resolution of groups, in each case subject to appropriate pre-conditions and safeguards.

2.7 Under the Insurance and Life Insurance Acts, APRA may apply to the Federal Court for the appointment of a judicial manager to assume control of an insurer where certain statutory preconditions are met, such as where an insurer has failed to comply with a prudential standard or a direction from APRA, or is in financial distress. In contrast, under the Banking Act, it is APRA that appoints a statutory manager to an ADI without application to the Court.

2.8 While applying to the Court for the appointment of a judicial manager is likely to represent an appropriate resolution tool for a failing insurer in most circumstances, there may be specific situations where APRA needs the ability to appoint a statutory manager to an insurer. In particular, this could be the case where the insurer is large or part of a complex financial group, or its distress poses a risk to the financial system or economy, so that a more rapid resolution response may be needed.

2.9 In relation to groups, the global financial crisis demonstrated that it is particularly difficult to ensure the effective resolution of a failing entity that is part of a wider group of companies. The structures of financial groups can be complex, involving numerous business lines and support services linked through different ownership and contractual arrangements. It may not be clear exactly how the different members of a group are linked by inter-dependencies, for example through the provision of critical intra-group services, or where the risks and control in a group ultimately lie.

2.10 Understanding the position of the failing regulated entity, disentangling its affairs from those of the rest of the group, and ensuring it can be resolved quickly and effectively present considerable challenges. In the absence of effective group resolution powers, it may be particularly difficult to resolve a distressed regulated entity or group quickly and effectively.

2.11 Extending the statutory management regime to apply to insurers in certain circumstances, and to address the resolution of groups, is consistent with relevant international standards on resolution regimes. The Key Attributes note the need for resolution powers to apply to relevant group entities, and were updated in 2014 to include sector-specific guidance on the resolution of insurers. The BCBS and IAIS have also taken steps to incorporate the Key Attributes into their standards.

2.12 Other amendments include new powers to appoint a statutory manager to the Australian business of a foreign ADI or insurer (see Chapter 7 for further details), and enhanced moratorium and immunity provisions in respect of statutory and judicial management. In recognition that the use of statutory management powers could affect third party rights, including those of creditors, the Bill also introduces certain new preconditions and safeguards as appropriate.

Summary of new law

2.13 Schedules 1-3, 5 and 6 to this Bill amends the Industry Acts, the PSN Act and APRA Act to:

- enhance APRA’s statutory management powers in respect of ADIs, including new statutory management powers in relation to foreign ADIs;
- provide APRA with new statutory management powers in respect of insurers;
- provide APRA with new statutory management powers in respect of authorised NOHCs of regulated entities, and domestically incorporated subsidiaries of authorised NOHCs or regulated entities;
- enhance the moratorium provisions with respect to the statutory and judicial management provisions of the Industry Acts; and
- enhance the statutory immunity provisions applying to statutory and judicial managers.

2.14 The Bill also includes a number of other technical amendments to the Industry Acts in relation to statutory and judicial management, to:

- ensure that the Insurance and Life Insurance Acts prevail over the Corporations Act to the extent of any inconsistency (as is already the case under the Banking Act);
- confirm that the PGPA Act does not apply to an entity under the control of a statutory manager;
- clarify that APRA can replace a statutory manager and provide APRA with standing to apply for the replacement of a judicial manager with another person;
- confirm that more than one person can be appointed as a statutory or judicial manager;
- clarify the effect of the appointment of a judicial manager to an insurer on the directors and officers of that entity; and
- repeal unnecessary sections in the Insurance and Life Insurance Acts relating to judicial management.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Statutory management of group entities</i>	
APRA may, in certain circumstances, appoint a statutory manager to take control of an authorised NOHC of a regulated entity, or a domestically incorporated subsidiary of an authorised NOHC or regulated entity. APRA will continue to have power to appoint a statutory manager to an ADI.	APRA may, in certain circumstances, appoint a statutory manager to an ADI. APRA does not have the power to appoint a statutory manager to an authorised NOHC of a regulated entity, or a subsidiary of an authorised NOHC or regulated entity, unless that subsidiary is also an ADI.
<i>Statutory management of insurers</i>	
APRA may, in certain circumstances, appoint a statutory manager to an insurer, an authorised NOHC of an insurer, or a domestically incorporated subsidiary of an authorised NOHC or an insurer(as noted above).	APRA may, in certain circumstances, appoint a statutory manager to an ADI. APRA does not have the power to appoint a statutory manager to an insurer.

<i>New law</i>	<i>Current law</i>
<i>External administration of holding company as a trigger for statutory or judicial management</i>	
<p>A statutory manager may take control of a regulated entity where an external administrator has been appointed to a holding company of the entity.</p> <p>APRA may apply for a judicial manager to be appointed to an insurer where an external administrator has been appointed to a holding company of the insurer.</p>	<p>The appointment of an external administrator to a holding company is not a ground for a statutory manager to take control of a subsidiary ADI.</p> <p>It is also not a ground for APRA to apply for a judicial manager to be appointed to a subsidiary insurer.</p>
<i>Application for appointment of an external administrator to a foreign ADI or foreign insurer as a trigger for statutory or judicial management</i>	
<p>The fact that an appointment of, or an application to appoint, an external administrator to a foreign ADI or foreign insurer (or similar procedure) has been undertaken in a foreign country will be a potential trigger for the appointment of a judicial manager to an insurer or a statutory manager to an ADI or insurer.</p>	<p>The fact that an appointment of, or application to appoint, an external administrator to a foreign ADI or foreign insurer (or similar procedure) has been undertaken in a foreign country is not a specific ground for appointment of an ADI statutory manager or a judicial manager.</p>
<i>Widening the moratorium provisions applicable where a statutory or judicial manager is appointed</i>	
<p>The moratorium provisions for statutory and judicial management have been enhanced to include moratoriums on enforcement processes and disposal of property and to place restrictions on exercise of third party property rights.</p> <p>A supplier of an essential service must not, in certain circumstances, refuse to provide those services while a statutory or judicial manager is in control of the entity's business.</p> <p>These provisions also apply where a statutory manager takes control of an authorised NOHC or a domestically incorporated subsidiary of an authorised NOHC or regulated entity (that is, a target body corporate).</p>	<p>Court proceedings that are not criminal or civil penalty proceedings cannot begin or continue against an ADI or insurer while a statutory or judicial manager is in control of the ADI or insurer's business unless the Court grants leave or APRA consents to the proceedings.</p>

<i>New law</i>	<i>Current law</i>
<i>Banking Act statutory manager not intended to be constrained by subsection 13A(3) of the Banking Act</i>	
The Banking Act is amended to put beyond doubt that a statutory manager is able to manage an ADI's business without being constrained by the operation of subsection 13A(3) (which establishes the priority of certain creditors).	It is unclear whether a Banking Act statutory manager that has taken control of an ADI would be constrained in their actions by subsection 13A(3) which sets out the priorities for application of assets of an ADI in Australia.
<i>Enhanced immunity for statutory and judicial managers</i>	
Enhanced statutory immunities apply to statutory and judicial managers. Statutory and judicial managers are exempt from civil or criminal liability for actions done or not done in the exercise, or purported exercise, of powers, functions, or duties of the statutory or judicial manager under the Industry Acts, except where these actions or omissions are taken in bad faith.	ADI statutory managers are covered by immunity for losses that are not incurred because of fraud, dishonesty, negligence, or wilful failure to comply with the Banking Act. Judicial managers are not subject to any liability to any person in respect of anything done or not done, in good faith in the exercise of the powers, functions or duties of the judicial manager under the Insurance or Life Insurance Acts.
<i>Terminating statutory management of an ADI that remains a going concern</i>	
There is no longer a condition for terminating the statutory management of an entity that deposit liabilities have been paid or APRA is satisfied that they will be paid out. APRA will still need to be satisfied that it is no longer necessary to remain in control of the body corporate's business (for example, because the resolution of the entity has been successfully implemented). (Note that this amendment is concerned with the ultimate termination of the statutory management process, defined as an 'ultimate termination of control', rather than the termination of a particular administrator's appointment (in relation to the latter, see below.)	One of the conditions for the termination of statutory management of an ADI is that deposit liabilities have been paid or APRA is satisfied that they will be paid out, and APRA considers that it is no longer necessary for it or an administrator to remain in control of the body corporate's business.

<i>New law</i>	<i>Current law</i>
<i>Discretion for APRA to terminate appointment of a statutory manager</i>	
<p>In addition to the current law, APRA will be able to terminate the appointment of an administrator where APRA considers that such action is necessary to:</p> <ul style="list-style-type: none"> • facilitate the resolution of the body corporate or its group or group members; or • protect the interests of policyholders or depositors; or • promote financial system stability in Australia. <p>This amendment is concerned with the situation where the appointment of a particular administrator is terminated rather than an ultimate termination of control in relation to the entire statutory management process.</p>	<p>APRA may only terminate the appointment of a particular administrator of an ADI's business where the administrator contravenes a requirement of Division 2 of Part 2 of the Banking Act, or where the terms and conditions of the administrator's appointment provide for termination.</p>
<i>Replacing a statutory or judicial manager</i>	
<p>Where APRA terminates an administrator's appointment (as distinct from an ultimate termination of statutory management control of the entity), APRA may appoint a replacement (which might mean appointing itself).</p> <p>APRA may apply to the Court for the cancellation of a judicial manager's appointment.</p>	<p>APRA does not currently have explicit power to appoint a replacement statutory manager, and does not have standing to apply to the Court for the cancellation of a judicial manager's appointment.</p>
<i>Application of legislation during statutory management</i>	
<p>The provisions of the Industry Acts and FSCODA will continue to apply to an entity under statutory management.</p> <p>The amendments also ensure that the PGPA Act does not apply to an entity if that entity's business is controlled by a statutory manager.</p>	<p>The Banking Act provides that the obligations on ADIs and the continuing operation of the Banking Act and FSCODA in relation to ADIs are unaffected by the appointment of an administrator to, or the fact that a statutory manager is in control of, an ADI's business.</p> <p>It is unclear if the PGPA Act applies in relation to an ADI under statutory management.</p>

<i>New law</i>	<i>Current law</i>
<i>Clarifying the effect of judicial management on officers and the board</i>	
When a judicial manager is appointed to an insurer, the existing officers (within the meaning of the Corporations Act) of the insurer cease to have the powers of an officer with respect to that insurer, and the judicial manager gains the powers and functions of the board of directors of the insurer, including the board's powers of delegation. Any purported act by an officer who ceased to have the powers and functions of an officer is invalid and of no effect.	When a judicial manager is appointed to an insurer, the scope of the judicial manager's powers is unclear. It is also unclear whether directors and officers of an insurer continue to have powers and functions with respect to the management of the insurer under judicial management.
<i>Clarifying the law regarding multiple statutory/judicial manager appointments</i>	
Provisions have been included to clarify that multiple individuals may be appointed as statutory or judicial managers, and consequential amendments are made to allow references to an individual statutory or judicial manager in the Industry Acts to be interpreted as a reference to any one of the statutory or judicial managers appointed to an entity.	APRA's powers regarding the appointment of multiple statutory managers are unclear. The Court's powers regarding the appointment of multiple judicial managers are also unclear.
<i>Amending the definition of 'subsidiary' under the Insurance Act to align with the Banking Act and Life Insurance Act</i>	
Under the Insurance Act, a company is defined as a subsidiary if its holding company is in a position to cast, or control the casting of, more than 50 per cent (the threshold percentage) of the maximum number of votes that might be cast at a general meeting of the company, or holds more than 50 per cent of the issued share capital of the company.	Under the Insurance Act, a company is defined as a subsidiary if its holding company is in a position to cast, or control the casting of, more than 25 per cent (threshold percentage) of the maximum number of votes that might be cast at a general meeting of the company, or holds more than 25 per cent of the issued share capital of the company. In contrast, under the Banking Act and Life Insurance Act, the threshold percentage is 50 per cent.

<i>New law</i>	<i>Current law</i>
<i>Insurance and Life Insurance Acts to have effect despite the Corporations Act</i>	
The Insurance and Life Insurance Acts have effect despite the Corporations Act where there is a conflict between the provisions of those Acts.	It is unclear whether the Insurance Act or Life Insurance Act have priority over the Corporations Act where there is a conflict between the provisions of those Acts. By contrast, the Banking Act states that in the event of an inconsistency between the Banking Act and Corporations Act, the provisions in the Banking Act will prevail to the extent of the inconsistency.

Detailed explanation of new law

General provisions

2.15 The Bill expands the existing statutory management regime for ADIs to apply to related bodies corporate of the regulated entity in certain circumstances. This expanded statutory management regime under the Banking Act is then adapted into the Insurance and Life Insurance Acts (see 2.41 to 2.43) so that a statutory manager can now be appointed to a regulated entity, its authorised NOHC, and a domestically incorporated subsidiary of the authorised NOHC or a subsidiary of the regulated entity.

2.16 For ease of reading, the Explanatory Memorandum will first address the amendments applying the statutory management regime to related bodies corporate in the Banking Act, followed by an explanation of how the newly expanded Banking Act statutory management regime is transposed into the Insurance and Life Insurance Acts. Cross-references to the equivalent new provisions of the Insurance and Life Insurance Acts in the Schedules to the Bill are included below for ease of reference.

Statutory management of group entities

Definitions – related body corporate

2.17 The Bill inserts a new definition of ‘related body corporate’. It is defined as a body corporate that is related to the first-mentioned body corporate. For the purposes of the Banking Act, this is determined in the same way as the Corporations Act. *[Schedule 1, items 10 and 11, subsections 5(1) and 5(2A) of the Banking Act; Schedule 2, items 7 and 8, subsections 3(1) and*

section 4B of the Insurance Act; Schedule 3, item 115, of the Schedule Dictionary of the Life Insurance Act]

2.18 This new definition is used throughout the Banking Act, including in the provisions that place safeguards on the exercise of a statutory manager's powers and functions (see 2.34 to 2.40).

Definitions – Banking Act statutory manager

2.19 The Bill repeals the definition of 'ADI statutory manager' and inserts a new definition of 'Banking Act statutory manager'. *[Schedule 1, items 1 and 4, subsection 5(1) of the Banking Act]*

2.20 A Banking Act statutory manager is either APRA (where it is in control) or an administrator appointed by APRA to control an entity under the Banking Act. *[Schedule 1, item 65, subsection 13A(2) of the Banking Act]*

2.21 The reason for the change in definition is that, as a result of the amendments in the Bill, it will be possible to appoint a statutory manager to not only an ADI but also an authorised NOHC or a domestically incorporated subsidiary of an ADI or authorised NOHC under the Banking Act. The term 'ADI statutory manager' is therefore no longer appropriate.

Definitions – target body corporate and relevant ADI

2.22 The Bill amends section 13A of the Banking Act, which currently provides for statutory management of only ADIs, to extend the statutory management regime to authorised NOHCs and domestically incorporated subsidiaries of authorised NOHCs and ADIs. The amendments allow APRA to appoint a statutory manager to a 'target body corporate' that is incorporated in Australia in certain circumstances. *[Schedule 1, item 65, subsection 13A(1B) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(3) of the Insurance Act; Schedule 3, item 52, subsection 179AA(3) of the Life Insurance Act]*

2.23 The term 'relevant ADI' is defined with respect to its relationship to the target body corporate. For example, if a Banking Act statutory manager takes control of an authorised NOHC, the ADI subsidiary of that authorised NOHC, in connection with which the appointment was made, would be the 'relevant ADI'.

2.24 The Bill also allows regulations to exclude the kinds of entities specified in the regulations from the scope of the statutory management regime. For example, regulations might carve out entities that are regulated under other legislation and subject to a bespoke external administration regime. *[Schedule 1, item 65, paragraph 13A(1B)(d) of the Banking*

Act; Schedule 2, item 58, paragraph 62ZOA(3)(d) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(3)(d) of the Life Insurance Act]

Pre-conditions to appointing a statutory manager to target entities

2.25 The Bill provides that APRA may take control of a target body corporate or appoint an administrator to take control of a target body corporate in certain circumstances. *[Schedule 1, item 65, subsection 13A(1C) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(4) of the Insurance Act; Schedule 3, item 52, subsection 179AA(4) of the Life Insurance Act]*

2.26 The Bill amends section 13A of the Banking Act to set out the circumstances where a Banking Act statutory manager may take control of a target body corporate. *[Schedule 1, item 65, subsections 13A(1B), 13A(1E) and 13A(1F) of the Banking Act]*

2.27 A Banking Act statutory manager may take control of a target body corporate if:

- APRA has appointed a statutory manager to the relevant ADI, or has a statutory basis and intention to do so; and
- the target body corporate provides services or conducts functions or business considered essential to maintain the operations of the relevant ADI. *[Schedule 1, item 65, subsection 13A(1D) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(5) of the Insurance Act; Schedule 3, item 52, subsection 179AA(5) of the Life Insurance Act]*

2.28 Group entities may perform services or functions that are essential to the operation of the relevant ADI, including for example IT and human resource functions, treasury and corporate services, custodial services, funding and other specialist financial services. Further, groups can be structured so that entities in the group may hold assets or liabilities on behalf of each other, including the relevant ADI. Subject to the relevant pre-conditions being met, APRA may take control of such a target body corporate, enhancing APRA's ability to stabilise the operations of the relevant ADI in a crisis situation.

2.29 The Bill also permits a Banking Act statutory manager to take control of a target body corporate where:

- APRA has appointed a statutory manager to the relevant ADI, or has a statutory basis and intention to do so; and
- APRA considers that it is necessary for a Banking Act statutory manager to take control of the target body corporate to facilitate the resolution of the relevant ADI, an authorised NOHC of the relevant ADI, a 'relevant group of bodies

corporate' of which the relevant ADI is a member, or a member or members of such a group. The term 'resolution' is further explained at Chapter 10. *[Schedule 1, item 65, subsection 13A(1E) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(6) of the Insurance Act; Schedule 3, item 52, subsection 179AA(6) of the Life Insurance Act]*

2.30 A 'relevant group of bodies corporate' is defined in existing section 5 of the Banking Act as either the group comprising an ADI and its subsidiaries together or the group comprising an authorised NOHC and its subsidiaries together.

2.31 A Banking Act statutory manager may also take control of a target body corporate where:

- an external administrator has been appointed to the target body corporate, or APRA considers that, in the absence of external support, the target body corporate may become unable to meet its obligations or may suspend payment; and
- APRA considers that it is necessary for a Banking Act statutory manager to take control of the target body corporate to enable the relevant ADI to maintain its operations, or to facilitate the resolution of the relevant ADI, an authorised NOHC of the relevant ADI, a relevant group of bodies corporate of which the relevant ADI is a member, or a particular member or members of such a group. *[Schedule 1, item 65, subsection 13A(1F) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(7) of the Insurance Act; Schedule 3, item 52, subsection 179AA(7) of the Life Insurance Act]*

2.32 This is intended to address the circumstances where the appointment of an external administrator to an entity in the group, or more generally the financial distress of such an entity, may cause or exacerbate distress in the relevant ADI. This could arise through a number of channels, including as a result of adverse contagion impacts to the relevant ADI, or through interruption to essential services provided to the relevant ADI by the target body corporate.

2.33 This provision also allows APRA to co-ordinate resolution of the relevant ADI, including the continued provision of appropriate services within the group, in circumstances where this might be frustrated if an external administrator of another kind is appointed with conflicting duties. *[Schedule 1, item 65, subsection 13A(1F) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(7) of the Insurance Act; Schedule 3, item 52, subsection 179AA(7) of the Life Insurance Act]*

Safeguards on the powers and functions of a statutory manager of a target body corporate

2.34 The amendments provide safeguards in relation to the use of a Banking Act statutory manager's powers and functions for certain target bodies corporate. These are intended to provide additional protections for the interests of relevant stakeholders (for example, shareholders and creditors) of the target body corporate or other entity in the group. *[Schedule 1, item 131, section 14AAA of the Banking Act; Schedule 2, item 58, section 62ZOE of the Insurance Act; Schedule 3, item 52, section 179AE of the Life Insurance Act]*

2.35 The first safeguard generally requires the Banking Act statutory manager to consider fair value where performing or exercising its powers and functions to require the provision of services to or by the target body corporate.

2.36 Specifically, this section prevents the provision of services between related bodies corporate or transfer of assets (including cash or other funds) between the entity under management and another entity in the group in certain circumstances. The prohibition will not apply if:

- the supply or transfer is made for fair value; or
- the supply or transfer occurs under a binding arrangement that existed before the statutory management; or
- in the case of an asset transfer (including a transfer of cash or other funds), if it was in the ordinary course of business; or
- in the case of a transfer of funds, the shareholders of the body corporate have agreed by ordinary resolution to that use of the funds (see 2.39) *[Schedule 1, item 131, section 14AAA of the Banking Act; Schedule 2, item 58, section 62ZOE of the Insurance Act; Schedule 3, item 52, section 179AE of the Life Insurance Act]*

2.37 As noted, in relation to this safeguard, the statutory manager may rely on existing binding arrangements (such as intra-group arrangements) that existed before its appointment whether or not at fair value, or to otherwise only make new arrangements which are for fair value.

2.38 The second safeguard prevents the use of a Banking Act statutory manager's powers and functions over an authorised NOHC of an ADI where:

- the performance or the exercise requires using funds of the authorised NOHC or a subsidiary of the authorised NOHC to

increase the level of capital of the relevant ADI to a specified level; and

- the shareholders of the authorised NOHC have not agreed, by ordinary resolution, to that use of the funds. *[Schedule 1, item 131, subsection 14AAA(3) of the Banking Act, Schedule 2, item 58, subsection 62ZOE(3) of the Insurance Act; Schedule 3, item 52, subsection 179AE(3) of the Life Insurance Act]*

2.39 In this subsection, the term ‘ordinary resolution’ refers to the ordinary meaning of the term in company law – generally, this means an ordinary resolution that is passed by a majority of votes cast by shareholders of the company entitled to vote on the resolution at the meeting in person or by proxy (if proxies are allowed).

2.40 This amendment does not prevent a statutory manager of an authorised NOHC from using funds of the authorised NOHC to increase the level of capital of the relevant ADI, where those funds were raised following the exercise of the statutory manager’s power to facilitate a recapitalisation under section 14AA (as amended by the Bill) of the Banking Act .

Statutory management of insurers

2.41 The Bill amends the Insurance and Life Insurance Acts to create a statutory management regime for insurers.

2.42 The statutory management regimes in the Insurance and Life Insurance Acts are intended to substantially align with the Banking Act (as amended by this Bill) where appropriate. This includes applying the expanded statutory management regime for ADIs (and related body corporates) detailed at 2.17 to 2.40 (with relevant modifications) to insurers and their related bodies corporate. This means that a statutory manager can now be appointed to an insurer, its authorised NOHC, and a domestically incorporated subsidiary of the authorised NOHC or insurer, with appropriate safeguards. *[Schedule 2, item 58, sections 62ZOA to 62ZOZ, 62ZOZA and 62ZOZB of the Insurance Act; Schedule 3, item 52, sections 179AA to, 179AZ, 179AZA and 179AZB of the Life Insurance Act]*

2.43 There are some important differences with respect to statutory management between the Industry Acts, in particular in relation to the circumstances in which a statutory manager can take control of an insurer, as explained below.

Power to take control of an insurer

2.44 The Bill empowers APRA to appoint a statutory manager to an insurer, an authorised NOHC of an insurer, and a domestically incorporated subsidiary of an authorised NOHC or insurer in certain circumstances. *[Schedule 2, item 58, section 62ZOA) of the Insurance Act; Schedule 3, item 52, section 179AA) of the Life Insurance Act]*

2.45 The Bill amends the Insurance and Life Insurance Acts to provide for the pre-conditions that must be satisfied in order for APRA to appoint a statutory manager to a general insurer or life insurer *[Schedule 2, item 58, section 62ZOA of the Insurance Act; Schedule 3, item 52, section 179AA of the Life Insurance Act]*

2.46 These require that APRA be satisfied that at least one of the grounds for appointing a judicial manager to an insurer be met (see sections 62L and 62M of the Insurance Act, and sections 158 and 159 of the Life Insurance Act, as amended) and further statutory management pre-conditions are met. *[Schedule 2, item 58, paragraph 62ZOA(1)(a) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(1)(a) of the Life Insurance Act]*

2.47 Under the existing law, the Court has power to appoint a judicial manager under section 62L of the Insurance Act or section 159 of the Life Insurance Act if APRA has undertaken a formal investigation of the insurer and, having regard to the results of the investigation, it is in the interests of policyholders that the order be made. The Court also has power to appoint a judicial manager under section 62M of the Insurance Act or section 159 of the Life Insurance Act if, in general terms, the insurer is in financial difficulty or something has occurred that may threaten its position, or it has defaulted in compliance with a regulatory requirement. Under sections 62M of the Insurance Act and 159 of the Life Insurance Act, the Court must also consider that the time needed to make or complete an investigation of the insurer would be likely to prejudice the interests of policyholders.

2.48 Note that the Bill separately makes amendments to sections 62M of the Insurance Act and 159 of the Life Insurance Act in relation to the grounds for appointment of a judicial manager in situations where an investigation has not been undertaken; see 2.69.

2.49 Specifically, in addition to being satisfied that a ground exists for the appointment of a judicial manager, APRA must also be satisfied that one of five further conditions (or triggers) is met in order for an Insurance Act statutory manager or a Life Insurance Act statutory manager to be appointed to a general insurer or life insurer respectively. These further pre-conditions reflect the fact that judicial management is likely to remain an appropriate means of resolving a failing insurer in most circumstances, whereas statutory management is only expected to be

used where further specific pre-conditions are met. *[Schedule 2, item 58, subsection 62ZOA(1) of the Insurance Act; Schedule 3, item 52, subsection 179AA(1) of the Life Insurance Act]*

2.50 The five triggers for the appointment of an Insurance Act statutory manager or a Life Insurance Act statutory manager require that APRA be satisfied that:

- an Australian financial sector statutory manager (or AFS statutory manager) has taken control of a related body corporate to the insurer (for example, a Banking Act statutory manager has been appointed to a related ADI to the insurer); or
- the insurer's financial position is deteriorating rapidly or is likely to deteriorate rapidly, and failure to respond quickly to the deterioration would be likely to prejudice policyholders of the insurer; or
- it is likely that the insurer will be unable to carry on insurance business in a way that is consistent with the stability of the financial system in Australia; or
- an external administrator has been appointed to a holding company of the insurer (or a similar appointment has been made in a foreign country in respect of such a holding company) and the appointment poses a significant threat to the operation or soundness of the insurer, the interests of policyholders of the insurer, or the stability of the financial system in Australia; or
- if the insurer is a foreign insurer:
 - an application for the appointment of an external administrator (or for a similar procedure) has been made in a foreign country); or
 - an appointment of an external administrator to the foreign insurer (or a similar appointment has been made) in a foreign country.

[Schedule 2, item 58, subsection 62ZOA(2) of the Insurance Act; Schedule 3, item 52, subsection 179AA(2) of the Life Insurance Act]

2.51 The term ‘AFS statutory manager’ is defined in the Insurance and Life Insurance Acts as a Banking Act statutory manager under the Banking Act, an Insurance Act statutory manager under the Insurance Act, or a Life Insurance Act statutory manager under the Life Insurance Act. *[Schedule 2, item 1, subsection 3(1) of the Insurance Act; Schedule 3, item 110, Schedule Dictionary of the Life Insurance Act]*

2.52 The first trigger above addresses circumstances where a statutory manager has been (or will be) appointed to another entity in the same group as the insurer; for example, an ADI. The fact that a statutory manager has been appointed to another entity in the group will often be indicative of wider group problems requiring co-ordinated resolution. In these situations, rather than having both a statutory manager and a judicial manager in place within the same group, it may be desirable to have the same person in charge of the different entities in the group, appointed under the same or similar terms of engagement, and subject to directions from APRA. However, depending on the particular circumstances, it is also possible that APRA may choose to appoint different statutory managers, or to apply for the Court to appoint a judicial manager, to different entities in the group. *[Schedule 2, item 58, paragraph 62ZOA(2)(a) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(a) of the Life Insurance Act]*

2.53 The second trigger addresses circumstances where the deterioration or likely deterioration of an insurer’s financial position is rapid enough to warrant a quicker and more certain means of stabilising the insurer, and implementing a resolution, than applying to the Court for appointment of a judicial manager. Speed of action and certainty could be particularly important in situations where an insurer’s financial condition is deteriorating rapidly, such as where it is part of a financial group and is adversely affected by intra-group contagion. *[Schedule 2, item 58, paragraph 62ZOA(2)(b) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(b) of the Life Insurance Act]*

2.54 The third trigger addresses circumstances where an insurer may conduct activities that are sufficiently critical to the stability of the Australian financial system (and potentially the real economy) that the financial distress of the insurer requires rapid action to be taken in the interests of financial stability. *[Schedule 2, item 58, paragraph 62ZOA(2)(c) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(c) of the Life Insurance Act]*

2.55 The fourth trigger addresses circumstances where an appointment of an external administrator to a holding company of a insurer has the potential to trigger contagion impacts within the group, which could lead to or exacerbate distress in the insurer. The Bill also inserts this trigger in the Banking Act (see 2.59 to 2.65 for more detail). *[Schedule 1, item 64, paragraph 13A(1)(d) of the Banking Act, Schedule 2, item 58, paragraph 62ZOA(2)(d) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(d) of the Life Insurance Act]*

2.56 The fifth trigger applies only to foreign insurers and applies where:

- an application for the appointment of an external administrator in a foreign jurisdiction or jurisdictions, or for a similar procedure, has been made in a foreign jurisdiction; or
- an external administrator has been appointed, or a similar appointment has been made, in a foreign jurisdiction.

2.57 This trigger captures situations where, for example, a court process has been commenced in foreign jurisdictions for an appointment of an external administrator, or a foreign regulator has directly appointed an external administrator or similar person, or a secured creditor has appointed an external administrator under a deed or contract. See 2.66 to 2.68 for more detail. *[Schedule 2, item 58, paragraph 62ZOA(2)(e) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(e) of the Life Insurance Act]*

2.58 As described above, the statutory management regimes for the Insurance and Life Insurance Act will include the power to appoint a statutory manager to target bodies corporate of the relevant insurer (see 2.25 to 2.36), subject to the same preconditions and safeguards on these powers described at 2.34 to 2.40.

Other reforms to the statutory and judicial management frameworks

Appointment of external administrator to holding company as grounds for taking control of a regulated entity

2.59 In a situation where an external administrator (for example, a liquidator or receiver) is appointed to a holding company of a regulated entity, this has the potential to trigger contagion impacts within the group that could lead to or exacerbate distress in the regulated entity. In particular, the appointment of an external administrator to a holding company may adversely affect the financial condition or orderly resolution of regulated entities that are subsidiaries of the holding company. This is because the external administrator of the holding company may take actions, through the holding company, that affect those subsidiaries of the holding company.

2.60 In these circumstances, it may be necessary for APRA to move quickly to assume control of the subsidiary regulated entity via statutory management, or to apply to the Court for the appointment of a judicial manager to the regulated entity (where it is an insurer), where the holding company's external administration presents serious risks to the regulated entity.

2.61 As such, the Bill provides an additional trigger for the appointment of a statutory manager to a regulated entity. This provides that a Banking Act statutory manager can be appointed to take control of a regulated entity's business where the regulated entity is a subsidiary of a holding company and an external administrator has been appointed to the holding company (or a similar appointment has been made in a foreign country in respect of such a holding company). As noted above, an equivalent trigger is included in the new statutory management regime for insurers in the Insurance Act and Life Insurance Act

2.62 This trigger is subject to the further condition that APRA be satisfied that the appointment of an external administrator (or similar person) to the holding company poses a significant threat to either:

- the operation or soundness of the regulated entity; or
- the interests of depositors or policy holders of the regulated entity; or
- the stability of the financial system in Australia. *[Schedule 1, item 64, paragraph 13A(1)(d) of the Banking Act; Schedule 2, item 58, paragraph 6ZOA(2)(d) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(d) of the Life Insurance Act]*

2.63 These provisions refer to a 'holding company' with respect to the regulated entity. The Bill defines the term 'holding company' for various purposes in the Industry Acts to mean a body corporate of which another body corporate is a subsidiary, with subsidiary generally having the same meaning as in the Corporations Act. The definition is based on the definition of 'holding company' in existing subsection 4(1) of the Transfer Act, and includes bodies corporate that are incorporated either in Australia or a foreign country. *[Schedule 1, item 7, subsection 5(1) of the Banking Act; Schedule 2, item 4, subsection 3(1) of the Insurance Act; Schedule 3, item 113, Schedule Dictionary of the Life Insurance Act]*

2.64 This amendment is intended to address a risk that can materialise whether or not the holding company is a regulated entity, so it is appropriate to extend this new ground for appointing a statutory manager to the ADI (or insurer, in the corresponding Insurance and Life Insurance Act provisions) in circumstances where the holding company is not a regulated entity.

2.65 Note that this additional trigger extends to procedures that are similar to external administration that have been made in a foreign country. For example, this could include circumstances where a foreign creditor obtains an order to wind-up the holding company in another jurisdiction, or where a foreign resolution authority uses its powers to implement a resolution of the holding company in its jurisdiction and this

involves the appointment of a manager, conservator or similar person to take control of all or part of the holding company.

2.66 Consistent with these changes to the Banking Act (see 2.61 and 2.61), the Bill adds an equivalent new trigger for an appointment of a judicial manager under the Insurance Act and Life Insurance Act. Section 62M of the Insurance Act and section 159 of the Life Insurance Act currently provide that a judicial manager may be appointed to an insurer if one of a number of grounds of a prudential nature is satisfied (for example, the insurer has failed to comply with a prudential standard) *and* the time needed to make or complete an investigation of the insurer would be likely to prejudice the interests of policyholders. The new trigger for appointment of a judicial manager under these sections requires that the Court must be satisfied that an external administrator has been appointed to a holding company of the insurer (or similar appointment has been made in a foreign country in respect of such a holding company) and that APRA considers that this poses a significant threat to the operation or soundness of the insurer, the interests of policyholders or the stability of the financial system in Australia. *[Schedule 2, item 30, paragraph 62M(a)(iva) of the Insurance Act; Schedule 3, item 26, paragraph 159(a)(iiia) of the Life Insurance Act]*

2.67 The Bill also provides additional triggers for the appointment of a statutory manager to a foreign ADI. The additional triggers are that if the ADI is a foreign ADI:

- an application for the appointment of an external administrator of the foreign ADI, or for a similar procedure in respect of the foreign ADI, has been made in a foreign country; or
- an external administrator has been appointed to the foreign ADI, or a similar appointment has been made in respect of the foreign ADI, in a foreign country *[Schedule 1, item 64, paragraph 13A(1)(e) of the Banking Act]*

2.68 The equivalent of these triggers (see 2.66) has been added to the new statutory management provisions in the Insurance Act for foreign general insurers and in the Life Insurance Act for foreign life insurers. *[Schedule 2, item 58, paragraph 62ZOA(2)(e) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(e) of the Life Insurance Act]*

2.69 The Bill adds equivalents of the new paragraph 13A(1)(e) in the Banking Act as new triggers for the appointment of a judicial manager to foreign insurers under the Insurance Act and the Life Insurance Act. Namely, the Court must be satisfied that there has been an application for, or appointment of, an external administrator to the foreign insurer, or for a similar procedure, in a foreign country. *[Schedule 2, item 30, paragraphs*

62M(a)(ivb) and 62M(a)(ivc) of the Insurance Act; Schedule 3, item 26, paragraphs 159(a)(iiib) and 159(a)(iiic) of the Life Insurance Act]

Widening the moratorium provisions applicable where a statutory or judicial manager is appointed

2.70 When a statutory manager is appointed to an ADI or insurer, or a judicial manager is appointed to an insurer, it is important that the statutory or judicial manager not be subjected to a multiplicity of time-consuming and costly litigious and enforcement actions that have the potential to distract from or hamper the stabilisation or orderly resolution of the entity or group. The statutory or judicial manager will also need time to assess the financial and operational position of the institution, and need to have access to, and be able to utilise, the institution's resources for the purposes of the administration and any resolution action.

2.71 The Bill amends the Industry Acts to expand the moratorium provisions applicable upon the appointment of a statutory or judicial manager to a regulated entity or (in the case of statutory management) a target body corporate. The enhancements assist with one of the primary aims of statutory or judicial management, which is to stabilise the relevant entity and prepare for implementation of the resolution, by ensuring this can be done without the constraints of creditor or other third party actions that could otherwise impede the orderly nature of a resolution.

2.72 The Bill replaces existing section 15B of the Banking Act with enhanced moratorium provisions. These enhanced moratorium provisions are consistent throughout the Industry Acts. The new moratorium provisions are broadly based on provisions in Division 6 of Part 5.3A, and section 600F of the Corporations Act (with appropriate amendment).
[Schedule 1, item 190, sections 15B to 15BE of the Banking Act; Schedule 2, items 33 and 58, sections 62PA to 62PE and 62ZOR to 62ZOW of the Insurance Act; Schedule 3, items 28 and 52, sections 161 to 161E and 179AR to 179AW of the Life Insurance Act]

2.73 The enhanced moratorium provisions in the Industry Acts provide that a person cannot begin or continue a proceeding in a court or a tribunal against a body corporate while a statutory or judicial manager is in control of the body corporate's business. The exception from this prohibition is if it is a proceeding in respect of an offence or a contravention of a provision of a law for which a pecuniary penalty (however described) may be imposed. A proceeding is covered by the new moratorium provision in respect of court and tribunal proceedings if: the proceeding is against the body corporate; or, it relates to property of the body corporate; or, it is to enforce any security granted by either the body corporate or a related body corporate, over property owned, used, possessed or occupied by the body corporate, or in which the body corporate has an interest. The reference to a tribunal means a body that

has characteristics similar to those of a court of law, and includes an industrial tribunal and an arbitral tribunal. *[Schedule 1, item 190, section 15B of the Banking Act; Schedule 2, items 33 and 58, sections 62ZOR and 62P of the Insurance Act; Schedule 3, items 52 and 28, sections 179AR and 161 of the Life Insurance Act]*

2.74 The amendments to existing sections 15B of the Banking Act, 62P of the Insurance Act and 161 of the Life Insurance Act do not change the status quo in the respect of criminal and civil penalty proceedings. So, as is currently the position, the stays against proceedings beginning or commencing will not apply to a proceeding in respect of an offence or a contravention of a provision of a law for which a pecuniary penalty may be imposed.

2.75 The enhanced moratorium provisions in the Industry Acts also ensure that no enforcement process in relation to the property of a body corporate can be begun or proceeded with if a statutory manager or judicial manager is in control of that body corporate's business. *[Schedule 1, item 190, section 15BA of the Banking Act; Schedule 2, items 33 and 58, sections 62ZOS and 62PA of the Insurance Act; Schedule 3, items 52 and 28, sections 179AS and 161A of the Life Insurance Act]*

2.76 In the case of the statutory management regime, APRA or the statutory manager could consent to such proceedings beginning or continuing, or the court or tribunal could grant leave for the proceedings or enforcement process to begin or continue on the ground that the person would be caused hardship if leave was not granted. If consent is given, APRA or the statutory manager cannot revoke the consent. Neither APRA nor the statutory manager is liable to an action or other proceedings for damages in respect of a refusal to give consent.

2.77 A person intending to apply for leave of the court or tribunal must give APRA at least 10 days' notice of the intention to apply (or a shorter period, if the court or tribunal considers that exceptional circumstances make this necessary). APRA may apply to the court or tribunal to be joined as a party to the proceedings for leave. If APRA is joined as a party, the court or tribunal must have regard to APRA's views in deciding whether to grant leave, and if so, whether to impose terms and the nature of those terms. *[Schedule 1, item 190, sections 15B and 15BA of the Banking Act; Schedule 2, item 58, sections 62ZOR and 62ZOS of the Insurance Act; Schedule 3, item 52, sections 179AR and 179AS of the Life Insurance Act]*

2.78 In the case of the judicial management regime, the judicial manager could consent to such proceedings or enforcement processes regarding property to begin or commence, or the court or tribunal would be able to permit such proceedings or enforcement processes regarding property to commence or continue on the ground that the person would be caused hardship if leave was not granted. If consent is given, the judicial

manager cannot revoke the consent. The judicial manager is also not liable to an action or other proceedings for damages in respect of a refusal to give consent.

2.79 A person intending to apply for leave of the court or tribunal must give APRA and the judicial manager at least 10 days' notice of the intention to apply (or a shorter period, if the court or tribunal considers that exceptional circumstances make this necessary). APRA or the judicial manager may apply to the court or tribunal to be joined as a party to the proceedings for leave. If APRA or the judicial manager is joined as a party, the court or tribunal must have regard to APRA or the judicial manager's (as applicable) views in deciding whether to grant leave, and if so, whether to impose terms and the nature of those terms. *[Schedule 2, item 33, sections 62P and 62PA of the Insurance Act; Schedule 3, item 28, sections 161 and 161A of the Life Insurance Act]*

2.80 The amendments to the Industry Acts also ensure that a person must not dispose of property if the property is owned by a body corporate that has a statutory or judicial manager in control of its business. Disposal is allowed if APRA or the statutory manager consents under the statutory management regime, or if the judicial manager consents under the judicial management regime. If consent is not given, APRA and the statutory manager or the judicial manager (as applicable) are not liable to an action or other proceeding for damages in respect of a refusal to give consent. *[Schedule 1, item 190, section 15BB of the Banking Act; Schedule 2, items 33 and 58, sections 62PB and 62ZOT of the Insurance Act; Schedule 3, items 28 and 52, sections 161B and 179AT of the Life Insurance Act]*

2.81 The amendments ensure that existing section 440B ('Restrictions on exercise of third party property rights') of the Corporations Act applies during a period in which a statutory or judicial manager is in control in the same way it applies during the administration of a company. The reference in paragraph 440B(2)(a) of the Corporations Act to the administrator's written consent is to be treated as a reference to the statutory or judicial manager's written consent (whichever is relevant) or APRA's written consent. Paragraph 440B(2)(b) of the Corporations Act also applies, which means that the Court can also provide leave to proceed. This means that the restrictions on exercise of third party property rights set out in section 440B of the Corporations Act do not apply in relation to the exercise of a third party's rights in property if the rights are exercised with the statutory or judicial manager's or, in the case of statutory management, APRA's, written consent, or (in accordance with section 440B of the Corporations Act) with the leave of the Court. Neither APRA, the statutory manager nor the judicial manager (as applicable) are liable to an action or other proceeding for damages in respect of a refusal to give consent. The applied section 440B protections are intended to operate independently of, and without limitation from, the other moratorium provisions dealing with court and tribunal proceedings,

enforcement processes regarding property and on the disposal of property. *[Schedule 1, item 190, section 15BC of the Banking Act; Schedule 2, items 33 and 58, sections 62PC and 62ZOU of the Insurance Act; Schedule 3, items 28 and 52, sections 161C and 179AU of the Life Insurance Act]*

2.82 The amendments also ensure that suppliers of essential services to a body corporate that is under statutory or judicial management cannot refuse services to the body corporate solely on the basis of an amount owing to them for services provided before the statutory or judicial management. The supplier must also not make it a condition of the supply of the essential service that the amount be paid first. An ‘essential service’ for these purposes has the same meaning as in section 600F of the Corporations Act, namely electricity, gas, water or a carriage services within the meaning of the *Telecommunications Act 1997*. *[Schedule 1, item 190, section 15BD of the Banking Act; Schedule 2, items 33 and 58, sections 62PD and 62ZOV of the Insurance Act; Schedule 3, items 28 and 52, sections 161D and 179AV of the Life Insurance Act]*

2.83 The amendments to the Industry Acts clarify that whilst a statutory or judicial manager is in control of a body corporate, the body corporate is not required to hold an annual general meeting in accordance with the requirements under sections 250N or 601BR of the Corporations Act. *[Schedule 1, item 190, section 15BE of the Banking Act; Schedule 2, items 58 and 33, sections 62ZOW and 62PE of the Insurance Act; Schedule 3, items 28 and 52, sections 161E and 179AW of the Life Insurance Act]*

2.84 In the case of the Life Insurance Act, where it is possible to appoint a judicial manager to only part of the business of the life insurer, the amendments provides that if only part of the business of the life company is under judicial management, then existing sections 250N or 601BR of the Corporations Act will apply, in which case the life insurer must continue to hold an annual general meeting. This is because, when a judicial manager is appointed to only part of the business of a life insurer, the appointment will in most cases be made to a particular statutory fund, or particular statutory funds, of the life insurer, leaving other business of the company to be managed by the board, who will be accountable to the company’s shareholders. *[Schedule 3, item 28, subsection 161E(3) of the Life Insurance Act]*

2.85 The Bill clarifies that the new moratorium provisions relating to property rights do not prevent the exercise of a contractual right in relation to an asset that secures liabilities to holders of covered bonds, or their representatives if payments under the covered bonds to the holders or representatives are not made. *[Schedule 1, items 190 and 231, subsections 15BA(8), 15BB(4), 15BC(5), 31B(2) of the Banking Act]*

2.86 Further details on how the new moratorium provisions interact with the PSN Act is outlined at Chapter 6.

Clarifying that a Banking Act statutory manager is not constrained by subsection 13A(3) of the Banking Act

2.87 The Bill amends the Banking Act to clarify that a statutory manager is able to manage an ADI's business in accordance with the provisions of the Banking Act, without being constrained by the operation of existing subsection 13A(3) of the Banking Act.

2.88 Subsection 13A(3) provides that if an ADI becomes unable to meet its obligations or suspends payment, the assets in Australia of the ADI are to be available to meet the ADI's liabilities in a particular order of priority. The first two priority liabilities are APRA's costs and expenses of the financial claims scheme (if relevant), followed by the ADI's liabilities in Australia in relation to protected accounts, followed by certain other debts.

2.89 The wording of subsection 13A(3) could be interpreted to apply to a statutory manager appointed after the ADI has become unable to meet its obligations or has become insolvent. This interpretation would place the statutory manager under an obligation to refrain from paying liabilities other than in the order of priority set out in this section. The amendment puts it beyond doubt that this is not the intention by providing that a statutory manager is not constrained by subsection 13A(3). [*Schedule 1, item 68, subsection 13A(3AA) of the Banking Act*]

Immunity for statutory managers and judicial managers

2.90 The Bill amends the existing provisions in the Industry Acts to enhance the statutory immunity of statutory and judicial managers under those Acts.

2.91 Robust immunity provisions are important elements of the statutory and judicial management frameworks. In taking actions considered necessary by APRA to protect depositor and policyholder interests and promote financial system stability, statutory and judicial managers could be required to take actions that have the potential to adversely affect others, including directors, shareholders and certain classes of creditors of the relevant entity. They may also be concerned about the risk of liability arising from the management of a large and complex organisation that is undergoing financial stress.

2.92 It is conceivable that adversely affected stakeholders may subsequently seek to recover any loss suffered via legal action against the statutory or judicial manager personally. Moreover, the circumstances of a statutory or judicial manager's appointment are such that they may be required to take actions of a higher-than-usual level of risk or in situations of considerable uncertainty.

2.93 Therefore, it is necessary that a statutory or judicial manager has confidence that they can take action required to manage and stabilise a distressed entity within the limits of their powers, without the risk of incurring personal liability. If there is significant uncertainty on this matter, there is a high risk that suitable persons will not be willing to assume an appointment as statutory or judicial managers.

2.94 The amendments increase the level of protection afforded to statutory and judicial managers to a level similar to that afforded to APRA, its members, staff or agents under existing section 58 of the APRA Act. The amendments also signpost APRA's secrecy provision in section 56, Part 6, of the APRA Act as it applies to statutory and judicial managers in the same way as it does to APRA staff, as a statutory or judicial manager will fall within the definition of "officer" in subsection 56(1) of the APRA Act. *[Schedule 1, item 149, section 14C of the Banking Act; Schedule 2, items 56 and 58, sections 62ZM and 62ZOK and of the Insurance Act; Schedule 3, items 51 and 52, sections 179 and 179AK of the Life Insurance Act]*

2.95 Each of those sections has been amended to include provisions equivalent to section 58 of the APRA Act, including a limitation on the statutory immunity for 'bad faith'.

2.96 It is not intended that these provisions affect the ability of a statutory or judicial manager to incur personal contractual liability. For example, these provisions do not cover contractual arrangements entered into by the statutory or judicial manager when retaining advisors or acquiring goods and services on their own account. Nor do the provisions affect the liability of the entity under statutory management itself.

2.97 Subject to the above, these enhanced immunity provisions are intended to provide that statutory or judicial managers are protected from any breaches of directors' duties under the Corporations Act, any other Commonwealth legislation or common law. For the avoidance of doubt, the Bill clarifies that a statutory manager cannot be liable for insolvent trading under section 588G of the Corporations Act. The existing subsection 14C(4) of the Banking Act provides similar protection. However, the Bill repeals the existing subsection 14C(4) and the new provision is located within the new general immunity provision for the purposes of clarifying its relationship with the general immunity provision. This protection is replicated in the Insurance Act and Life Insurance Acts. *[Schedule 1, item 149, subsection 14C(3); Schedule 2, items 56 and 58, subsection 62ZM(3) and 62ZOK(3) of the Insurance Act; Schedule 3, items 51 and 52, subsections 179(3) and 179AK(3) and of the Life Insurance Act]*

2.98 These enhanced immunity provisions operate independently of the other immunity sections within each respective Industry Act and section 58 of the APRA Act. The immunity provisions are not intended to limit each other. *[Schedule 1, items 252, section 70AB of the Banking Act;*

Schedule 2, item 137, section 127D of the Insurance Act; Schedule 3, item 107, section 246C of the Life Insurance Act

Transactions under statutory management not voidable

2.99 The Bill amends the Banking Act to prevent the transactions of a Banking Act statutory manager from being voidable under existing section 588FE of the Corporations Act (This applies to uncommercial transactions, insolvent transactions and unfair preferences, and is similar to protection given by section 588FE where an administrator has been appointed under Part 5.3A of the Corporations Act (voluntary administration). Equivalent provisions are inserted into the Insurance Act and the Life Insurance Act). *[Schedule 1, item 151, section 14CA of the Banking Act; Schedule 2, item 58, section 62ZOL of the Insurance Act; Schedule 3, item 52, section 179AL of the Life Insurance Act]*

2.100 These amendments are intended to help ensure that service providers and other counterparties can be confident in any dealings with the statutory manager regardless of the financial position of the entity under statutory management.

Terminating control of a regulated entity

2.101 The Bill amends section 13C of the Banking Act, which empowers APRA to terminate its control of an ADI, or the statutory management of the ADI, where APRA has achieved its resolution objectives with respect to the ADI. Such a termination is defined in the section as an ‘ultimate termination of control’ and it brings the statutory management process to an end.

2.102 This amendment removes the previous requirement that, in order to end the statutory management of an ADI, its deposit liabilities in Australia need to have been repaid, or APRA needs to be satisfied that suitable provision has been made for their repayment. *[Schedule 1, item 79, section 13C of the Banking Act]*

2.103 Given that the resolution of an ADI may not always involve the winding up of the ADI or the repayment of deposit liabilities (for example, where a transfer or recapitalisation is undertaken), this amendment is necessary to give APRA the ability to end the statutory management of an ADI at the point where it considers that statutory management is no longer necessary.

2.104 Further, because the statutory management regime has been extended in scope to cover entities that may not have deposit liabilities (such as authorised NOHCs or subsidiaries that are not ADIs), the Banking Act has been amended to ensure that APRA can end the statutory management of such entities when it deems it necessary to do so.

2.105 For example, APRA may appoint a statutory manager to a service company within a relevant group of bodies corporate to ensure that it continues to provide essential services to a relevant ADI. As the service company itself has no deposit liabilities, this amendment will ensure APRA is able to end the statutory management when it deems it appropriate.

2.106 An example of circumstances where APRA may deem it necessary to end the statutory management of a target body corporate would be where appropriate arrangements have been made for the continued provision of the essential services provided by the target body corporate as part of the resolution of the relevant ADI.

2.107 As explained at 2.41 to 2.43, these amendments to the Banking Act are replicated in the Insurance and Life Insurance Acts with respect to the statutory management of insurers. *[Schedule 2, item 58, section 62ZOC of the Insurance Act; Schedule 3, item 52, section 179AC of the Life Insurance Act]*

Replacement of a statutory manager

2.108 The Bill amends section 14E of the Banking Act to allow APRA to terminate the appointment of an administrator of a body corporate's business and to appoint another person as administrator or itself take control. This is important to ensure APRA maintains confidence in the ability of the statutory manager to carry out APRA's instructions and meet APRA's objectives for the orderly resolution of the relevant ADI. The statutory management itself will continue, as this process does not involve an 'ultimate termination of control' of the kind described at 2.101.

2.109 APRA may only exercise this power if the administrator contravenes a requirement of Division 2 of Part II of the Banking Act (regarding statutory management and protection of depositors), or if APRA considers that this is necessary to;

- facilitate the resolution of the entity, a relevant group of bodies corporate of which the entity is a member, or another member of such a group; or
- if the body corporate is an ADI – protect the interests of depositors of the ADI; or
- promote financial system stability in Australia. *[Schedule 1, item 162, section 14E of the Banking Act; Schedule 2, item 58, section 62ZOO of the Insurance Act; Schedule 3, item 52, section 179AO of the Life Insurance Act]*

2.110 The exercise of this power does not cancel the statutory management of the body corporate. Rather, it cancels the appointment of a particular person as Banking Act statutory manager of the body corporate.

2.111 Where APRA is the statutory manager of a body corporate, and a condition listed at 2.109 is satisfied, APRA can replace itself as statutory manager by appointing a person (or one or more persons) as administrator(s).

2.112 The Bill also inserts an adapted form of this provision into the Insurance and Life Insurance Acts, referring to policyholders rather than depositors, with respect to statutory management of insurers. *[Schedule 2, item 58, section 62ZO of the Insurance Act; Schedule 3, item 52, section 179AO of the Life Insurance Act]*

Statutory manager not subject to PGPA Act

2.113 The Bill ensures that the PGPA Act does not apply to a statutory manager under any of the Industry Acts, avoiding an unintended outcome that might otherwise arise where an entity is placed into statutory management. This amendment addresses the concern that APRA's influence or control in relation to the statutory management process may result in the entity falling within the definition of Commonwealth company in the PGPA Act. The PGPA Act imposes a variety of corporate governance and financial reporting obligations on Commonwealth companies, having regard to their public sector ownership or control. It is not intended that these requirements apply in relation to a body under statutory management. *[Schedule 1, item 192, subsection 15D(3) of the Banking Act; Schedule 2, item 58, subsection 62ZOY(3) of the Insurance Act; Schedule 3, item 52, subsection 179AY(3) of the Life Insurance Act]*

Clarifying amendments to judicial management

2.114 The Bill repeals sections 62Q of the Insurance Act and 162 of the Life Insurance Act, as these sections, which provide that an insurer is not to be judicially managed except under the Insurance Act or Life Insurance Act as the case may be, are unnecessary. This is because judicial management of a life insurer, as defined in the Life Insurance Act, can only occur under that Act, and judicial management of a general insurer can only occur under the Insurance Act. *[Schedule 2, item 34, section 62Q of the Insurance Act; Schedule 3, item 29, section 162 of the Life Insurance Act]*

Effect of judicial management on existing directors and officers

2.115 The Bill amends sections 62T of the Insurance Act and 165 of the Life Insurance Act to clarify the effect of judicial management on the powers of directors and officers of the insurer.

2.116 The new law replaces the existing terminology regarding the ‘vesting’ and ‘divesting’ of the ‘management’ of the insurer, as these terms do not precisely define the effect of judicial management on the existing directors and officers of the insurer. *[Schedule 2, items 39 to 42 and 55, subsections 62U(1) to 62U(4), and 62ZK(2) of the Insurance Act; Schedule 3, items 34 to 37 and 50, and subsections 165A(1) to 165A(4) and 177(2) of the Life Insurance Act]*

2.117 For example, it is uncertain whether the appointment of a judicial manager under the current law removes directors and officers (and other persons exercising management functions) from their positions or whether it merely deprives them of their powers and functions. Further, the current law is expressed to divest *any* person vested with the ‘management’ of an insurer of that management, without distinguishing between strategic and middle or lower level functions. In many cases it will be appropriate for the latter to continue exercising their functions immediately following the appointment of a judicial manager, subject to the judicial manager’s discretion and oversight. .

2.118 The new law provides that a person who had the powers and functions of an ‘officer’ ceases to have those powers and functions once a judicial manager has been appointed. The new law also includes provisions that invalidate any actions taken after the commencement of the judicial management by a person who had the powers and functions of an officer before the appointment of a judicial manager. These purported acts have no effect to the extent that they are performed after the appointment of a judicial manager to the insurer. *[Schedule 2, item 38, section 62T of the Insurance Act; Schedule 3, item 33, section 165 of the Life Insurance Act]*

2.119 These amendments also include provisions that explain the effect of judicial management on a foreign general insurer’s agent in Australia, as well as the members of a foreign life insurer’s Compliance Committee (see 7.32).

2.120 The Bill defines the term ‘officer’ as having the same meaning as it has in the Corporations Act. Section 9 of that Act defines ‘officer’ to include directors and any person who makes, or participates in the making of, decisions that affect the whole or a substantial part of the business of the entity, or who has the capacity to affect significantly the entity’s financial standing. *[Schedule 2, item 38, subsection 62T(4) of the Insurance Act; Schedule 3, item 33, subsection 165(6) of the Life Insurance Act]*

2.121 Consequential amendments have been made to the provisions for judicial management in the Insurance and Life Insurance Acts to update the judicial management regimes of both Acts as a consequence of this change.

Effect on directors of cancelling judicial management

2.122 The Bill amends sections 62ZF of the Insurance Act and 172 of the Life Insurance Act to clarify the effect of cancelling judicial management on the board of directors of the insurer. *[Schedule 2, item 50 subsection 62ZF(5) of the Insurance Act; Schedule 3, item 45, subsection 172(5) of the Life Insurance Act]*

2.123 The amendments ensure that, on the cancellation of judicial management of an insurer, the judicial manager ceases to have the powers and functions of an officer of the insurer, and the board of directors resumes the powers and functions of officers of the general insurer.

2.124 In the event that all the directors of the insurer have either resigned or for some other reason no longer hold their appointment, the judicial manager may seek to appoint new directors before the cancellation takes effect. Alternatively, APRA can apply to the Court for an order that directs the judicial manager to appoint directors to the insurer.

Powers and functions of multiple statutory or judicial managers

2.125 The Bill amends the Industry Acts, to clarify that one or more persons may be appointed as statutory manager. The amendments also clarify the powers and functions of each statutory manager where more than one person has been appointed as a statutory manager of an entity. *[Schedule 1, item 65, subsection 13A(2A) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(9) of the Insurance Act; Schedule 3, item 52, subsection 179AA(9) of the Life Insurance Act]*

2.126 In particular, the amendments define the default arrangements where multiple statutory managers have been appointed to an entity, being that each of the statutory managers may exercise all of the powers and functions under the relevant Act either jointly or individually.

2.127 The amendments also provide that APRA may place limits or conditions on the ability of any or all statutory managers to perform powers and exercise functions jointly or individually. APRA may do so by giving a notice to the statutory managers that specifies these limits and conditions.

2.128 The amendments also clarify that a reference in each of the Industry Acts to a statutory manager is a reference to one or more of those statutory managers in the relevant Act, as the case requires.

2.129 The Bill also amends sections 62R of the Insurance Act and 163 of the Life Insurance Act to reflect the above amendments in relation to judicial managers. Some minor adaptations were required in order to

apply these changes to the judicial management provisions. For example, it is the Court (and not APRA) that has the power to specify the limits or conditions on the ability of any or all judicial managers to perform powers and exercise functions jointly or individually. In addition to conferring jurisdiction to the Court in this instance, the Bill confers jurisdiction to the Court in various provisions throughout the Industry Acts because that is the most appropriate court of jurisdiction due to the complex nature of the matters. *[Schedule 2, item 35, section 62R of the Insurance Act; Schedule 3, item 30, section 163 of the Life Insurance Act]*

2.130 The amendments clarify that the Court may make an initial appointment of two or more judicial managers, and may subsequently appoint one or more additional judicial managers. Where multiple or additional appointments are made, the default position is that the functions and powers of a judicial manager may be performed or exercised by all of the judicial managers acting jointly, or each of them acting individually. However at the time of making the appointment the Court may specify limits or conditions on the ability of judicial managers to perform functions or exercise powers jointly or individually.

2.131 These provisions are broadly based on similar provisions in the Corporations Act providing for multiple appointments of liquidators, provisional liquidators and other external administrators under that Act.

2.132 The amendments also provide that if, subsequent to the appointment of a judicial manager, a situation arises or is likely to arise where there may be no judicial manager the Court may appoint another judicial manager of the general insurer. *[Schedule 2, item 35, subsection 62R(1A) of the Insurance Act; Schedule 3, item 30, subsection 163(1A) of the Life Insurance Act]*

2.133 This will ensure that casual vacancies can be filled but does not limit the more general power under the Insurance Act and the Life Insurance Acts to appoint an additional judicial manager in other situations.

Cancelling the appointment of a judicial manager

2.134 The amendments provide that the Federal Court may also cancel the appointment of a judicial manager and appoint another judicial manager on application by APRA or of its own motion. These provisions are concerned with the removal and replacement of a particular judicial manager (or particular judicial managers) rather than the termination of the judicial management process as such (sections 62ZF of the Insurance Act and 172 of the Life Insurance Act, on the other hand, are concerned with the cancellation of the judicial management itself). *[Schedule 2, item 36, subsection 62R(2) of the Insurance Act; Schedule 3, item 31, subsection 163(2) of the Life Insurance Act]*

2.135 The power to apply to the Court for the cancellation of a judicial manager's appointment is intended to be flexible and might be used in a range of situations. For example, APRA may apply where the judicial manager is unable, for unforeseen reasons, to continue to act, or where the judicial manager does not have the skills or resources to continue the judicial management or has otherwise lost the confidence of the court or APRA.

Appointing a statutory or judicial manager in absence of external support

2.136 The Bill amends the Insurance and Life Insurance Acts to expressly allow the Court to disregard external support for the entity when it is making an order to place the entity under judicial management. *[Schedule 2, items 28 and 29, subparagraphs 62M(1)(a)(i) and 62M(1)(ii) of the Insurance Act; Schedule 3, item 25, subparagraph 159(1)(a)(i) of the Life Insurance Act]*

2.137 Equivalent provisions are also inserted into the Insurance and Life Insurance Acts to expressly allow APRA to disregard external support for the entity when exercising its discretion to appoint a statutory manager to an entity. This is intended to ensure that the provision of external support to a stressed entity, for example some form of temporary public support, would not fetter the ability of APRA to determine that the preconditions are met for appointing a statutory manager or placing the entity under judicial management. *[Schedule 2, item 58, subsection 62ZOA(7) of the Insurance Act; Schedule 3, item 52, subsection 179AA(7) of the Life Insurance Act]*

2.138 In effect, these amendments harmonise the Insurance and Life Insurance Acts with related provisions in the Banking Act.

2.139 The existing Banking Act provisions also include the power to establish regulations that define things that may not be considered external support for this purpose, and an equivalent of this regulations-making power is included in the equivalent provisions in the Insurance and Life Insurance Acts *[Schedule 2, item 32, subsection 62M(3) of the Insurance Act; Schedule 3, item 27, subsection 159(3) of the Life Insurance Act]*

Statutory manager recommending directions from APRA

2.140 Upon the appointment of an administrator to take control of an entity under statutory management, the administrator may decide that a possible course of action will have strategic implications, and should therefore be determined by APRA. While it is expected that processes for addressing these situations would be provided for in the contractual or other arrangements agreed between APRA and the administrator, there is currently no provision that provides a means by which the administrator

can request APRA to formally direct it as to the appropriate course of action to take.

2.141 The current law in paragraph 14B(1)(a) of the Banking Act provides formal means by which an administrator may recommend that APRA issue a formal direction under Division 1BA or section 29 *to the ADI* under its control. The amendments provide that an administrator may also recommend that APRA issues a formal direction under existing subsection 14D(3) *in respect of the administrator's control of the ADI*. Subsection 14D(3) provides that APRA may give an administrator of an ADI's business a direction relating to the control of the ADI's business. The administrator must act in accordance with the direction. The expansion of the statutory management regime to group entities means that provision is further enhanced so that an administrator may also recommend that APRA issues a formal direction under subsection 14D(3) in respect of a related bodies corporate to the ADI.

2.142 Equivalent provisions have been added to the Insurance and Life Insurance Acts. *[Schedule 1, items 146 and 153, subsections 14B(1) and 14D(3) of the Banking Act; Schedule 2, item 58, subsections 62ZOJ(1) and 62ZOM(3) of the Insurance Act; Schedule 3, item 52, subsections 179AJ(1) and 179AM(3) of the Life Insurance Act]*

Appointing a statutory manager over a foreign regulated entity

2.143 The Bill implements provisions allowing for the appointment of a statutory manager over the Australian business assets and liabilities of a foreign regulated entity.

2.144 The term 'Australian business assets and liabilities' refers to the scope of business of a foreign regulated entity that APRA's crisis management powers are to extend to under the amendments in this Bill – see Chapter 7 for more information about the amendments to APRA's crisis management powers regarding foreign regulated entities.

2.145 It is intended that such a statutory manager would be able to exercise any powers and functions necessary to manage the Australian business assets and liabilities of the entity in order to achieve the objectives of the statutory management in Australia. To that end, the Bill provides that the statutory manager have the powers and functions of the board of the foreign regulated entity in so far as they relate to the Australian business assets and liabilities of the entity. This would include the powers and functions of a foreign general insurer's agent in Australia and Compliance Committee members of a foreign life insurer.

Continued application of the Insurance and Life Insurance Acts during judicial management

2.146 The Bill makes minor amendments to existing provisions in the Insurance and Life Insurance Acts that provide that the appointment of a judicial manager does not affect the continued operation of those Acts or FSCODA in relation to the insurer's obligations under those Acts.

2.147 These amendments ensure that there is no doubt that these Acts continue to operate during the period of time (if any) between the Court making an order for the judicial management of an insurer and the commencement of judicial management by providing that neither:

- the making of an order by the Court that the insurer be placed into judicial management; nor
- the commencement of judicial management

affects the continued operation of those Acts in relation to the obligations of an insurer under those Acts. [*Schedule 2, items 44 to 46, section 62W of the Insurance Act; Schedule 3, items 39 to 41, section 166 of the Life Insurance Act*]

Amending the definition of 'subsidiary' under the Insurance Act to align with the Banking Act and Life Insurance Act

2.148 Under the existing definition of 'subsidiary' in the Insurance Act, a company will be a 'subsidiary' of another company if the other company is in a position to cast, or control the casting of, more than 25 per cent (the threshold percentage) of the maximum number of votes that might be cast at a general meeting of the company, or holds more than 25 per cent of the issued share capital of the company. In contrast, under the Banking Act and Life Insurance Act, the threshold percentage is the usual 50 per cent. The definition in the Banking and Life Insurance Acts follows the definition of 'subsidiary' in the Corporations Act.

2.149 The reason for the different definition of 'subsidiary' in the Insurance Act appears to be historical. The 25 per cent threshold percentage was originally employed in a test defining when two companies were related to each other for the purpose of certain provisions of the Insurance Act. Most of the provisions the 25 per cent test' was used in, with the exception of the investigation provisions discussed at 2.148 to 2.151, were repealed in 2002, or prior to that.

2.150 However, despite the repeal of those provisions, the definition of 'subsidiary' has remained unchanged and continues to apply to newer provisions of the Insurance Act, although the definition is not intended to apply as a matter of policy. For example, under prudential standards made

by APRA in relation to general insurers, ‘subsidiary’ is defined according to the 50 per cent percentage threshold, in harmony with the definition of ‘subsidiary’ in the Banking Act, Life Insurance Act and the prudential standards applicable to ADIs and life companies.

2.151 In light of this, the Bill amends the definition of ‘subsidiary’ in section 4 of the Insurance Act to be consistent with the definition used in the Banking Act and Life Insurance Acts. [*Schedule 2, item 8, section 4 of the Insurance Act*]

2.152 Section 16 of the Life Insurance Act determines how bodies corporate are related to each other for the purposes of the Life Insurance Act, except for the purposes of Part 7 of the Life Insurance Act relating to monitoring and investigation powers. In existing Part 7 of the Life Insurance Act, which relates to investigations, APRA is given power to investigate not only a life company but also an ‘associated body corporate’ of a life company. Section 128 provides that two bodies are ‘associated’ with each other if they are ‘related to each other’ and certain other conditions are satisfied. Section 129 provides that the question of whether two bodies are ‘related’ to each other for these purposes is to be determined applying the Corporations Act tests but on the basis of a ‘more than a quarter’ control test instead of the usual ‘more than half’ control test. This operates, as noted, for the purposes of the investigation provisions.

2.153 The equivalent of Part 7 of the Life Insurance Act is the existing Part V of the Insurance Act. Subsection 52(3) in Part V provides for the investigation of an ‘associated body corporate’ of an insurer. Subsection 50(2) of the Insurance Act, like section 128 of the Life Insurance Act, provides that two bodies are associated with each other where they are ‘related to each other’ and certain other conditions are satisfied. The Bill inserts a new provision in existing section 50 in similar terms to section 129 of the Life Insurance Act (and in similar terms to a provision that was incorrectly repealed by the *General Insurance Reform Act 2001*). This will restore consistency between the scope of monitoring and investigation powers under the Insurance Act and Life Insurance Act. It should be emphasised that this amended provision in section 50 is only relevant in the context of investigations and not more generally. As discussed above, a ‘50 per cent test’ will apply elsewhere in defining ‘subsidiary’, as will the usual Corporations Act definition of ‘related body corporate’. [*Schedule 2, items 7, 8 and 24, subsection 3(1), section 4B and subsection 50(3) of the Insurance Act*]

Insurance and Life Insurance Acts to have effect despite the Corporations Act

2.154 The Bill amends the Insurance and Life Insurance Acts to clearly indicate that those Acts have effect despite any provisions in the Corporations Act. The Banking Act already includes a provision for that Act to have effect despite provisions of the Corporations Act. *[Schedule 2, item 137, section 127E of the Insurance Act; Schedule 3, item 108, section 251AA of the Life Insurance Act]*

2.155 Further consequential amendments have been made to the Industry Acts, for the avoidance of doubt, regarding the way that these Acts interact with the Corporations Act. These amendments are included because certain provisions are expressed to apply despite the Corporations Act, even though there is a general override in existing section 70B of the Banking Act, (and the new corresponding provisions in the Insurance Act Life Insurance Act as discussed above). These amendments will ensure that the mentions of the Corporations Act in the specific provisions do not limit the general scope of section 70B of the Banking Act and the counterpart provisions in the Insurance and Life Insurance Acts so that the relevant Industry Acts have effect despite the Corporations Act. *[Schedule 1, items 98, 127 and 138, paragraphs 13G(3)(a), 14A(5B)(a), and 14AA(4)(a) of the Banking Act; Schedule 2, items 47, 53 and 106, paragraphs 62Z(4)(a), 62ZJ(3)(b)(i), and 103D(3)(a) of the Insurance Act; Schedule 3, items 42, 48 and 76, paragraphs 168A(4)(a), 176(3)(b)(i), and 230AD(3)(a) of the Life Insurance Act]*

Consequential and minor amendments

2.156 As a consequence of introducing a statutory management regime into the Insurance and Life Insurance Acts, the Bill inserts an equivalent to section 13BA of the Banking Act into the those Acts. This requires APRA to issue a written notice to the body corporate to which APRA is appointing a statutory manager. It also specifies that a statutory manager takes control of a body corporate's business at the time specified in a notice (which cannot be earlier than the notice is given) or if the notice does not specify a time, then at the time the notice is given. In line with the existing section 13BA of the Banking Act, the Bill provides that the notice made by APRA is not a legislative instrument. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003* *[Schedule 2, item 58, section 62ZOB of the Insurance Act; Schedule 3, item 52, section 179AB of the Life Insurance Act]*

2.157 As a consequence of introducing a statutory management regime into the Insurance and Life Insurance Acts, an equivalent section to section 14AA (as amended by the Bill) of the Banking Act was inserted into each of the Insurance and Life Insurance Acts (that is, sections 62ZOF of the Insurance Act and 179AF of the Life Insurance Act).

Consistent with the treatment of section 14AAA of the Banking Act (see 2.40), the new sections 62ZOE of the Insurance Act and 179AE of the Life Insurance Act also do not prevent a statutory manager of an authorised NOHC from using funds of the authorised NOHC to increase the level of capital of the relevant insurer, where those funds were raised following the exercise of the statutory manager's power to facilitate a recapitalisation under sections 62ZOF of the Insurance Act or 179AF of the Life Insurance Act. *[Schedule 2, item 58, section 62ZOF of the Insurance Act; Schedule 3, item 52, section 179AF of the Life Insurance Act]*

2.158 As a consequence of introducing a statutory management regime into the Insurance and Life Insurance Acts, the Bill inserts an equivalent to section 14AB of the Banking Act into those Acts (as amended by the Bill to cover group entities). This provides that before a statutory manager exercises a power to facilitate recapitalisation, the statutory manager must consider a report on the fair value of shares or rights from an expert unless APRA determines that this is not required because the delay to act would detrimentally affect policyholders and the financial system stability in Australia. In line with the existing section 14AB of the Banking Act, the determination is not a legislative instrument. The Bill also provides that the written notice from the Minister to the expert of the assumptions for the valuation of the company or rights is not a legislative instrument. These provisions were included to assist readers, as such a determination from APRA or written notice from the Minister are not legislative instruments within the meaning of subsection 8(1) of the *Legislation Act 2003*. *[Schedule 2, item 58, section 62ZOG of the Insurance Act; Schedule 3, item 52, section 179AG of the Life Insurance Act]*

2.159 Also as a consequence of introducing a statutory management regime for the Insurance and Life Insurance, the Bill inserts an equivalent to section 14AD of the Banking Act into those Acts. This allows APRA to require a person to give information relating to the business of the body corporate that is under statutory management in certain circumstances. If a person refuses or fails to give the information or documents as required by APRA, they commit an offence with a penalty of 12 months imprisonment or 50 penalty units, or both. A person is not excused from complying with APRA's requirement on the ground that doing so would tend to incriminate the individual or make the individual liable to a penalty.

2.160 It is critical that APRA has the power to obtain information from officers of the failed entity in order to assist with the management and resolution of the entity or to help understand the cause of the failure. Although the existing section 14AD of the Banking Act does not excuse a person from providing information on self-incrimination grounds, both it and the new provisions under the Bill provide a safeguard where the information is sought from an individual. Neither the information or

document given, the giving of the information or document, nor any information, document or thing obtained as a direct or indirect consequence of giving the information or document, is admissible in evidence against the individual in a criminal proceeding or a proceeding for the imposition of a penalty. The only exception to this safeguard is in a proceeding in respect of the falsity of the information or document. This exception is appropriate to discourage the production of false information or document. The new provisions based on the existing section 14AD of the Banking Act strikes an appropriate balance between the rights of the individual and the desirability of the regulator having power to obtain relevant information about a failed entity. *[Schedule 2, item 58, section 62ZOI of the Insurance Act; Schedule 3, item 52, section 179AI of the Life Insurance Act]*

2.161 To facilitate the extension of the Banking Act statutory management regime to group entities, the term ‘ADI statutory manager’ has been replaced with the term ‘Banking Act statutory manager’ in the Banking Act. This is to ensure that no confusion arises as to the scope of entities that a statutory manager may take control of under the Banking Act. As a consequence of introducing the statutory management regime to the Insurance and Life Insurance Acts, the terms ‘Insurance Act statutory manager’ and ‘Life Insurance Act statutory manager’ are introduced into the Insurance and Life Insurance Acts. *[Schedule 1, items 4 and 65, subsections 5(1) and 13A(2) of the Banking Act; Schedule 2, item 58, subsection 62ZOA(8) of the Insurance Act; Schedule 3, item 52, subsection 179AA(8) of the Life Insurance Act]*

2.162 To facilitate the extension of the Banking Act statutory management regime to group entities, the definition of ‘administrator’ is widened from being an administrator appointed under subsection 13A(1) to take control of an ADI’s business, to cover an administrator appointed under subsection 13A(1) to take control of the body corporate’s business. Equivalent amendments are made to the Insurance and Life Insurance Acts. *[Schedule 1, item 2, section 5(1) of the Banking Act; Schedule 2, item 1, section 3(1) of the Insurance Act; Schedule 3, item 110, Schedule Dictionary of the Life Insurance Act]*

2.163 As a consequence of introducing a statutory management regime for the Insurance and Life Insurance Acts, the definition of ‘relevant group of bodies corporate’ from the Banking Act is inserted (with relevant modifications) into the Insurance and Life Insurance Acts. *[Schedule 2, items 7 and 8, subsection 3(1) and section 4A of the Insurance Act; Schedule 3, items 4 and 117, section 15A and the Schedule Dictionary of the Life Insurance Act]*

2.164 Further minor amendments have been made to the Transfer Act and PSN Act to reflect the changes in terminology and structure in the Industry Acts. For example, the amendments will include references to ‘Banking Act statutory manager’, ‘Insurance Act statutory manager’ and ‘Life Insurance Act statutory manager’ in section 25 of the Transfer Act in

the relevant pre-condition for the making of a transfer determination under that section.

2.165 Further amendments have been made to adapt the existing provisions of the Banking Act to replace the term ‘ADI’ with ‘body corporate’ as appropriate. This is to ensure that each provision in the Banking Act that relates to statutory management can be applied with respect to target bodies corporate where appropriate.

2.166 As the statutory management regimes in the Insurance and Life Insurance Acts are closely adapted from the provisions of the Banking Act, equivalent changes have been carried over to those Acts.

2.167 A number of minor changes have been made to the Banking and Insurance Acts to clarify and distinguish between the use of the term ‘related body corporate’ for the purposes of the statutory management regime and the use of ‘related body corporate’ for the whistleblower protection provisions of those Acts *[Schedule 1, items 235 to 238, subsections 52A(2) and 52A(3) and paragraphs 52E(1)(b) and 52E(1)(c) of the Banking Act; Schedule 2, items 18 to 22, subsections 38A(2) and 38A(3), paragraphs 38E(1)(b)(i) and 38E(1)(b)(ii) and 38E(1)(c) of the Insurance Act]*.

2.168 As a consequence of inserting a new definition for determining whether bodies corporate are related to each other (see 2.152), a cosmetic change was made so that the existing phrase ‘related company’ in the Insurance Act is amended to ‘a body corporate that is related to’ to be consistent with the new wording. *[Schedule 2, items 7 and 8, subsection 3(1) and section 4B of the Insurance Act]*

2.169 As a consequence of introducing the statutory management regime for the Insurance and Life Insurance Acts, the existing definition of ‘external administration’ in the PSN Act is expanded to include a Banking Act statutory manager, an Insurance Act statutory manager, or a Life Insurance Act statutory manager taking control of a person’s business. *[Schedule 5, item 6, section 5 of the PSN Act]*

2.170 Under the existing section 48 of the APRA Act, APRA has power to appoint people to perform particular roles (for example, investigators and administrators under Division 2 of Part II of the Banking Act). As a consequence of inserting a statutory management regime into the Insurance and Life Insurance Acts, the Bill adds investigators and administrators appointed under Division 1A of Part VB of the Insurance Act or Division 1AA of Part 8 of the Life Insurance Act as additional examples in the Note. *[Schedule 6, item 2, section 48 of the APRA Act]*

Application and transitional provisions

2.171 The provisions of this Bill will apply from the date of Royal Assent.

Chapter 3

Directions powers

Outline of chapter

3.1 Schedules 1 to 3 to this Bill amend the Industry Acts to enhance the scope and efficacy of APRA's directions powers.

Context of amendments

3.2 The Industry Acts enable APRA to issue enforceable directions to regulated entities and authorised NOHCs in specified circumstances.

3.3 In most situations, APRA is able to address any prudential concerns that arise in relation to regulated entities by working cooperatively with the board and management and, where applicable, their authorised NOHC. In these instances, the board and senior management maintain full responsibility for decisions made by the regulated entity and, where applicable, the group of which it may be part.

3.4 However, there may be times when APRA considers it necessary to use more direct tools, such as its directions powers, to rectify or manage prudential concerns.

3.5 Directions powers enable APRA to compel a regulated entity to take specific action to address particular prudential issues that have been identified. Directions powers may also be necessary to limit further deterioration in the financial condition of a regulated entity in a period of emerging stress, and to facilitate the resolution of a distressed regulated entity.

3.6 By international standards, APRA's directions powers are reasonably comprehensive. However, refining and, where appropriate, enhancing the triggers that allow the issue of directions will help ensure that APRA can respond in a more timely and decisive way to emerging prudential concerns that affect an entity.

3.7 Equally, broadening the scope of the directions powers, both in respect of the matters on which directions may be given and the entities to which directions may be given, will assist APRA to respond effectively and promptly to resolve a distressed regulated entity.

3.8 A related issue is that in complying with an APRA direction, an entity, its directors or other officers may breach what would (but for the existence of the direction) normally be their obligations or duties under the Corporations Act or other law. Such a potential conflict of duties could give rise to delay and impede the effectiveness of APRA's direction powers, particularly in a crisis. The Bill therefore addresses this issue by introducing a specific immunity provision for an entity, its directors and management when complying with an APRA direction. This is consistent with the Key Attributes, which note the need for directors and other key officers of financial institutions to be protected from liability arising from compliance with directions.

Summary of new law

- 3.9 Schedules 1 to 3 to this Bill amend the Industry Acts to:
- extend APRA's ability to issue directions to subsidiaries of authorised NOHCs and subsidiaries of regulated entities;
 - clarify the scope of APRA's 'catch-all' directions power;
 - clarify that APRA may issue directions requiring entities to take specified actions to facilitate resolution, whether in normal times or during a crisis;
 - clarify that APRA may give directions despite external support being in place;
 - extend APRA's ability to issue recapitalisation directions to a regulated entity's authorised NOHC and certain other holding companies;
 - harmonise recapitalisation directions powers with general directions powers;
 - ensure that complying with an APRA direction will not be grounds for an entity, its directors or management to be held liable under any other law (subject to a good faith and reasonableness test);
 - harmonise the protection from liability provisions in the Industry Acts; and
 - provide for APRA to determine that the giving of a direction should be confidential.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Directions to subsidiaries</i>	
APRA may give directions to subsidiaries of authorised NOHCs and subsidiaries of regulated entities.	APRA does not have the power to give directions directly to subsidiaries of authorised NOHCs and subsidiaries of regulated entities.
<i>Catch-all directions power</i>	
APRA may give directions about other matters regarding the affairs of the regulated entity (including in relation to specific transactions and other matters).	It is unclear whether APRA has the power under the 'catch-all' ground to give directions regarding specific transactions involving the regulated entity.
<i>Pre-positioning directions power</i>	
APRA may give directions to require entities to take specified actions to facilitate resolution, whether during normal times or in an emerging stress.	It is unclear whether APRA has the power to give directions, or all the kinds of directions that might reasonably be necessary, to require regulated entities to take specified actions to facilitate resolution, both in normal times or in an emerging stress.
<i>Power to give directions despite external support being in place</i>	
APRA may give directions to insurers despite external support being in place.	It is unclear whether APRA may disregard external support for an insurer in deciding whether to give a direction.
<i>Scope of recapitalisation directions powers</i>	
Where APRA is giving a recapitalisation direction to a regulated entity, a corresponding direction may be given to the entity's authorised NOHC and any subsidiary of the authorised NOHC which is also a holding company of the regulated entity.	APRA does not have the power to give recapitalisation directions to authorised NOHCs or other holding companies of regulated entities.

<i>New law</i>	<i>Current law</i>
<i>Harmonise recapitalisation directions powers with general directions powers</i>	
<p>APRA may give a recapitalisation direction that can:</p> <ul style="list-style-type: none"> • deal with some or a particular class of matters; • specify time for compliance; • be varied by notice in writing if APRA considers that the variation is necessary and appropriate; and • be later revoked if APRA considers that the direction is no longer necessary or appropriate. 	<p>In relation to a recapitalisation direction, APRA does not have express power in the Industry Acts to:</p> <ul style="list-style-type: none"> • deal with some or a particular class of matters; • specify time for compliance; • vary the direction; or • revoke the direction.
<i>Protection from liability when complying with an APRA direction</i>	
<p>An entity, its directors or management will not be held liable for actions or omissions in good faith that are reasonable in order to achieve the purpose of complying with an APRA direction.</p>	<p>It is unclear that the general immunity provision in section 70A of the Banking Act provides an entity, its directors or management with the requisite level of immunity when complying with an APRA direction.</p>
<i>Streamline the protection from liability provisions in the Industry Acts</i>	
<p>A person will be protected from liability if they act in good faith and without negligence in the exercise or performance of powers, functions or duties under the Insurance and Life Insurance Acts. (This is separate from the special protection afforded for compliance with a direction.)</p>	<p>No equivalent provision of section 70A of the Banking Act is in the Insurance or Life Insurance Acts; although various provisions under the Insurance and Life Insurance Acts provide some protection for auditors and actuaries.</p>
<i>Confidentiality of certain directions</i>	
<p>APRA may make a determination that the giving of a direction should be confidential in certain circumstances.</p>	<p>Currently only APRA staff are subject to legislative secrecy obligations in relation to directions.</p>

Detailed explanation of new law

3.10 To assist with the operation of APRA’s directions powers under the Industry Acts, the Bill inserts a definition of ‘direction under this Act’ to mean a direction under any of the following provisions:

- sections 11CA, 11CC, 13E, 17, 23, 29 and 31F of the Banking Act;
- sections 17, 27, 49R, 74, 76, 78, 103B and 104 of the Insurance Act; or
- sections 27A, 125A, 230AB or 230B of the Life Insurance Act. *[Schedule 1, item 4, subsection 5(1) of the Banking Act; Schedule 2, item 1, subsection 3(1) of the Insurance Act; Schedule 3, item 110, Schedule Dictionary of the Life Insurance Act]*

General directions powers

Triggers for issuing directions to a regulated entity or authorised NOHC

3.11 Paragraphs 11CA(1)(c) of the Banking Act, 104(1)(b) of the Insurance Act, and 230B(1)(b) of the Life Insurance Act currently provide that APRA may give a direction to a body corporate if APRA has reason to believe that the body corporate is likely to contravene any one of certain listed laws and ‘such a contravention is likely to give rise to a prudential risk’.

3.12 The Bill amends these provisions to replace the condition that ‘such a contravention is likely to give rise to a prudential risk’ with ‘the direction is reasonably necessary for one or more prudential matters relating to the body corporate’. *[Schedule 1, item 33, paragraph 11CA(1)(c) of the Banking Act; Schedule 2, item 113, paragraph 104(1)(b) of the Insurance Act; Schedule 3, item 83, paragraph 230B(1)(b) of the Life Insurance Act]*

3.13 This amendment reflects that the term ‘prudential matters’ is specifically defined in the Industry Acts and so provides greater clarity to the relevant grounds for APRA’s directions powers. In addition, given the amendments to the definition of ‘prudential matters’ (see 10.14 to 10.17), this clarifies that APRA can direct a body corporate to take actions to address issues concerning their resolvability (or the resolvability of a group of which it is a member) for resolution purposes.

3.14 The Bill amends the grounds under the Industry Acts to enhance APRA’s ability to give a direction to a body corporate (a regulated entity or authorised NOHC) as a result of the conduct or circumstances of its subsidiaries. The new grounds are:

- APRA has reason to believe that:
 - a subsidiary has contravened a provision of the relevant Industry Act, a regulation (in the case of the

Banking Act, a prudential requirement regulation), a prudential standard or the FSCODA; or

- a subsidiary is likely to contravene an Industry Act, a regulation (in the case of the Banking Act, a prudential requirement regulation), a prudential standard or the FSCODA; or
 - a subsidiary is conducting its affairs in a way that may cause it to be unable to continue to supply services to the body corporate (IT or treasury functions for example); and
- APRA considers that the direction is reasonably necessary for one or more prudential matters relating to the regulated entity or authorised NOHC (prudential matters test).

3.15 The Bill also inserts additional grounds to enable APRA to give a direction to a body corporate (a regulated entity or authorised NOHC), if:

- APRA has reason to believe that:
 - the direction is in respect of a subsidiary and is necessary in the interests of depositors or policyholders of the regulated entity; or
 - the direction is in respect of a subsidiary and the failure to issue such a direction would materially prejudice the interests of depositors or policyholders of the regulated entity.

3.16 The Bill provides that these grounds, as well as the existing ground that a subsidiary is conducting its affairs in a way that may cause or promote instability in the Australian financial system, are not subject to the additional prudential matters test. This is because a prudential element is implicit in each of these three grounds themselves. *[Schedule 1, item 34, subsections 11CA(1AA) and 11CA(1AB) of the Banking Act; Schedule 2, item 114, subsections 104(1A) and 104(1B) of the Insurance Act; Schedule 3, item 84, subsections 230B(1AA) and 230B(1AB) of the Life Insurance Act]*

3.17 The amendments reflect the various circumstances in which the conduct of a subsidiary of a regulated entity or authorised NOHC may necessitate APRA giving a direction to the regulated entity or authorised NOHC. The amended triggers described in 3.14 also provide grounds for APRA to give directions directly to subsidiaries (see 3.22).

3.18 The Bill amends the Banking Act to provide that a decision of APRA to give a direction to an ADI or authorised NOHC to take action in relation to a subsidiary under subsection 11CA(1AA) as a result of the ground referred to in paragraph (1AA)(a), (b), (c) or (d), is reviewable internally and upon application to the Administrative Appeals Tribunal if the person disagrees with the internal review outcome. These grounds apply where APRA believes that: a subsidiary of the ADI/NOHC has contravened the Banking Act or FSCODA; a subsidiary of the ADI/NOHC has contravened a prudential requirement regulation or prudential standard; a subsidiary of the ADI/NOHC is likely to contravene any of these; or the direction in respect of the subsidiary is necessary in the interests of relevant depositors. These grounds broadly correspond to similar grounds for the giving of a direction to an ADI or an authorised NOHC which may currently be subject to such a review under the Banking Act. Equivalent changes are made to the Insurance Act and the Life Insurance Act. *[Schedule 1, item 42, subsection 11CA(5A) of the Banking Act; Schedule 2, item 119, subsection 104(10) of the Insurance Act; Schedule 3, item 106, subsection 236(1) of the Life Insurance Act]*

Directions to subsidiaries

3.19 APRA currently does not have power under the Industry Acts to issue a direction directly to subsidiaries of regulated entities or subsidiaries of authorised NOHCs.

3.20 APRA can instead indirectly influence the activities of other entities in the group by giving directions to the regulated entity or authorised NOHC to give instructions to their respective subsidiaries.

3.21 However, there is a risk of delay in the directions being acted on by the subsidiary, particularly if the board of the subsidiary in question is uncooperative or slow to comply with instructions. Time may be of the essence in resolving a failing regulated entity. It may therefore be important to avoid delays that could compromise the resolution of a regulated entity. The ability for APRA to issue a direction directly to a relevant subsidiary in certain circumstances could help avoid delay and improve the effectiveness of APRA's directions power.

3.22 The Bill amends the Industry Acts to enable APRA to issue a direction to a body corporate that is a subsidiary of the regulated entity, or of an authorised NOHC.

3.23 APRA may issue such a direction only if it has already given, or would otherwise be entitled to give, the regulated entity or authorised NOHC a direction under the subsections identified at 3.14 due to one or more of the grounds having been satisfied in respect of the subsidiary. *[Schedule 1, item 34, subsection 11CA(1AC) of the Banking Act; Schedule 2, item 114,*

subsection 104(1C) of the Insurance Act; Schedule 3, item 84, subsection 230B(1AC) of the Life Insurance Act]

3.24 The Bill enables regulations to be made under the Industry Acts to specify that a particular body corporate that is a subsidiary cannot be given such a direction. For example, regulations might carve out entities that are regulated under other legislation and subject to a separate directions powers regime. *[Schedule 1, item 34, subsection 11CA(1AD) of the Banking Act; Schedule 2, item 114, subsection 104(1D) of the Insurance Act; Schedule 3, item 84, subsection 230B(1AD) of the Life Insurance Act]*

3.25 The Bill also amends the Industry Acts to clarify that the different subsections setting out the triggers for directions do not limit each other. *[Schedule 1, item 34, subsection 11CA(1AE) of the Banking Act; Schedule 2, item 114, subsection 104(1E) of the Insurance Act; Schedule 3, item 84, subsection 230B(1AE) of the Life Insurance Act]*

3.26 The Bill amends the Banking Act to provide that a decision of APRA to give a direction to a subsidiary under subsection 11CA(1AC) as a result of the ground referred to in paragraph (1AC)(a) or (b), to the extent that the paragraph relates to a ground referred to in paragraphs (1AA)(a), (b), (c) or (d), is reviewable internally and upon application to the Administrative Appeals Tribunal if the person disagrees with the internal review outcome. These grounds apply where APRA believes that: the subsidiary has contravened the Banking Act or FSCODA; the subsidiary has contravened a prudential requirement regulation or prudential standard; the subsidiary is likely to contravene any of these; or the direction to the subsidiary is necessary in the interests of relevant depositors. These grounds broadly correspond to similar grounds for the giving of a direction to an ADI or an authorised NOHC which may currently be subject to such a review under the Banking Act. Equivalent changes are made to the Insurance Act and the Life Insurance Act. *[Schedule 1, item 42, subsection 11CA(5A) of the Banking Act; Schedule 2, item 119, subsection 104(10) of the Insurance Act; Schedule 3, item 106, subsection 236(1) of the Life Insurance Act]*

Catch-all directions power

3.27 The general directions powers in the Industry Acts provide a non-exhaustive list of the different kinds of directions that APRA may give to a regulated entity or authorised NOHC where the relevant pre-conditions are met.

3.28 Since the circumstances under which APRA may need to make a direction are difficult to identify before the event, the list currently also includes a ‘catch-all’ power for APRA to make a direction to do ‘anything else as to the way in which the affairs of the body corporate are to be conducted or not conducted’ (current paragraph 11CA(2)(p) of the Banking Act) or ‘to do, or refrain from doing, an act that relates to the

way in which the affairs of the body corporate are to be conducted or not conducted' (current paragraphs 104(3)(u) of the Insurance Act and 230B(2)(v) of the Life Insurance Act).

3.29 These 'catch-all' directions powers are intended to provide APRA with the flexibility to make directions about other matters regarding the affairs of the regulated entity that are not contemplated by the other kinds of general directions listed in the Industry Acts.

3.30 However, the reference to 'the way' in which the affairs of the body corporate are to be conducted could be interpreted narrowly to mean that directions under the 'catch-all' power are limited to the general manner in which a regulated entity carries on its business (for example, the regulated entity's systems and processes). On this narrow interpretation, the 'catch-all' might not necessarily extend to directions regarding specific transactions involving the regulated entity.

3.31 The Bill therefore amends the 'catch-all' directions power under the Industry Acts by deleting the reference to 'the way'. *[Schedule 1, item 37, paragraph 11CA(2)(r) of the Banking Act; Schedule 2, item 117, paragraph 104(3)(w) of the Insurance Act; Schedule 3, item 87, paragraph 230B(2)(x) of the Life Insurance Act]*

3.32 This amendment is intended to put beyond doubt that APRA has the power to make directions about particular matters or transactions of a regulated entity (as well as directions as to the 'way' in which such matters are conducted generally).

3.33 As with the other paragraphs in subsection 11CA(2) of the Banking Act (and the equivalent subsections 104(3) of the Insurance Act and 230B(2) of the Life Insurance Act), the reference to the 'body corporate' in the 'catch-all' power (and in the new paragraphs referred to under 'Pre-positioning directions power' in 3.34 to 3.39) is intended to refer either to the body corporate to which the direction is given or, if the direction is to cause a subsidiary to take an action, to the subsidiary.

Pre-positioning directions power

3.34 APRA's supervision of regulated entities includes working with them to ensure that viable contingency plans are in place for managing a crisis affecting the relevant ADI or insurer, and the group of which it may be part. Along with a wide and flexible set of crisis management powers, planning for resolution during normal times is an integral part of ensuring appropriate crisis preparedness. Consistent with the amendments in the Bill, APRA will further develop its framework for resolution planning, including formally reflecting this in its prudential framework through

standards and guidance, following appropriate consultation (see Chapter 10).

3.35 Resolution planning will include an assessment of whether APRA's crisis management powers can be used to resolve a relevant entity or group in a credible and orderly manner, and whether APRA considers there to be any existing obstacles to resolution. In cases where obstacles to resolution are identified through the planning process, APRA's supervision of regulated entities would include working with the relevant entity to address these obstacles in an appropriate way.

3.36 In order to provide an appropriate legislative basis for the resolution planning process, it is necessary for APRA to have a clear power to make prudential standards on resolution (see 10.17) and the power to enforce these prudential standards or otherwise require actions to facilitate resolution, through directions where necessary. As such, the Bill clarifies that APRA's directions powers allow it to require a regulated entity to implement appropriate pre-positioning measures to address obstacles to resolution.

3.37 The Bill amends the Industry Acts to empower APRA to give a direction to a regulated entity, authorised NOHC and subsidiaries to do any one or more of the following:

- to make changes to the body corporate's systems, business practices or operations; or
- to reconstruct, amalgamate or otherwise alter all or part of the business, structure or organisation of the body corporate or of the group constituted by the body corporate and its subsidiaries. [*Schedule 1, item 37, paragraphs 11CA(2)(p) and 11CA(2)(q) of the Banking Act; Schedule 2, item 117, paragraphs 104(3)(u) and 104(3)(v) of the Insurance Act; Schedule 3, item 87, paragraphs 230B(2)(v) and 230B(2)(w) of the Life Insurance Act*]

3.38 These amendments are intended to clarify that, where an appropriate precondition for the exercise of APRA's general directions power is met (for example, breach of a prudential standard), APRA can direct a regulated entity, authorised NOHC or their subsidiaries to take the necessary actions required to facilitate resolution. The wording is intended to cover a wide range of potential pre-positioning measures that APRA could direct, for example including changes to business processes or the operational structure of a group in order to facilitate continuity of critical functions of the regulated entity, or the continued provision of critical intra-group shared services, during a resolution. Such a direction could be given, in line with the prudential framework for resolution planning noted above, during normal times or in response to an emerging stress.

- 3.39 The Bill also amends the Industry Acts to clarify that:
- the kinds of direction that may be given are not limited by any other provision in the respective Parts (apart from subsection 11CA (2AA) of the Banking Act, which affords protection to holders of covered bonds); and
 - the kinds of direction that may be given under a particular paragraph are not limited by any other paragraph in that subsection. *[Schedule 1, item 38, subsections 11CA(2AAA) and 11CA(2AAB) of the Banking Act; Schedule 2, item 118, subsections 104(4B) and 104(4C) of the Insurance Act; Schedule 3, item 88, subsections 230B(3B) and 230B(3C) of the Life Insurance Act]*

Power to give directions despite external support being in place

3.40 The *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Act 2010* inserted subsections 11CA(1B) and (1C) in the Banking Act to ensure that APRA may give a direction to an ADI or authorised NOHC despite any external support being in force. This was intended to ensure that the provision of external support to a stressed entity, for example some form of temporary public support, would not fetter the ability of APRA to determine that the preconditions are met for giving a direction to the entity.

3.41 However, corresponding amendments were not made to the Insurance and Life Insurance Acts for this purpose, even though the directions powers under the Industry Acts are generally aligned.

3.42 The Bill amends the Insurance and Life Insurance Acts to clarify that APRA may disregard external support for an insurer in giving a direction. These amendments ensure consistency in the directions powers across the Industry Acts. *[Schedule 2, item 116, subsection 104(2A) of the Insurance Act; Schedule 3, item 86, subsection 230B(1B) of the Life Insurance Act]*

3.43 The Bill also enables regulations to be made under the Insurance and Life Insurance Acts to specify that a particular form of support is not external support. This enables the regulations to clarify any types of external support that are not to be disregarded by APRA in deciding to give a direction under the Insurance and Life Insurance Acts. This is consistent with the approach in the equivalent provision of the Banking Act. *[Schedule 2, item 116, subsection 104(2B) of the Insurance Act; Schedule 3, item 86, subsection 230B(1C) of the Life Insurance Act]*

Recapitalisation directions powers

Scope

3.44 The current Part II, Division 2, Subdivision AA of the Banking Act, Part IX, Division 1 of the Insurance Act, and Part 10A, Division 2, Subdivision A of the Life Insurance Act empower APRA to direct a regulated entity that is not subject to statutory or judicial management to increase its level of capital.

3.45 Presently, where APRA has given such a direction to a regulated entity, it could not use the recapitalisation directions powers to issue a corresponding direction to the regulated entity's authorised NOHC or other relevant holding companies.

3.46 In cases where a regulated entity is a subsidiary of an authorised NOHC, APRA's inability to issue a recapitalisation direction to the authorised NOHC or other relevant holding companies could significantly restrict the effectiveness of the recapitalisation direction power in facilitating the resolution of the regulated entity.

3.47 In particular, this becomes an issue where the direction would have the effect of requiring the regulated entity to seek additional capital from its holding company and these funds were unavailable at the holding company. The regulated entity's authorised NOHC, and any subsidiary of the authorised NOHC which is also a holding company of the regulated entity, would not be able to rely on the relevant provisions in the Industry Acts (including, for example the provisions overriding contracts and listing rules) to facilitate raising additional capital with which to recapitalise the regulated entity.

3.48 The Bill amends the Industry Acts to extend the definition of 'recapitalisation direction' to allow APRA to issue a recapitalisation direction to an authorised NOHC and any other intermediate holding company of the regulated entity. [*Schedule 1, item 9, subsection 5(1) of the Banking Act; Schedule 2, item 6, subsection 3(1) of the Insurance Act; Schedule 3, item 114, the Schedule Dictionary of the Life Insurance Act*]

Definitions – NOHC/NOHC subsidiary

3.49 The Bill inserts a new definition of 'NOHC/NOHC subsidiary' in the Industry Acts to mean a body corporate that is any of the following:

- an authorised NOHC; or
- a subsidiary of an authorised NOHC. [*Schedule 1, item 7, subsection 5(1) of the Banking Act; Schedule 2, item 4, subsection 3(1)*]

of the Insurance Act; Schedule 3, item 113, the Schedule Dictionary of the Life Insurance Act]

3.50 The Bill amends the Industry Acts to ensure that the recapitalisation divisions apply to the NOHC/NOHC subsidiary in the same way that it does for a regulated entity in certain circumstances. *[Schedule 1, item 90, section 13D of the Banking Act; Schedule 2, item 96, section 103A of the Insurance Act; Schedule 3, item 66, section 230AA of the Life Insurance Act]*

3.51 The result of these amendments is that the existing sections governing valuation requirements, compliance and non-compliance, supply of information, offences and exceptions to Part IV of the *Competition and Consumer Act 2010*, amongst other things, apply in respect of the new power to direct a NOHC/NOHC subsidiary to facilitate the recapitalisation of a regulated entity.

Recapitalisation direction by APRA to a NOHC/NOHC subsidiary

3.52 The precondition for issuing a recapitalisation direction to a NOHC/NOHC subsidiary is that APRA has firstly given a recapitalisation direction to a regulated entity, which is the ‘primary recapitalisation direction’.

3.53 For the purposes of facilitating compliance with the primary recapitalisation direction, APRA may then give the NOHC/NOHC subsidiary (or, if appropriate, several entities, for example a NOHC and a holding company of the ADI that is a subsidiary of the NOHC) a recapitalisation direction that requires it to do anything that is specified in the direction, provided that:

- the regulated entity to which the primary recapitalisation direction was given is a subsidiary of the NOHC/NOHC subsidiary; and
- the NOHC/NOHC subsidiary is registered as a company under the Corporations Act, and has share capital; and
- the business of the NOHC/NOHC subsidiary is not under the control of a statutory manager. *[Schedule 1, item 91, subsections 13E(1A) and 13E(1B) of the Banking Act; Schedule 2, item 98, subsections 103B(1A) and 103B(1B) of the Insurance Act; Schedule 3, item 68, subsections 230AB(1A) and 230AB(1B) of the Life Insurance Act]*

Additional contents of a recapitalisation direction

3.54 The Bill amends the Industry Acts to facilitate down streaming of the capital raised by the NOHC/NOHC subsidiary to the regulated entity.

3.55 To achieve this, the recapitalisation direction may direct the NOHC/NOHC subsidiary to do any of the following:

- issue shares, or rights to acquire shares, in the NOHC/NOHC subsidiary, or other capital instruments in the NOHC/NOHC subsidiary of a kind specified in the direction; or
- acquire shares, or rights to acquire shares, in the regulated entity, or other capital instruments in the regulated entity of a kind specified in the direction; or
- acquire shares, or rights to acquire shares, in a NOHC/NOHC subsidiary which is a subsidiary of the directed NOHC/NOHC subsidiary and of which the regulated entity is a subsidiary, or other capital instruments in that body corporate of a kind specified in the direction. *[Schedule 1, item 93, subsection 13F(1A) of the Banking Act; Schedule 2, item 101, subsection 103C(1A) of the Insurance Act; Schedule 3, item 71, subsection 230AC(1A) of the Life Insurance Act]*

Harmonisation of recapitalisation directions powers with general directions powers

3.56 The *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Act 2010* empowered APRA to issue a recapitalisation direction to an ADI or insurer. However, certain provisions relating to general directions powers were not extended to recapitalisation directions powers, even though these provisions are equally relevant.

3.57 The Bill amends the Industry Acts to replicate existing subsections from the general directions powers in the recapitalisation directions powers, so that APRA is able to give a recapitalisation direction which can:

- deal with some or a particular class of matters;
- specify time for compliance;
- be varied by notice in writing if APRA considers that the variation is necessary and appropriate; and
- be later revoked if APRA considers that the direction is no longer necessary or appropriate. *[Schedule 1, items 92 and 93, subsections 13E(5) to 13E(7) and 13F(1C) of the Banking Act; Schedule 2, items 100 and 101, subsections 103B(4) to 103B(6) and 103C(1C) of the Insurance Act; Schedule 3, items 70 and 71, subsections 230AB(4) to 230AB(6) and 230AC(1C) of the Life Insurance Act]*

3.58 The Bill amends the Insurance and Life Insurance Acts to clarify that APRA may disregard external support for an insurer in giving a general direction, and the Bill allows regulations to be made under the Insurance and Life Insurance Acts to specify that a particular form of support is not external support (see 3.40 to 3.43). Consequential amendments were also made to clarify that APRA may disregard external support for an insurer in giving a recapitalisation direction, and to enable regulations to be made to specify that a particular form of support is not to be considered external support. [*Schedule 2, items 97 and 99, paragraph 103B(1)(b) and subsection 103B(2A) of the Insurance Act; Schedule 3, items 67 and 69, paragraph 230AB(1)(b) and subsection 230AB(2A) of the Life Insurance Act*]

Immunities

Protection from liability when complying with an APRA direction

3.59 In recognition of the seriousness of situations in which directions may be given, the Industry Acts provide that non-compliance with a direction gives rise to criminal sanction. Consequently, a regulated entity, its directors and other officers, employees and agents must take reasonable steps to ensure compliance with a direction.

3.60 The Corporations Act imposes certain duties and obligations on a company and its directors and other officers, including the requirement for directors and other officers to exercise their powers and discharge their duties in the best interests of the company and for a proper purpose.

3.61 In addition to the duties and liabilities of a company and its directors and other officers under the Corporations Act, common law and equity, there may be other legislation that imposes both civil and criminal personal liability on company directors, officers, employees and agents for some actions taken on behalf of their companies. Some of these provisions may impose sanctions on a strict liability basis; others may deem a director liable for breaches by the company.

3.62 Given the range of duties imposed on a company and its directors and other officers (and, in some cases, on other employees and agents), there is a risk (or at least perceived risk) that a regulated entity or its directors, officers, employees or agents could be held liable for actions they take to ensure compliance with directions from APRA. This could result in reluctance to promptly comply with an APRA direction if there is a concern that, in doing so, they could potentially breach their duties, including those under the Corporations Act.

3.63 These potential conflicts of duty could cause delay in the implementation of an APRA direction, which could be particularly problematic in a stress scenario.

3.64 Section 70A of the Banking Act provides that a person is not subject to any liability to any person in respect of anything done, or omitted to be done, in good faith and without negligence in the exercise or performance, of powers, functions or duties under the Act. However, the actions of a regulated entity, its directors or officers in complying with an APRA direction may involve a choice of possible courses and as such may not all necessarily constitute actions that are in the performance of duties or functions under the Act for the purposes of section 70A, and therefore may not provide clear protection from liability under the Corporations Act or other law. There is no equivalent provision of section 70A in the Insurance or Life Insurance Acts.

Protection from liability

3.65 The Bill amends the Industry Acts to provide protection from liability for a regulated entity, its directors and other officers, senior managers, other employees and agents when complying with an APRA direction. The protection extends to directors and other officers, senior managers, other employees and agents of a body corporate that is in the same relevant group of bodies corporate (that is, a subsidiary of the directed body corporate, or a subsidiary of an authorised NOHC of the directed body corporate).

3.66 For a person to benefit from protection in relation to a direction given to a body corporate, the person must be one of the following:

- an officer or senior manager of the body corporate or of a member of a relevant group of bodies corporate of which the body corporate is also a member, with ‘officer’ having the same meaning as in section 9 of the Corporations Act; or
- an employee or agent of the body corporate, or of a member of a relevant group of bodies corporate of which the body corporate is also a member, with ‘employee’ being further defined to include a person engaged to provide advice or services;
- the body corporate or a member of a relevant group of bodies corporate of which the body corporate is also a member.
[Schedule 1, item 252, section 70AA of the Banking Act; Schedule 2, item 137, section 127C of the Insurance Act; Schedule 3, item 107, section 246B of the Life Insurance Act]

3.67 The amendments provide that any reasonable steps taken by such a person, acting in good faith, for the purpose of either complying with a direction (see 3.10), or the provisions related to the confidentiality of certain directions under the Industry Acts (see 3.87 to 3.92), will not

expose that person to any civil or criminal liability. The ‘reasonableness’ standard applies to the course of action taken by the person to facilitate the direction. The amendments provide that it is to be treated as reasonable for a person to do a thing, or omit to do a thing, in order to achieve a purpose unless no reasonable person in that person’s position would do the thing, or omit to do the thing, in order to achieve that purpose. *[Schedule 1, item 252, section 70AA of the Banking Act; Schedule 2, item 137, section 127C of the Insurance Act; Schedule 3, item 107, section 246B of the Life Insurance Act]*

3.68 The reference to acting in ‘good faith’ means that in some respects the scope of the immunity is narrower than that provided to statutory managers (see 2.95). Immunity is provided to a statutory manager (or a person acting on behalf of a statutory manager) unless their act or omission is in ‘bad faith’. This distinction is appropriate because a statutory manager will be a professional appointed by APRA and, given the important role they would be likely to play in a resolution, they need to be provided with a level of immunity equivalent to that which APRA itself has under section 58 of the APRA Act. *[Schedule 1, item 149, section 14C of the Banking Act; Schedule 2, items 56 and 58, sections 62ZM and 62ZOK of the Insurance Act; Schedule 3, items 51 and 52, sections 179AK and 179 of the Life Insurance Act]*

3.69 The amendments also clarify that this immunity is not limited by, and does not itself limit, any of the other immunities in the Industry Acts, nor section 58 of the APRA Act. *[Schedule 1, item 252, section 70AB of the Banking Act; Schedule 2, item 137, section 127D of the Insurance Act; Schedule 3, item 107, section 246C of the Life Insurance Act]*

Harmonise the protection from liability provisions in the Industry Acts

3.70 The Industry Acts currently provide protection from liability for certain persons when they exercise powers or discharge functions under the Acts. However, the provisions differ among the Acts in terms of scope and level of protection.

3.71 For example, as noted in paragraph 3.64, existing section 70A of the Banking Act provides protection from liability where a person acts in good faith and without negligence in the exercise of duties under the Act. This protection covers, for example, auditors who are under an obligation to provide information to APRA about the ADIs to which they have been appointed.

3.72 Under the Insurance and Life Insurance Acts there is no provision equivalent to section 70A of the Banking Act. However, existing section 49C of the Insurance Act does offer some protection for auditors and actuaries (where they act in good faith and without negligence), but it is limited to the provision of information to APRA.

3.73 Similarly, the Life Insurance Act protects auditors and actuaries in circumstances limited to the voluntary provision of information to APRA. Further, existing sections 89 and 99 of that Act protect auditors and actuaries by specifically providing for the conferral of qualified privilege (which is mainly relevant in a defamation context) in respect of statements made by them in certain circumstances.

3.74 As noted in paragraph 3.63, providing appropriate protection from liability for persons exercising powers or discharging functions under the Acts is important in ensuring that the relevant powers and functions are effective, particularly in a crisis situation where delays could be most problematic.

3.75 The Bill harmonises the general liability provisions in the Industry Acts by replicating section 70A of the Banking in the Insurance and Life Insurance Acts with appropriate modifications. *[Schedule 2, item 137, section 127B of the Insurance Act; Schedule 3, item 107, section 246A of the Life Insurance Act]*

3.76 As a result, the Bill repeals section 49C of the Insurance Act, and subsections 88A(2) and 98A(2) of the Life Insurance Act, respectively, as these specific immunities are made redundant by the introduction of a general immunity provision that provides broader protection for auditors and actuaries. *[Schedule 2, item 23, section 49C of the Insurance Act; Schedule 3, items 20 and 22, subsections 88A(2) and 98A(2) of the Life Insurance Act]*

3.77 The amendments also clarify that these immunities are not limited by, and do not themselves limit, any of the other immunities in the Industry Acts, nor section 58 of the APRA Act. *[Schedule 2, item 137, section 127D of the Insurance Act; Schedule 3, item 107, section 246C of the Life Insurance Act]*

Confidentiality of certain directions

3.78 The Industry Acts currently purport to include a secrecy requirement in relation to directions through a reference to Part 6 of the APRA Act. For example, section 11CF of the Banking Act provides that ‘information relating to directions and revocation of directions is subject to the secrecy requirements in Part 6 of the [APRA Act], unless the information has been published in the *Gazette*...’. This reference appears to be erroneous because Part 6 of the APRA Act does not operate to impose any confidentiality obligations on regulated entities or their employees, officers or contractors. Part 6 of the APRA Act operates to impose secrecy obligations upon APRA and its employees, who are bound by these provisions in any event without the need for such a cross-reference.

3.79 The Bill therefore repeals the following provisions:

- section 11CF, and subsections 13P(9), 29(9) and 31F(9) of the Banking Act;
- subsection 103L(9) and section 107 of the Insurance Act; and
- subsection 230AK(9) and section 230E of the Life Insurance Act;

to correct this error and to introduce a substantive new secrecy regime for regulated entities. *[Schedule 1, items 48, 103, 230 and 234, section 11CF, and subsections 13P(9), 29(9) and 31F(9) of the Banking Act; Schedule 2, items 111 and 125, subsection 103L(9) and section 107 of the Insurance Act; Schedule 3, items 81 and 94, subsection 230AK(9) and section 230E of the Life Insurance Act]*

Application

3.80 The new secrecy provisions apply if APRA has firstly given an entity (the ‘directed entity’) a direction under an Industry Act (see 3.10).

3.81 APRA may then make a determination that the direction is covered by the secrecy provision if APRA considers that such a determination is necessary to protect depositors/policyholders or to promote financial system stability in Australia.

3.82 This reflects the fact that in certain circumstances it may be appropriate to keep the giving of a direction confidential for a limited period in order to meet the aforementioned objectives. APRA may subsequently revoke the determination once it is no longer required.

3.83 As soon as practicable after making it, APRA must give the directed entity a copy of the determination.

3.84 The Bill provides that such determinations made by APRA are not legislative instruments. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*. *[Schedule 1, item 56, section 11CH of the Banking Act; Schedule 2, item 135, section 109 of the Insurance Act; Schedule 3, item 102 section 231 of the Life Insurance Act]*

3.85 APRA must also consider whether it is appropriate in the circumstances to make an additional determination to allow further disclosure within the regulated entity under the ‘Disclosure allowed by APRA’ exception (see 3.95). *[Schedule 1, item 56, subsection 11CH(5) of the Banking Act; Schedule 2, item 135, subsection 109(5) of the Insurance Act; Schedule 3, item 102, subsection 231(5) of the Life Insurance Act]*

3.86 In the unlikely circumstances that a determination may put the secrecy provision in potential conflict with the *Privacy Act 1988*, APRA would consider additional safeguards. For example, if a determination is made restricting disclosure of the fact that a direction was made, and the direction constituted or contained personal information about an individual, APRA would consider whether it is appropriate to make a determination allowing disclosure of relevant information about the direction to that individual in order to allow the individual access to the information consistent with Australian Privacy Principle 12.

Offence provision

3.87 The Bill amends the Industry Acts to introduce a criminal offence, punishable by imprisonment for two years, if a ‘person’ discloses information and the information reveals the fact that the direction was made.

3.88 A ‘person’ is defined as either:

- the directed entity;
- an officer, employee or contractor of the directed entity at a time on or after APRA gave the direction to the directed entity; or
- any other person who in the course of their employment has acquired information that reveals the fact that the direction was made.

3.89 The offence provision applies if APRA has made a determination that the direction is covered by the secrecy provision (see 3.81). Fault liability applies to the offence, meaning that in order to commit the offence it must be shown that a fault (or mental) element exists for each physical element. In relation to this offence, the person must have intended to disclose information. They must also have been aware that a determination had been made in relation to that information or have been reckless as to that possibility.

3.90 However, the offence provision does not apply if:

- the disclosure is authorised by another section of the secrecy provision (detailed below); or
- the disclosure is required by an order or direction of a court or tribunal. [*Schedule 1, item 56, section 11CI of the Banking Act; Schedule 2, item 135, section 109A of the Insurance Act; Schedule 3, item 102, section 231A of the Life Insurance Act*]

3.91 The evidentiary burden of the showing the matters in 3.90 rests on the person bound by the secrecy provision because they are best positioned to provide the evidence as it is within their knowledge. There is no broad-based exception to the offence for people bound by the secrecy provision who are authorised to disclose information under a Commonwealth or other law. In order to avoid a potential conflict between different laws, a person covered by the secrecy provision may approach APRA to seek a variation of the determination.

3.92 For clarity, paragraph 14.1(2)(b) of the *Criminal Code Act 1995* (standard geographical jurisdiction) would capture regulated entities operating internationally within the scope of the secrecy provision to the extent that their disclosure of information overseas has an impact in Australia, such as by precipitating market concerns about the financial soundness of the entity.

Authorised disclosure

3.93 The Bill inserts various grounds into the Industry Acts to allow the disclosure of information that reveals the fact that a direction covered by the secrecy provision was made, as outlined below.

Disclosure of publicly available information

3.94 The Bill amends the Industry Acts to allow a person captured by the secrecy provision to disclose information that reveals the fact that the direction was made if the information has already been lawfully made available to the public. [*Schedule 1, item 56, section 11CJ in of the Banking Act; Schedule 2, item 135, section 109B of the Insurance Act; Schedule 3, item 102, section 231B of the Life Insurance Act*]

Disclosure allowed by APRA

3.95 The Bill amends the Industry Acts to allow a person captured by the secrecy provision to disclose information that reveals the fact that the direction was made if APRA has made a determination allowing such disclosure.

3.96 In making such a determination, APRA can allow a specified person, in relation to a specified direction, or class of directions, to disclose specified information. As soon as practicable after making it, APRA must give the directed entity, and the specified person, a copy of the determination.

3.97 The Bill provides that such determinations made by APRA are not legislative instruments. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*.

3.98 APRA may also make a determination, by legislative instrument, for a specified *class* of persons, to disclose specified information in relation to a specified class of directions.

3.99 In giving a determination to allow disclosure, APRA may include conditions relating to any of the following:

- the kind of entities to which the disclosure may be made;
- the way in which the disclosure is to be made; or
- any other matter that APRA considers appropriate. *[Schedule 1, item 56, section 11CK of the Banking Act; Schedule 2, item 135, section 109C of the Insurance Act; Schedule 3, item 102, section 231C of the Life Insurance Act]*

Disclosure to legal representative for purpose of seeking legal advice

3.100 The Bill amends the Industry Acts to allow a person captured by the secrecy provision to disclose information that reveals the fact that the direction was made if:

- the disclosure is to the person's legal representative; and
- the purpose of disclosing such information is for the legal representative to provide legal advice, or another legal service, in relation to the direction. *[Schedule 1, item 56, section 11CL of the Banking Act; Schedule 2, item 135, section 109D of the Insurance Act; Schedule 3, item 102, section 231D of the Life Insurance Act]*

Disclosure allowed by APRA Act secrecy provision

3.101 The Bill amends the Industry Acts to allow a person captured by the secrecy provision to disclose information that reveals the fact that the direction was made if:

- the person is an APRA member, an APRA staff member, or a Commonwealth officer within the meaning of the *Crimes Act 1914* who has received information about the direction in the course of their employment and is therefore an 'officer' within paragraph (c) of the definition of that term in section 56 of the APRA Act; and
- the information is protected information, or is contained in a protected document within the meaning of section 56 of the APRA Act (APRA's secrecy provision); and

- the disclosure is in accordance with subsections 56(3), (4), (5), (5AA), (6), (6A), (7), (7A), (7B) or (7C) of the APRA Act.

3.102 The Bill also clarifies that disclosure of information in relation to a direction is not an offence under section 56 of the APRA Act if the disclosure is authorised by a particular section under the new secrecy provisions in the Industry Acts. *[Schedule 1, item 56, section 11CM of the Banking Act; Schedule 2, item 135, section 109E of the Insurance Act; Schedule 3, item 102, section 231E of the Life Insurance Act]*

Disclosure in circumstances set out in the regulations

3.103 The Bill inserts a regulations-making power into each of the Industry Acts to allow a person captured by the secrecy provision to disclose information if it is made in circumstances specified in the regulations. The penalty of imprisonment for 2 years is high so it is important to provide a regulations-making power to address circumstances that were unforeseen as at the time of the passage of this Bill. *[Schedule 1, item 56, section 11CN of the Banking Act; Schedule 2, item 135, section 109F of the Insurance Act; Schedule 3, item 102, section 231F of the Life Insurance Act]*

Disclosure for purpose

3.104 The Bill amends the Industry Acts to allow a person covered by the secrecy provision to disclose information that reveals the fact that the direction was made if:

- another person covered by the regime disclosed that information in accordance with the allowable grounds; and
- the disclosure by the relevant person is for the same purpose. *[Schedule 1, item 56, section 11CO of the Banking Act; Schedule 2, item 135, section 109G of the Insurance Act; Schedule 3, item 102, section 231G of the Life Insurance Act]*

3.105 As an example, this ground would allow disclosure by a solicitor who discloses to a barrister for the purposes of getting legal advice.

Exceptions operate independently

3.106 The Bill amends the Industry Acts to ensure that the grounds allowing disclosure under the secrecy provision do not limit each other. *[Schedule 1, item 56, section 11CP of the Banking Act; Schedule 2, item 135 section 109H of the Insurance Act; Schedule 3, item 102, section 231H of the Life Insurance Act]*

Consequential and minor amendments

Directions to subsidiaries

3.107 Consequential amendments are made due to the extension of the directions power to subsidiaries. *[Schedule 1, item 35, paragraph 11CA(1A)(b) of the Banking Act; Schedule 2, item 115, paragraph 104(2)(b) of the Insurance Act; Schedule 3, item 85, paragraph 230B(1A)(b) of the Life Insurance Act]*

3.108 Consequential amendments are made to the provisions in the Industry Acts relating to the supply of information about the issue and revocation of directions due to the extension of the directions power to subsidiaries. *[Schedule 1, items 44 to 47, section 11CE, of the Banking Act; Schedule 2, items 121 to 124, section 106 of the Insurance Act; Schedule 3, items 90 to 93, section 230D of the Life Insurance Act]*

3.109 Consequential amendments are made to the offence provisions in the Industry Act relating to non-compliance with a direction due to the extension of the directions power to subsidiaries. *[Schedule 1, items 49 to 55, section 11CG of the Banking Act; Schedule 2, items 126 to 134, section 108 of the Insurance Act; Schedule 3, items 95 to 101, section 230F of the Life Insurance Act]*

3.110 Further consequential amendments are made to section 65 of the Banking Act to capture subsidiaries, with the result being that subsidiaries may also be directed to comply with the Banking Act. That section currently provides that where an ADI or an authorised NOHC is convicted of an offence against this Act or the regulations, the Full Court of the Federal Court may, upon the application of the Attorney-General by motion, direct the ADI or NOHC to comply with the provision. Should the ADI or NOHC fail to comply, the Court may authorize APRA to assume control of, and to carry on, the business of the entity. As noted, this provision will be extended to subsidiaries. *[Schedule 1, items 246, 247 and 248, subsections 65(1) to 65(4) of the Banking Act]*

Recapitalisation directions power

3.111 Consequential amendments are made to the Industry Acts to capture a recapitalisation direction given to a NOHC/NOHC subsidiary. *[Schedule 1, items 94 and 95, subsections 13F(2) and 13F(3) of the Banking Act; Schedule 2, items 102 and 103, subsections 103C(2) and 103C(3) of the Insurance Act; Schedule 3, items 72 and 73, subsections 230AC(2) and 230AC(3) of the Life Insurance Act]*

3.112 Further consequential amendments are made to the Industry Acts to ensure that references to depositors, policyholders and policy owners, respectively, are correct. *[Schedule 1, items 100 and 101, subsections 13H(1A) and 13H(4) of the Banking Act; Schedule 2, items 108 and 109, subsections 103E(1A) and 103E(4) of the Insurance Act; Schedule 3, items 78 and 79, subsections 230AE(1A) and 230AE(4) of the Life Insurance Act]*

Clarification

3.113 Section 7 of the Life Insurance Act sets out the parts and provisions of the Life Insurance Act that APRA has general administration of. It does not clearly provide that APRA administers the part of the Life Insurance Act where the general directions power, recapitalisation directions powers and the prudential standard making power reside. The Bill clarifies that APRA has general administration over Part 10A 'Prudential standards and directions'. *[Schedule 3, item 2, paragraph 7(1)(a)(iia) of the Life Insurance Act]*

Application and transitional provisions

3.114 The amendments made by Schedule 1 of the Bill to section 11CA of the Banking Act (the general directions power in the Banking Act), subdivision AA of Division 2 of Part II of the Banking Act (recapitalisation directions) and section 65 of the Banking Act (directions by the Court) apply to directions given on and after the Bill receives Royal Assent. *[Schedule 1, items 253 and 254]*

3.115 The amendments made by Schedule 2 of the Bill to section 104 of the Insurance Act (general directions power) and Division 1 of Part IX of the Insurance Act (recapitalisation directions) apply to directions given on and after the Bill receives Royal Assent. *[Schedule 2, items 139 and 140]*

3.116 The amendments made by Schedule 3 of the Bill to section 230B of the Life Insurance Act (general directions power) and Subdivision A of Division 2 of Part 10A (recapitalisation directions) apply to directions given on and after the Bill receives Royal Assent. *[Schedule 3, items 118 and 119]*

Chapter 4

Transfer powers

Outline of chapter

4.1 Schedule 4 to this Bill amends the Transfer Act to enhance the operation and scope of APRA's compulsory transfer powers.

Context of amendments

4.2 Part 4 of the Transfer Act provides for compulsory transfers of business between regulated entities. Following amendments to the Act in 2008 and 2010, the compulsory transfer of business provisions now extend to ADIs (and related parties of ADIs), general insurers, and life companies.

4.3 Compulsory transfer of business powers are an important tool in the package of resolution options available to APRA. The Transfer Act enables some or all of the business of a regulated entity (including assets, liabilities, legal rights and obligations, data and systems) to be transferred to another regulated entity in the same category, which could include transfers to a newly established bridge entity or asset management vehicle.

4.4 APRA may effect a compulsory transfer without the need for the approval of owners, shareholders, creditors, or the separate novation (by private contractual means) of liabilities. The power to implement transfers in this way could be used, in the course of resolution, to facilitate the sale of all or part of the business of a distressed entity to one or multiple buyers, depending on the situation. This may be particularly relevant in ensuring the continuity of an entity's critical functions in resolution, where part or all of the regulated business of a regulated entity might be transferred to another existing regulated entity or a newly established bridge entity for this purpose.

4.5 By international standards, the existing Transfer Act provides a comprehensive framework for compulsory transfers of business in resolution. However, there are certain areas in which the provisions could be enhanced to provide APRA with greater flexibility and certainty when arranging a compulsory transfer in a resolution.

4.6 For example, in some situations, rather than transferring all of the assets and liabilities comprising the business of a failed regulated entity, it would be more expedient for APRA to be able to transfer ownership of the shares in the entity. Additional amendments, which ensure that compulsory transfer of business powers apply to certain related entities of a regulated entity, will further align the Transfer Act with international best practice. The Key Attributes note that resolution authorities should have at their disposal a broad range of resolution powers, including those necessary to effect transfers of business from a failed entity (and, in certain circumstances, its related entities), and the power to transfer the ownership of shares in a failed entity.

Summary of new law

- 4.7 Schedule 4 to this Bill amends the Transfer Act to:
- enable APRA to compulsorily transfer the shares in a failing regulated entity to another body corporate;
 - widen the scope of Part 4 of the Transfer Act to apply to related entities of insurers; and
 - remove the requirement for complementary State or Territory legislation to be in place in relation to transfers of business.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Compulsory transfer of shares</i>	
In certain circumstances aligned with the preconditions for a compulsory transfer of business under the Transfer Act, APRA may transfer the shares in a failing regulated entity from the existing shareholders to a body corporate.	Under the Transfer Act, APRA has no power to transfer the shares in a failing regulated entity to another body corporate.

<i>New law</i>	<i>Current law</i>
<i>Widening the scope to include related entities of insurers</i>	
In addition to what APRA may determine under the current law, APRA may determine that there is to be a total or partial transfer of business from a body corporate that is related to a general or life insurer (but is not itself an ADI, general insurer or life insurer) to another body corporate under certain circumstances.	Under the Transfer Act, APRA may determine that there is to be a total or partial transfer of business from a body corporate that is related to an ADI (but is not itself an ADI, general insurer or life insurer) to another body corporate under certain circumstances. There are no equivalent provisions in the Transfer Act in respect of a body corporate related to an insurer.
<i>Removing the requirement for complementary State or Territory legislation to be in place</i>	
APRA may give effect to transfers of business even in the absence of State or Territory legislation being in place to facilitate transfers of business.	For a transfer of business to occur, APRA must be satisfied that legislation to facilitate the transfer is in place in the State or Territory in which the transferring and receiving bodies are established.

Detailed explanation of new law

Compulsory transfer of shares

4.8 APRA's powers under the Transfer Act enable it to compulsorily transfer all of the assets and liabilities of a failing regulated entity to another regulated entity. However, there is no explicit power to transfer the failing entity's shares to another body corporate as a means of achieving the same outcome. This is because shares in an entity are not assets of the failing entity but rather are assets of the shareholders. The interest of a shareholder in a share is not 'business' that is transferrable under the Transfer Act.

4.9 The ability to transfer the shares of a failing regulated entity could in some circumstances provide a more efficient and simpler means of achieving an orderly resolution, than effecting a full transfer of all of the assets and liabilities of the entity.

4.10 The amendments in the Bill rely to a large extent on the existing architecture and mechanics of the Transfer Act to enable a compulsory transfer of shares in certain circumstances, with the majority of amendments being minor consequential changes to existing definitions and supporting provisions, as articulated below.

Title

4.11 The Bill amends the long title of the Transfer Act by inserting ‘to provide for transfers of shares and other interests in some kinds of financial institutions’. *[Schedule 4, item 1, Title of the Transfer Act]*

4.12 The Bill also amends the short title of the Transfer Act, which may be cited as the *Financial Sector (Transfer and Restructure) Act 1999*. *[Schedule 4, item 2, section 1 of the Transfer Act]*

4.13 These amendments reflect the expanded operation of the Act, which now provides for compulsory transfers of shares.

Definitions

4.14 The Bill amends a variety of definitions under subsection 4(1) of the Transfer Act to enable a compulsory transfer of shares.

4.15 Firstly, the Bill amends paragraph (b), and includes a new paragraph (c), in the definition of ‘certificate of transfer’ to mean the following, respectively:

- in relation to a voluntary transfer of business – a certificate issued under section 18;
- in relation to a compulsory transfer of business – a certificate issued under section 33; and
- in relation to a compulsory transfer of shares – a certificate issued under section 33. *[Schedule 4, item 4, subsection 4(1) of the Transfer Act]*

4.16 The Bill amends the definitions of ‘partial transfer’ and ‘total transfer’, to mean, respectively:

- a partial transfer means a transfer of business described in existing subsection 8(2) (which provides that a transfer of business is a partial transfer if it relates to some, but not all, of the transferring body's business); and
- a total transfer means a transfer of business described in existing subsection 8(3) (which provides that a transfer of business is a total transfer if it relates to all of the transferring body's business. *[Schedule 4, items 7 and 13, subsection 4(1) of the Transfer Act]*

4.17 The Bill amends the definition of ‘compulsory transfer determination’, to mean:

- a compulsory transfer of business determination; or
- a compulsory transfer of shares determination.

4.18 The Bill further defines these two new terms as:

- ‘compulsory transfer of business determination’ means a determination under existing section 25 (the section conferring power on APRA to determine a compulsory transfer of business in certain situations); and
- ‘compulsory transfer of shares determination’ means a determination under section 25AA (which is a new provision inserted by the Bill, discussed below). *[Schedule 4, items 5 and 6, subsection 4(1) of the Transfer Act]*

4.19 These amendments clarify that there are now two potential options available to APRA under which to determine a compulsory transfer.

4.20 The Bill expands the definition of ‘receiving body’ to clarify that in relation to a transfer of shares under Part 4 of the Transfer Act, the receiving body is a body corporate to which shares in another body corporate are to be transferred, or have been transferred under that Part. *[Schedule 4, item 8, subsection 4(1) of the Transfer Act]*

4.21 This amendment is to differentiate a receiving body in the context of the two different types of compulsory transfers.

4.22 The Bill also expands the definition of ‘transferring body’ to clarify that in relation to a transfer of shares under Part 4, the transferring body is a body corporate, shares in which are to be transferred, or have been transferred, to another body corporate under that Part’. *[Schedule 4, item 14, subsection 4(1) of the Transfer Act]*

4.23 This amendment is to ensure that the existing architecture and mechanics of the Transfer Act can apply in the context of a share transfer. However, it is recognised that in the case of a transfer of shares, the actual transfer of ownership will be from the holders of the shares, not from the body corporate itself.

4.24 Separately, the Bill extends the definition of ‘regulated body’ to include a general insurer, and subsequently extends the definition of ‘regulated business’ to include a general insurer’s business (within the meaning of the Insurance Act). *[Schedule 4, items 9 and 10, subsection 4(1) of the Transfer Act]*

4.25 These amendments correct technical errors in the Transfer Act, which did not previously include a general insurer in the definitions, despite the compulsory transfer provisions applying equally to general insurers as a result of amendments to the Transfer Act in 2010. It should be noted that these amendments will not bring general insurers within the voluntary transfer of business provisions in Part 3 of the Transfer Act.

4.26 The Bill repeals the existing definition of ‘related’ in the Transfer Act and inserts a new definition of ‘related’ and a separate definition of ‘related body corporate’. The existing stand-alone definition of ‘related’ (in relation to bodies corporate) is replaced with a standard definition providing that whether a body corporate is related to another body corporate is to be determined in the same way as in the Corporations Act. This does not change the substantive meaning of the term ‘related’ in the Transfer Act. *[Schedule 4, items 12 and 15, subsection 4(1) and section 4A of the Transfer Act]*

4.27 The Bill extends the meaning of ‘share’ to mean:

- a legal or equitable right or interest in a share; and
- an interest in a share that is an interest of a kind specified in the regulations. *[Schedule 4, item 79, section 36AD of the Transfer Act]*

4.28 The adoption of a broad definition for ‘share’, including the ability to specify additional interests in regulations, ensures that the powers in the Transfer Act can operate to transfer all relevant ownership interests in the shares of the regulated entity.

Substantive transfer of shares amendments

4.29 The Bill amends the overview provisions in existing section 8 of the Transfer Act to include a transfer of shares as a kind of transfer that is permitted under the Act, noting that the Act also provides for compulsory transfers of shares in regulated entities. *[Schedule 4, item 19, subsection 8(1A) of the Transfer Act]*

4.30 For a compulsory transfer of shares to take effect, APRA must:

- assuming the preconditions for doing so are satisfied (see 4.35), make a determination (the compulsory transfer of shares determination) that there is to be a transfer of shares in a body (the transferring body) to another body corporate (the receiving body); and
- issue a certificate (the certificate of transfer) stating that the transfer is to take effect under existing section 33 of the Act.

4.31 For clarity, the transfer of shares takes effect when the certificate of transfer comes into force. [*Schedule 4, item 22, subsection 8(5A) of the Transfer Act*]

4.32 Separately, the Bill inserts notes into the Transfer Act to clarify that regulated entities making applications under the voluntary provisions in Part 3 cannot be general insurers. [*Schedule 4, items 20 and 23, subsections 8(4) and 9(1) of the Transfer Act*]

4.33 This is because the Insurance Act provides the mechanism for facilitating a voluntary transfer of a general insurer's business (see existing Part III Division 3A of the Insurance Act).

Preconditions for a transfer of shares

4.34 The Bill amends the Transfer Act to specify the preconditions under the Act that must be satisfied for a compulsory transfer of shares to be determined.

4.35 APRA may only make a compulsory transfer of shares determination if any of the following preconditions are met:

- for an ADI, either the Minister has declared that a transfer of shares should occur, or APRA is satisfied that any of the various specified conditions have been satisfied;
- for a life insurance company, APRA is satisfied that any of the various conditions have been satisfied; or
- for a general insurer, APRA is satisfied that any of the various conditions have been satisfied; and
- APRA has considered the interests of depositors or policy owners (as applicable) of the transferring body (when viewed as a group) and considers that, having regard to their interests, it would be appropriate for the transfer to be made; and
- if the receiving body is an ADI, life company or general insurer, APRA is satisfied that the transfer is appropriate, having regard to the interests of depositors or policy owners of the receiving body (as applicable) when viewed as a group; and
- the conditions relating to the consent of the receiving body, the interests of the financial system as a whole and other

relevant matters, and the consent of the Minister (or a decision by the Minister that their consent is not required).

4.36 The amendments provide that APRA cannot make a compulsory transfer of shares determination if the transferring body is any of the following:

- a foreign ADI (has the same meaning as in the Banking Act);
- a foreign general insurer (has the same meaning as in the Insurance Act); or
- an eligible foreign life insurance company (has the same meaning as in the Life Insurance Act).

4.37 APRA, in making a determination, must include particulars of the transfer, including the names of the transferring body and the receiving body, as well as a statement of the reasons detailing why the determination has been made.

4.38 The Bill provides that such determinations made by APRA are not legislative instruments. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*. [*Schedule 4, item 55, section 25AA of the Transfer Act*]

Ministerial declaration

4.39 The Bill extends the scope of existing section 25A in the Transfer Act to allow the Minister to also declare that a compulsory transfer of shares in a specified ADI to another specified body corporate can occur.

4.40 The Bill provides that such declarations made by the Minister are not legislative instruments. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*. [*Schedule 4, item 56, section 25A of the Transfer Act*]

4.41 The Bill extends the scope of existing section 29 in the Transfer Act to also provide that a Minister's consent to a compulsory transfer of shares is not required if the Minister has determined prior that his or her consent is not required in relation to the transfer. [*Schedule 4, items 62 and 63, subsection 29(1) of the Transfer Act*]

4.42 The Bill further clarifies the status of determinations made under existing subsection 29(1) to bring consistency and certainty to the legislation. As a result, for a determination dealing with the consent for a

particular transfer, the Bill clarifies that this is not a legislative instrument. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*. Alternatively, for a determination that consent is not required in relation to a class of transfers, the Bill clarifies that this is a legislative instrument. [*Schedule 4, item 64, subsections 29(2) and 29(3) of the Transfer Act*]

Content of a compulsory transfer of shares determination

Agreements about matters connected with the transfer

4.43 The Bill extends the scope of existing section 30 in the Transfer Act to also include a compulsory transfer of shares. In this instance, the transferring and receiving bodies may provide APRA with a written statement specifying a mechanism for determining things that are to happen, or that are to be taken to happen, in relation to a transfer of shares. [*Schedule 4, item 65, subsection 30(1) of the Transfer Act*]

4.44 This mechanism, read in conjunction with existing subsection 35(3) of the Transfer Act, can be used to ensure that legal and practical issues arising from the transfer of shares are dealt with, resolved or satisfied, or this is taken to be the case. This might be relevant, for example, where registration requirements need to be addressed following a transfer of shares.

Certificate of transfer

4.45 The Bill extends the scope of existing section 33 in the Transfer Act to also include a compulsory transfer of shares, so that APRA can rely on the existing machinery to specify provisions within the certificate of transfer to help facilitate a transfer of shares. [*Schedule 4, item 73, subsection 33(3) of the Transfer Act*]

4.46 This amendment affords APRA flexibility to include provisions specifying, or specifying a mechanism for determining, things that are to happen, or that are taken to be the case, in relation to shares that are to be transferred, or in relation to the transfer of shares that is to be effected.

Process for a compulsory transfer of shares determination

4.47 The Bill amends the Transfer Act to specify the timing and effect once a compulsory transfer of shares has been determined.

In this instance, when the certificate of transfer comes into force, all the shares in the transferring body, wherever those shares are located, become shares held by the receiving body without any transfer, conveyance or

assignment, and free from any trust, liability or other encumbrance.
[Schedule 4, item 76, section 35A of the Transfer Act]

4.48 All the shares in the transferring body, wherever those shares are located, become (respectively) shares held by the receiving body without any transfer, conveyance or assignment, and free from any trust, liability or other encumbrance. *[Schedule 4, item 76, section 35A of the Transfer Act]*

Ancillary provisions

Regulations

4.49 The Bill inserts a regulations-making power in the Transfer Act to allow special provisions to be made in regard to a compulsory transfer of shares. As such, the regulations may provide in relation to any of the following matters:

- the payment to the holder of shares in the transferring body of a purchase price for those shares;
- the resolution of disputes involving a holder of shares in the transferring body (including the resolution of such disputes by the Federal Court);
- the conferral of jurisdiction on the Federal Court for the purpose of the resolution of such disputes;
- the publication of information relating to the compulsory transfer of shares by APRA, the transferring body and the receiving body;
- the freeing of shares in the transferring body from any trust, liability or other encumbrance when they become shares held by the receiving body; and
- any matter incidental to the compulsory transfer of shares, or proposed compulsory transfer of shares, or any of the other matters mentioned in this subsection. *[Schedule 4, item 79, subsection 36AE(1) of the Transfer Act]*

4.50 In the case of a transfer of shares, calculating and arranging payment of a purchase price or compensation to shareholders (who may be numerous), and/or persons who have securities or similar interests in relation to shares, might require special arrangements. Rather than set out detailed machinery for these sorts of arrangements in the Bill, it will be possible to do so in the regulations. This is not intended to limit APRA's ability to provide for such matters and payment and compensation in

approved section 30 statements or under a certificate of transfer. The regulations may also address other incidental matters relating to compulsory share transfers. It is not intended that this limit the general regulation-making power in section 47 of the Transfer Act. Existing section 44 of the Transfer Act, which provides for compensation in certain circumstances where there has been a compulsory transfer of business, will also apply as a 'safety net' to a compulsory transfer of shares. *[Schedule 4, item 79, subsection 36AE(3) of the Transfer Act]*

4.51 The regulations may prescribe penalties, not exceeding 50 penalty units, for offences against the regulations. It is not anticipated that this will be used extensively, but if it is, a possible example of use may be to ensure that false or improper claims for compensation are not made in relation to any arrangements of the kind described above. *[Schedule 4, item 79, subsection 36AE(2) of the Transfer Act]*

Information sharing

4.52 The Bill extends the scope of existing section 42 in the Transfer Act to allow APRA to provide information (including personal or confidential commercial information) to the receiving body in connection with:

- the transferred shares; and
- the business of the transferring body. *[Schedule 4, item 92, section 42 of the Transfer Act]*

4.53 For clarity, information about the business of the transferring body would be covered by the secrecy provision under section 56 of the APRA Act, so this amendment would allow APRA to share information with the receiving body without breaching the secrecy provision.

Widening the scope to include related entities of insurers

4.54 Currently, under subsection 25(1B) of the Transfer Act, APRA may determine that there is to be a total or partial compulsory transfer of business from a body corporate related to an ADI, which is not itself an ADI, general or life insurer, to another body corporate in certain circumstances.

4.55 This may be necessary, for example, where an ADI's assets and liabilities are being transferred under the Transfer Act as part of a resolution, and a related entity of the ADI provides critical intra-group services essential to the ADI's continued operation. The same rationale applies to insurers but there is no equivalent to subsection 25(1B) in respect of a body corporate related to an insurer.

4.56 The Bill amends the Transfer Act to enable APRA to make a determination concerning a transfer from a body corporate related to an insurer to another body. *[Schedule 4, items 47 and 52, subsections 25(1DA) and 25(1G) of the Transfer Act]*

4.57 The Bill also amends existing subsections 25(1D) and 25(1F) in the Transfer Act by omitting ‘only the business’ and substituting ‘only business’. *[Schedule 4, items 45 and 50, subsections 25(1D) and 25(1F) of the Transfer Act]*

4.58 Accordingly, instead of reading ‘APRA may make a written determination that there is to be a transfer of *only the business* that is not regulated business from [an insurer] to a body corporate that is not [an insurer]’ these subsections will provide ‘APRA may make a written determination that there is to be a transfer of *only business* that is not regulated business from [an insurer] to a body corporate that is not [an insurer]’.

4.59 These amendments clarify that a transfer of unregulated business of a regulated entity to a non-regulated entity does not have to be a transfer of all the unregulated business of the transferor.

Removing the requirement for complementary State or Territory legislation to be in place

4.60 To give effect to transfers of business, the Transfer Act currently imposes the precondition that APRA be satisfied that legislation to facilitate the transfer must be in place in the State or Territory in which the transferring and receiving bodies are established.

4.61 A number of other Commonwealth transfer regimes, for instance those under the Insurance and Life Insurance Acts, do not impose preconditions of this nature. Although this is a matter which APRA and other relevant bodies would expect to address in the ordinary course, the absence of such State or Territory legislation should not prevent APRA from making a transfer of business under the Transfer Act.

4.62 The Bill therefore amends the Transfer Act so that APRA may make a voluntary or compulsory transfer determination, even in the absence of relevant State or Territory legislation. *[Schedule 4, items 28 to 31, 53, 54, 59 and 61, paragraphs 11(1)(d) and 25(2)(f), subsections 11(1A) and 25(2A), and sections 14 and 28 of the Transfer Act]*

4.63 The Bill clarifies that the requirement for State or Territory legislation referred to in paragraph 25(2)(f) must include provision to ensure that when a certificate of transfer comes into force under Division 3 of the Transfer Act, the receiving body is taken to be the successor in

law to the transferring body (to the extent of the transfer). This only applies in relation to a compulsory transfer of business. This requirement does not apply to a compulsory transfer of shares. *[Schedule 4, item 60, section 28 of the Transfer Act]*

Consequential amendments

Compulsory transfer of shares and restructure approvals

4.64 The Bill makes consequential amendments to Part 4A of the Transfer Act (Restructures) to widen the application of that Part so that it covers a restructure arrangement (under Part 5.1 of the Corporations Act) that facilitate compliance with a requirement under a direction or prudential standard. *[Schedule 4, items 80 to 86, sections 36A to 36L of the Transfer Act]*

4.65 Part 4A of the Transfer Act currently applies to a restructure that for the purposes of making a regulated entity (an ‘operating body’) a subsidiary of a NOHC. An operating body may apply to the Minister for a restructure approval, including a restructure instrument. A restructure instrument may give relief to the operating body and group entities from certain provisions in Division 1 of Part 2J.1, or Part 2J.2, of the Corporations Act in relation to restrictions on share capital and the self-acquisition of shares. A restructure instrument may also give relief from section 254T of the Corporations Act, which relates to the circumstances in which dividends may be paid. The instrument comes into force when a court makes an order under subsection 411(4) of the Corporations Act approving the restructure arrangement. Further, if the Minister issues a restructure approval, APRA may issue internal restructure certificates giving effect to the transfer of specified assets and liabilities between entities within the group.

4.66 As a result of the amendments to Part 4A, an operating body (an ADI, general insurer or life insurer) may apply to the Minister for a restructure approval where the restructure would facilitate compliance by the operating body (or a related body corporate of the operating body) with a direction (under section 11CA of the Banking Act, 104 of the Insurance Act or 230B of the Life Insurance Act) or prudential standard. (under section 11AF of the Banking Act, 32 of the Insurance Act or 230A of the Life Insurance Act). This would include, for example, a restructuring to meet general requirements of a prudential standard relating to group structure for the purposes of addressing potential barriers to resolution during normal times, in case a crisis should occur at some time in the future. *[Schedule 4, items 80 to 83, sections 36A and 36B of the Transfer Act]*

4.67 As is currently the case in relation to NOHC restructures of the kind currently covered by Part 4A of the Transfer Act, the Minister may impose conditions on a restructure approval made under the amended provisions. *[Schedule 4, item 84, section 36E of the Transfer Act]*

4.68 A restructure approval under the amended Part 4A may include a restructure instrument granting relief from Part 2J.1, or Part 2J.2 and section 245T of the Corporations Act, as is currently the position. *[Schedule 4, item 85, section 36G of the Transfer Act]*

4.69 APRA's power to issue an internal transfer certificate, giving effect to the transfer of assets and liabilities for the purposes of the restructure, is extended to cover both types of restructures under the amended Part 4A (that is, the kinds of NOHC restructures currently covered, and the prudential/direction restructures covered by the amended provisions). *[Schedule 4, item 86, section 36L of the Transfer Act]*

4.70 Consequential amendments are also made to the information-gathering power in existing section 41 of the Transfer Act. *[Schedule 4, items 88 to 91, section 41 of the Transfer Act]*

4.71 Section 41 currently confers power on APRA to exercise information-gathering powers in the Industry Acts for purposes connected with a voluntary or compulsory transfer of business under the Transfer Act. The situations where APRA can currently use those powers to obtain information are where a transfer is from or to an ADI or from or to a life company. APRA may also obtain information for the purposes of an internal restructure of a group that includes an ADI, life company or general insurer.

4.72 The amendments will ensure that the information-gathering powers apply in the following additional situations. First, they will correct a gap in subsection 41(3) which does not currently allow APRA to use the Insurance Act information-gathering powers to obtain information for the purposes of a (compulsory) transfer of business from or to a general insurer. Secondly, it will be possible to use the information-gathering powers for the purposes of a transfer of shares in an ADI, general insurer or life insurer. In summary, the powers may be used to obtain information for the purposes of: a transfer of business from or to an ADI, general insurer or life company; a compulsory transfer of shares in an ADI, general insurer or life company; and an internal restructure (under Part 4A of the Transfer Act) of a group that includes an ADI, general insurer or life company. *[Schedule 4, items 88 to 91, section 41 of the Transfer Act]*

4.73 The Bill makes consequential amendments to the Transfer Act to insert provisions and update references in multiple provisions to reflect

the addition of a compulsory transfer of shares, and to help differentiate where necessary between the two different types of compulsory transfer available under the Act. *[Schedule 4, items 16 to 18, 21, 22, 32 to 38, 42, 47, 50, 52, 57, 58, 63, 66 to 72, 74, 75, 79, 87 and 93 to 95, paragraphs 8(1)(a), 8(1)(b), subsection 8(1), paragraph(8)(5)(a), subsection 8(5), paragraph 24(1)(a), subsections 24(1A) and 24(1B), 24(2) to 24(5), paragraphs 25(1B)(a), 25(1DA)(a), subsection 25(1F) paragraph 25(1G)(a) section 26, subsection 27(1), section 29, subsection 31(1), paragraphs 31(1)(a), 31(1)(b), section 32, paragraphs 33(1)(c), 33(2)(b), 33(2)(c), section 35, subsection 35(1), section 36AC, paragraphs 37(1)(c) and 37(1)(d), subsections 43(4), 43(9), and paragraphs 43(9A)(a) and 43(9A)(b) of the Transfer Act]*

4.74 The Bill amends the existing paragraphs 25(1)(a)(iii) and (v) to correct an anomaly in the existing provisions. Under section 13A of the Banking Act, APRA has power to investigate an ADI or appoint a person to investigate the ADI. APRA also has power to take control of an ADI or appoint a person to take control of the ADI. The intention is that each of these four actions be a potential trigger for transfer of business (subject of course to any other relevant preconditions being satisfied as well). However the wording of the existing paragraphs (iii) and (iv) only covers where APRA has appointed an investigator and where APRA has appointed a statutory manager (the latter inadvertently being covered twice, once in each paragraph). The amendments will correct this by defining the relevant preconditions as APRA investigating or appointing a person to investigate, or a statutory manager being appointed (which will cover both where APRA is the statutory manager and where APRA appoints an administrator as statutory manager). *[Schedule 4, item 41, paragraph 25(1)(a) of the Transfer Act]*

4.75 The Bill makes consequential amendments to the *Income Tax Assessment Act 1997*, *Insurance Act*, *Life Insurance Act*, *APRA Act* and *PSN Act* to update references to reflect the new short title of the *Transfer Act*. *[Schedule 2, item 51, paragraph 62ZI(2)(aa) of the Insurance Act; Schedule 3, items 46 and 61, paragraph 175(2)(aa) and subsection 190(5) of the Life Insurance Act; Schedule 5, item 2, section 5 of the PSN Act; Schedule 6, item 1, paragraph 3(1)(f) of the APRA Act; Schedule 7, items 4, 5, 6, 9, 10, and 11, paragraph 202-47(1)(a), section 320-300, paragraphs 320-305(b), 615-35(a), subsection 703-37(1) and paragraph 703-37(4)(a) of the Income Tax Assessment Act 1997;*

4.76 The Bill makes consequential amendments to the *Insurance and Life Insurance Acts* to include a compulsory transfer of shares as a possible course of action that a judicial manager can recommend in its report. *[Schedule 2, item 52, paragraph 62ZI(2)(ab) of the Insurance Act; Schedule 3, item 47, paragraph 175(2)(ab) of the Life Insurance Act]*

4.77 The Bill amends the triggers for a transfer of business from a life insurance company or general insurer to include the appointment of a statutory manager to the insurer as a trigger (subject to any other relevant preconditions for transfer). *[Schedule 4, items 44, 46, 49 and 51, paragraphs 25(1C)(a)(iv), 25(1D)(a)(iii), 25(1E)(a) and 25(1F)(a)(iii) of the Transfer Act]*

4.78 The Bill clarifies that section 28, which sets out the matters to be included in State or Territory legislation supporting transfers of business, is enacted only for the purposes of paragraph 25(2)(f). As noted above, paragraph 25(2)(f) will be amended to provide that APRA must consider whether such legislation is in place in certain circumstances but may decide to undertake a transfer of business even if it is not or does not meet the requirements of section 28. Neither paragraph 25(2)(f) nor section 28 will apply to a compulsory transfer of shares under Part 4 [*Schedule 4, item 61, subsection 28(2) of the Transfer Act*]

Chapter 5

Conversion and write-off of capital instruments

Outline of chapter

5.1 Schedules 1-3 and 7 to this Bill amend the Industry Acts and the Corporations Act to provide certainty that capital instruments can be converted or written off as provided for in APRA's prudential standards.

Context of amendments

5.2 APRA's prudential standards require regulated entities to maintain minimum levels of regulatory capital. The prudential standards currently establish three categories of regulatory capital – 'Common Equity Tier 1' (CET1), 'Additional Tier 1' (AT1), and 'Tier 2' (T2) capital. AT1 and T2 capital instruments comprise securities (preference shares and subordinated notes, for example) that satisfy the eligibility criteria for AT1 and T2 capital set out in APRA's prudential standards.

5.3 In relation to AT1 and T2 capital, the prudential standards include particular requirements on the capacity of an instrument to 'absorb' losses experienced by a regulated entity through the conversion or write-off of these instruments in certain circumstances.

5.4 Under APRA's current prudential standards, the terms of AT1 and T2 instruments must provide that they absorb losses in the event of a 'non-viability trigger event'.³

³ Non-viability trigger events are described in Prudential Standard APS 111 Capital Adequacy – Measurement of Capital, Prudential Standard GPS 112 Capital Adequacy – Measurement of Capital, and Prudential Standard LPS 112 Capital Adequacy – Measurement of Capital. For example, for a capital instrument issued by an ADI incorporated in Australia, a non-viability trigger event is:

- (a) the issuance of a notice in writing by APRA to the ADI that conversion or write-off of capital instruments is necessary because, without it, APRA considers that the regulated entity would become non-viable; or

5.5 Further, in order for AT1 instruments that are accounted for as liabilities to be considered as regulatory capital of an ADI, they must also convert or be written off where the ADI holds CET1 capital equal to or less than 5.125 per cent of its risk weighted assets (as calculated using the relevant capital requirements set by APRA's prudential standards).

5.6 APRA's prudential framework provides for two mechanisms by which AT1 and T2 capital instruments may absorb losses: conversion of those instruments into ordinary shares (or equivalent for mutually-owned ADIs); or the write-off of the instruments.

5.7 While such provisions in AT1 and T2 capital instruments are expected to function in accordance with their terms, APRA and market participants have identified some potential legal impediments to the effective operation of conversion or write-off provisions in AT1 and T2 capital instruments in certain circumstances.

5.8 It is important that contractual conversion and write-off provisions in AT1 and T2 capital instruments operate as intended in the event that the circumstances of a regulated entity meet the relevant conditions.

5.9 In June 2014, the Government released a consultation paper on proposals to make certain the effective operation of contractual loss absorption provisions in regulatory capital instruments. The amendments described in this chapter follow from that consultation.

5.10 The amendments are applied to capital instruments other than those issued as AT1 or T2 capital to provide flexibility in the event of future changes to the regulatory capital framework. In order for the amendments to apply, any such instrument will need to be issued with terms included for the purposes of conversion and write-off provisions in APRA's prudential standards at the time.

Summary of new law

5.11 The Bill amends the Industry Acts to provide increased certainty in relation to the conversion and write-off of capital instruments, including amendments to provide that:

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- (b) a determination by APRA, notified to the regulated entity in writing, that without a public sector injection of capital, or equivalent support, the regulated entity would become non-viable.

- conversion or write-off can happen despite any impediment there may be in:
- any domestic or foreign law (other than, for conversion, any laws specified in the amendments or regulations made for that purpose, including laws applying to holdings in companies under Chapter 6 of the Corporations Act or under the *Financial Sector (Shareholdings) Act 1998*);
- the constitution of the entity that has issued the instrument or of an entity that is a party to the instrument and (for conversion) the constitution of the entity into whose shares the instrument converts (if different);
- any contract or arrangement to which the issuing entity, or an entity that is a party to the instrument, is a party, and (for conversion) to which the entity into whose shares the instrument converts (if different) is a party; and
- any listing rules or operating rules of a financial market in whose official list the issuing entity, an entity that is a party to the instrument, or (for conversion), an entity into whose shares the instrument converts (if different), is included; and
- any operating rules of a clearing and settlement facility through which the instrument is traded.
- a stay provision applies to contractual close-out rights that may arise as a result of the conversion or write-off of a capital instrument or the making of a determination by APRA that results in a requirement for the conversion or write-off of a capital instrument.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
It is certain that the terms of capital instruments that provide for the instrument to absorb losses by converting or being written off are effective despite potential legal impediments.	In some situations it is unclear that certain capital instruments will absorb losses – either by conversion or write off – due to potential legal impediments.

Detailed explanation of new law

Conversion and write-off of capital instruments

Definitions

5.12 The Bill amends the Industry Acts to incorporate several new definitions for the purpose of the amendments to provide certainty for the conversion and write-off of capital instruments.

5.13 The new term 'clearing and settlement facility' refers to a clearing and settlement facility as defined by section 761A of the Corporations Act. The provisions of this Bill use this definition to ensure that instruments may be converted or written off despite the operating rules of a clearing and settlement facility through which the instrument is traded. *[Schedule 1, item 31, section 11CAA of the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]*

5.14 The new term 'conversion and write-off provisions' refers to the provisions in APRA's prudential standards that require certain capital instruments to be converted into ordinary shares or mutual equity interests, or to be written off, in certain circumstances described in the prudential standards. *[Schedule 1, item 31, section 11CAA of the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]*

5.15 The provisions in the prudential standards that set these requirements are currently referred to as the 'loss absorption requirements' and requirements for 'loss absorption at the point of non-viability'.⁴ The term 'conversion and write-off provisions' is intended to refer to these provisions. However, the amendments leave room for future changes to APRA's prudential standards, including changes that might refer to instruments that are not currently considered capital under the prudential standards.

5.16 The new term 'conversion entity' is relevant in circumstances where an instrument includes terms that provide for the instrument, or rights under the instrument, to convert into ordinary shares or mutual equity interests of a different entity. Where such a conversion takes place, the instrument converts, or rights convert, into ordinary shares or mutual equity interests of the conversion entity. *[Schedule 1, item 31, section 11CAA of*

⁴ See for example Prudential Standard APS 111 Capital Adequacy – Measurement of Capital, Attachments F and J.

the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]

5.17 The new term ‘converts’ describes any process by which instruments, or rights under instruments, may be converted into ordinary shares or mutual equity interests. This term is broadly defined in order to accommodate current and future contractual approaches to how instruments are converted into ordinary shares or mutual equity interests. *[Schedule 1, item 31, section 11CAA of the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]*

5.18 The new term ‘mutual equity interests’ is only incorporated into the Banking Act conversion and write-off provisions, and refers to such interests as defined in APRA’s prudential standards. This term is relevant to circumstances where a capital instrument has been issued by a mutually-owned ADI, or by an entity described in existing subsection 11CAB(1) with respect to a mutually-owned ADI. *[Schedule 1, item 31, section 11CAA of the Banking Act]*

5.19 The new term ‘operating rules’ refers to operating rules as defined by section 761A of the Corporations Act. The provisions of the Bill use this definition to refer to the operating rules of a financial market or a clearing and settlement facility. *[Schedule 1, item 31, section 11CAA of the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]*

5.20 The term ‘related subsidiary’ refers to a subsidiary of a holding company of a regulated entity. Note that ‘holding company’ is now defined in the Industry Acts (see Chapter 10). This term is used to provide for circumstances where a related subsidiary issues capital instruments that count as regulatory capital for a conversion entity. The amendments provide certainty that those instruments will absorb losses despite potential legal impediments. *[Schedule 1, item 31, section 11CAA of the Banking Act; Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act]*

5.21 The amendments provide that conversion of regulatory capital instruments is effective despite any law except certain specified laws. The term ‘specified law’ refers to the following:

- the Financial Sector (Shareholdings) Act 1998;
- the Foreign Acquisitions and Takeovers Act 1975;
- Chapter 6 of the *Corporations Act 2001* (takeovers).
- any law prescribed in the regulations for the purposes of this paragraph. *[Schedule 1, item 31, section 11CAA of the Banking Act;*

Schedule 2, item 17, section 36A of the Insurance Act; Schedule 3, item 64, section 230AAB of the Life Insurance Act

5.22 The Bill also amends the Industry Acts to define the terms ‘financial market’ and ‘listing rules’ according to their definition in section 761A of the Corporations Act. *[Schedule 1, item 7, subsection 5(1) of the Banking Act; Schedule 2, item 4, subsection 3(1) of the Insurance Act; Schedule 3, item 113, Schedule Dictionary of the Life Insurance Act]*

Scope of instruments to which these amendments apply

5.23 The Bill amends the Industry Acts to describe the scope of instruments to which the amendments apply.

5.24 The amendments apply to instruments that include terms for the purposes of the conversion or write-off provisions in the prudential standards. *[Schedule 1, item 31, subsection 11CAB(1) of the Banking Act; Schedule 2, item 17, subsection 36B(1) of the Insurance Act; Schedule 3, item 64, subsection 230AAC(1) of the Life Insurance Act]*

5.25 The amendments apply to instruments issued by any of the following, or to which any of the following is a party:

- a regulated entity;
- a holding company of a regulated entity;
- a subsidiary or a related subsidiary of a regulated entity (see 5.20 for the definition of a related subsidiary); or
- an entity prescribed by the regulations for the purposes of these amendments. *[Schedule 1, item 31, subsection 11CAB(1) of the Banking Act; Schedule 2, item 17, subsection 36B(1) of the Insurance Act; Schedule 3, item 64, subsection 230AAC(1) of the Life Insurance Act]*

5.26 The amendments include a regulation-making power to prescribe other kinds of entities that might issue capital instruments that include terms for conversion or write-off. This is intended to allow flexibility to accommodate potential future capital raising structures.

5.27 Where a regulated entity is a subsidiary of one or more holding companies, the amendments are intended to cover any instrument issued to the market by a holding company of that regulated entity, and any corresponding intra-group instruments or arrangements between the regulated entity, the holding company and any intermediate holding company in order to meet the regulatory capital requirements of the regulated entity. In this case, conversion will occur in accordance with the

terms of those instruments or arrangements despite the potential legal impediments listed at 5.28.

Conversion despite other laws etc.

5.28 The Bill amends the Industry Acts to ensure that instruments that are within the scope of these amendments can be converted according to their terms despite any impediments there may be in:

- any domestic or foreign laws, except for those specified in the amendments and any regulations made for this purpose;
- the constitution of the entity that has issued the instrument, any entity that is a party to the instrument, or any conversion entity for the instrument;
- any contract or arrangement to which the issuing entity, any entity that is a party to the instrument, or any conversion entity for the instrument, is a party;
- any listing rules or operating rules of a financial market in whose official list the issuing entity, any entity that is a party to the instrument, or any conversion entity for the instrument, is included; and
- any operating rules of a clearing and settlement facility through which the instrument is traded. *[Schedule 1, item 31, subsection 11CAB(2) of the Banking Act; Schedule 2, item 17, subsection 36B(2) of the Insurance Act; Schedule 3, item 64, subsection 230AAC(2) of the Life Insurance Act]*

Write off despite other laws etc.

5.29 The Bill amends the Industry Acts to ensure that instruments that are within the scope of these amendments can be written off according to their terms despite any impediments there may be in:

- any domestic or foreign law;
- the constitution of the entity that has issued the instrument, or any entity that is a party to the instrument;
- any contract or arrangement to which the issuing entity, or any entity that is a party to the instrument, is a party; and
- any listing rules or operating rules of a financial market in whose official list the issuing entity, or any entity that is a party to the instrument, is included; and

- any operating rules of a clearing and settlement facility through which the instrument is traded. *[Schedule 1, item 31, subsection 11CAB(3) of the Banking Act; Schedule 2, item 17, subsection 36B(3) of the Insurance Act; Schedule 3, item 64, , subsection 230AAC(3) of the Life Insurance Act]*

5.30 The above provisions allow for an instrument to be converted or written off despite the laws of a foreign country or part of a foreign country. This is intended to include laws that are in force in a country or in part of a country despite that law not having been made or otherwise implemented in the foreign country. An example of this would be the self-executing laws of the European Union.

5.31 It should be noted that operating rules of financial markets and clearing and settlement facilities will generally constitute a contract or arrangement to which the entity is party. They have been expressly referred to in these provisions for the avoidance of doubt, including to capture issues that might arise where an instrument converts in the course of a trading and settlement process conducted through a clearing and settlement facility. The explicit inclusion of operating rules of financial markets and clearing and settlement facilities in these provisions is not intended to narrow the meaning of references to contracts and other arrangements in these provisions or similar override provisions elsewhere in the Industry Acts.

Consequential amendments

Definitions of ‘financial market’ and ‘listing rules’

5.32 As the terms ‘financial market’ and ‘listing rules’ are now defined terms in the Industry Acts (see 5.22), consequential amendments have been made to the following, to remove duplicate references. *[Schedule 1, items 99, 125 and 139, paragraphs 13G(3)(d), 14A(5B)(d), and 14AA(4)(d) of the Banking Act, Schedule 2, items 48, 54 and 107, paragraphs 62Z(4)(d)62ZJ(3)(b)(iv), and 103D(3)(d) of the Insurance Act and Schedule 3, items 43, 49 and 77, paragraphs 168A(4)(d) 176(3)(b)(iv) and 230AD(3)(d) of the Life Insurance Act]*

New notes in the Corporations Act

5.33 The Bill amends certain sections of the Corporations Act to include a new note in each of the sections confirming the effect of the amendments. *[Schedule 7, items 1 to 3, subsections 256B(1), 437F(8), and 468A(8) of the Corporations Act]*

5.34 The note explains that reductions in share capital (in existing subsection 256B of the Corporations Act), or alterations in the status of members of a company made during either the administration of the

company or after the commencement of winding up by the Court (in existing subsections 437F(8) and 468A(8) of the Corporations Act, respectively), are effective despite these sections if they result from an instrument being converted or written off for the purposes of the conversion and write-off provisions.

5.35 The inclusion of these notes in certain sections of the Corporations Act is only for the purpose of explaining the effect of conversion and write-off of non-equity capital instruments and is not intended to limit the application of the amendments more widely.

Application and transitional provisions

5.36 The amendments made by the Bill in relation to the conversion and write-off of capital instruments apply in relation to the conversion or writing-off of any instrument on or after the Bill receives Royal Assent, whether the instrument was issued before, at or after that time. *[Schedule 1, items 253 and 262; Schedule 2, items 139 and 144; Schedule 3, items 118 and 128]*

Chapter 6

Stays

Outline of chapter

6.1 Schedules 1 to 5 to this Bill enhance the stay provisions in the Industry Acts and Transfer Act, and make consequential amendments to the PSN Act.

Context of amendments

6.2 An important aspect of Australia's resolution regime for ADIs and insurers is the operation of the stay provisions located in the various Industry Acts and the Transfer Act. In general, the existing provisions prevent counterparties from:

- denying an obligation;
- accelerating a debt;
- closing-out any transaction; or
- enforcing a security,

under a contract with a regulated entity, where the basis for taking such action is that APRA has exercised a specified regulatory power in relation to that entity (e.g. a general directions power, a direction to recapitalise an ADI or insurer, appointment of statutory or judicial manager or a compulsory transfer of business power). The stay provisions are important in ensuring that pre-emptive actions by counterparties do not impede the ability for APRA to implement an orderly resolution of a regulated entity.

6.3 The existing stay provisions only apply where the entity against which the regulatory action is taken is also the party to the contract. This omission gives rise to the possibility that the exercise of a regulatory power against one entity may trigger the exercise of rights under a contract with another entity in the same group.

6.4 The triggering of termination rights under contracts of other group entities could have material, adverse effect on a financial group and on APRA's ability to implement an orderly resolution of the regulated

entity. This may particularly be the case where the related company in question provides essential services to an ADI, insurer or group, and relies on contractual arrangements with third parties to perform those services. More broadly, the exercise of termination rights in any contract entered into by a member of a financial group could significantly undermine confidence in APRA's efforts to stabilise a distressed regulated entity.

6.5 Extending the relevant stay provisions to address the issues above is consistent with the expanded scope of APRA's powers pursuant to the other amendments in the Bill.

6.6 A further important element of the resolution regime is the interaction of the stay provisions with the PSN Act. The PSN Act overrides a range of laws in order to ensure the validity of certain provisions relating to netting and the payments systems covered by the PSN Act. Consequential amendments are made to the PSN Act to take into account the enhancements to the stay provisions, the moratorium provisions for statutory and judicial management, and the extension of certain powers to group entities. This is intended to ensure that current protections under the PSN Act are retained and the rights of counterparties to close-out netting contracts are clear.

Summary of new law

1.61 Schedules 1 to 5 to this Bill amend the Industry Acts and Transfer Act to enhance the stay provisions, and make consequential amendments to the PSN Act, including amendments to:

- ensure that an exercise of a power in relation to an entity does not give rise to termination rights or other rights (that is, denying an obligation, accelerating a debt, closing-out on a transaction, or enforcing a security) in contracts of entities within the same relevant group of bodies corporate (that is, any group comprising the ADI or insurer and its subsidiaries or an authorised NOHC and its subsidiaries);
- ensure that the current protections afforded to counterparties to certain close-out netting contracts under the PSN Act are retained (with appropriate amendments to take into account stays applying to cross-default rights);
- set out the relationship between the enhanced moratorium provisions for statutory and judicial management and the PSN Act, as appropriate.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>The existing stay provisions in the Industry Acts and the Transfer Act have been enhanced so that an exercise of power made in respect of:</p> <ul style="list-style-type: none"> • a body corporate (which might be an ADI/insurer, or an authorised NOHC of an ADI/insurer, or a subsidiary of an authorised NOHC or ADI/insurer), <p>cannot be grounds for:</p> <ul style="list-style-type: none"> • a counterparty to that body corporate; or • a counterparty to a body corporate that is in the same relevant group of bodies corporate as the entity against which the power was exercised, <p>to deny an obligation, accelerate a debt, close-out on a transaction, or enforce a security.</p>	<p>The existing stay provisions in the Industry Acts and the Transfer Act operate so that an exercise of power made in respect of an entity cannot be used as a basis for a counterparty to a contract with <i>that entity</i> to deny an obligation, accelerate a debt, close-out on a transaction, or enforce a security.</p>
<p>The PSN Act includes express provisions dealing with the application of resolution actions to authorised NOHCs or subsidiaries of an authorised NOHC or ADI/insurer. It also caters for stays on actions under cross-default clauses and incorporates into its terms and definitions the amended and new stay and moratorium provisions provided for in the Bill.</p>	<p>The PSN Act deals with the interaction of certain provisions relating to netting and the payments system with the existing stay provisions in the Industry Acts and the Transfer Acts. However, it does not expressly deal with the application of relevant resolution actions to authorised NOHCs or subsidiaries of the authorised NOHC or ADI/insurers, or cater for stays on actions under cross-default clauses, or for the application of the amended and new stay and moratorium provisions provided for in the Bill.</p>

Detailed explanation of new law

Extend stay provisions to contracts entered into by a related body corporate within the same ‘relevant group of bodies corporate’

Enhance existing stay provisions in the Industry Acts and the Transfer Act

6.7 The Bill amends the existing stay provisions in the Industry Acts and the Transfer Act to ensure that the exercise of a power in relation to an entity does not give rise to termination rights or other rights in the contracts of entities within the same relevant group of bodies corporate as the entity against which the regulatory action was taken. An ADI/insurer and its subsidiaries, or an authorised NOHC and its subsidiaries, will constitute a relevant group of bodies corporate.

6.8 The relevant stay provisions are:

- direction under the Banking Act is not grounds for denial of obligations etc; *[Schedule 1, item 43, subsections 11CD(1) to 11CD(2) of the Banking Act]*
- recapitalisation direction under the Banking Act is not grounds for denial of obligations etc; *[Schedule 1, item 102, sections 13N of the Banking Act]*
- a recapitalisation facilitated by a statutory manager under the Industry Acts is not grounds for denial of obligations etc; *[Schedule 1, item 143, section 14AC of the Banking Act; Schedule 2, item 58, section 62ZOH of the Insurance Act; Schedule 3, item 52, section 179AF of the Life Insurance Act]*
- a statutory manager being in control under the Industry Acts is not grounds for denial of obligations etc; *[Schedule 1, item 191, section 15C of the Banking Act; Schedule 2, item 58, section 62ZOX of the Insurance Act; Schedule 3, item 52, section 179AX of the Life Insurance Act]*
- a compulsory transfer under the Transfer Act is not grounds for denial of obligations etc – note that this will apply not only to compulsory business transfers but also to compulsory share transfers; *[Schedule 4, item 78, sections 36AA of the Transfer Act]*
- a judicial manager being in control under the Insurance Act is not grounds for denial of obligations etc; *[Schedule 2, item 43, section 62V of the Insurance Act]*

- a recapitalisation facilitated by a judicial manager under the Insurance Act is not grounds for denial of obligations etc; *[Schedule 2, item 49, section 62ZB of the Insurance Act]*
- a recapitalisation direction under the Insurance Act is not grounds for denial of obligations etc; *[Schedule 2, item 110, section 103K of the Insurance Act]*
- a direction under the Insurance Act is not grounds for denial of obligations etc; *[Schedule 2, item 120, subsections 105(1) to 105(2) of Insurance Act]*
- a judicial manager being in control under the Life Insurance Act is not grounds for denial of obligations etc; *[Schedule 3, item 36, section 165B of the Life Insurance Act]*
- a recapitalisation facilitated by a judicial manager under the Life Insurance Act is not grounds for denial of obligations etc; *[Schedule 3, item 44, section 168C of the Life Insurance Act]*
- a recapitalisation direction under the Life Insurance Act is not grounds for denial of obligations etc; *[Schedule 3, item 80, sections 230AJ of the Life Insurance Act]* and
- a direction under the Life Insurance Act is not grounds for denial of obligations etc. *[Schedule 3, item 89, sections 230C(1) to 230C(2) of the Life Insurance Act]*

6.9 In summary, the enhanced stay provisions now provide that where a body corporate is a party to a contract (whether the proper law of the contract is Australia law or law of a foreign country), a counterparty to that contract cannot:

- deny an obligation;
- accelerate a debt;
- close-out any transaction; or
- enforce a security,

on the ground that an exercise of power (as specified under the relevant stay provision in that case e.g. directions power, power to recapitalise an ADI or insurer, appointment of a statutory or judicial manager and compulsory business transfer power) occurred against either the contracting body corporate or, if the body corporate is a member of a relevant group of bodies corporate, another member of that group. (A group comprising an ADI/insurer and subsidiaries will be a relevant group

of bodies corporate. A group comprising an authorised NOHC and subsidiaries will also be a relevant group of bodies corporate.)

6.10 Under these provisions, the body corporate against which the relevant regulatory action is taken could be an ADI or insurer, an authorised NOHC of the ADI/insurer, or a subsidiary of the ADI/insurer or authorised NOHC. In order for the stay to apply, either that body corporate, or a related body corporate that is a member of the same relevant group of bodies corporate, must be party to the relevant contract.

6.11 For example, if an ADI is party to a contract with a third party entity, and the contract includes a provision that purports to give the third party a right to terminate the contract with the ADI, if APRA gives a direction to a related body corporate of the ADI (that is in the same relevant group of bodies corporate), the relevant stay provision will operate to prevent action being taken under the contract on the basis of the direction.

6.12 The Bill makes consequential amendments to the existing protections afforded to counterparties affected by an exercise of a directions power. Under the current law, if a counterparty is prevented from fulfilling its obligations under a contract with a body corporate (for example, an ADI), because of the giving of a direction to that body corporate, the counterparty is relieved from all obligations owed to the body corporate under the contract, subject to any Court order (see subsections 11CD(2) of the Banking Act, 105(2) of the Insurance Act, and 230C(2) of the Life Insurance Act). The Bill extends this protection so that the counterparty is relieved of their obligations to the contracting body corporate (subject to any Court order) if they are prevented from fulfilling their obligations under the contract because of a direction regardless of whether the direction is given to the contracting body corporate itself or to a related body corporate of the contracting body corporate. *[Schedule 1, item 43, subsection 11CD(2) of the Banking Act; Schedule 2, item 120, subsection 105(2) of the Insurance Act; Schedule 3, item 89, subsection 230C(2) of the Life Insurance Act]*

New stay provisions – Conversion or write-off etc. not grounds for denial of obligations

6.13 Chapter 5 sets out the new provisions in the Industry Acts that provide certainty that capital instruments can be converted or written down as required by APRA's prudential standards. As a consequence of these new provisions corresponding stay provisions are added to the Industry Acts. *[Schedule 1, items 31, sections 11CAA, to 11CAC of the Banking Act; Schedule 2, item 17, sections 36A to 36C of the Insurance Act; Schedule 3, item 64, sections 230AAB to 230AAD of the Life Insurance Act]*

6.14 In summary, the Bill ensures that counterparties of a contracting entity (the ‘first entity’) cannot:

- deny an obligation;
- accelerate a debt;
- close-out any transaction; or
- enforce a security,

under a contract with the first entity on certain grounds. Specifically, the first entity cannot do so on the ground that a ‘relevant instrument’ is being or has been converted or written-off in accordance with the terms of that instrument or on the ground of the making of a determination (however described) by APRA that results in the relevant instrument being required to be converted or written off in accordance with the terms of the instrument. For the avoidance of doubt, these provisions are not intended to impede close-out of a contract on other grounds (for example, relating to an event that may have led to APRA making such a determination) or to impede the conversion or write off of instruments issued for the purposes of the conversion and write-off provisions themselves.

[Schedule 1, item 31, section 11CAC of the Banking Act; Schedule 2, item 17, section 36C of the Insurance Act; Schedule 3, item 64, section 230AAD of the Life Insurance Act]

6.15 A ‘relevant instrument’ is defined as an instrument:

- that contains terms that are for the purpose of conversion and write-off provisions and is issued by a regulated entity, a holding company of a regulated entity, a subsidiary or related subsidiary of a regulated entity or an entity of a kind prescribed by the regulations); and
- either:
 - the instrument was issued by the first entity (as noted above, the ‘first entity’ for these purposes is the party to the contract to which the stay provision applies); or
 - the first entity is a party to the instrument; or
 - the first entity is a conversion entity in relation to the instrument (that is, the instrument converts into ordinary shares of the first entity); or

- or, if the first entity is a body corporate that is a member of a ‘relevant group of bodies corporate’ (that is, a group comprising a regulated entity and its subsidiaries or an authorised NOHC of a regulated entity and the NOHC’s subsidiaries):
 - the instrument was issued by another member of that group; or
 - another member of that group is a party to the instrument; or
- another member of that group is a conversion entity in relation to the instrument. *[Schedule 1, item 31, subsection 11CAC(4) of the Banking Act; Schedule 2, item 179, subsection 36C(4) of the Insurance Act; Schedule 3, item 64, subsection 230AAD(4) of the Life Insurance Act]*

6.16 In summary, consistent with the other amendments to enhance the existing stay provisions in the Industry Acts and Transfer Act, the new stay provisions in the Industry Acts also extend to where the issuing entity, or a party to the instrument, or the conversion entity is a member of the same relevant group of bodies corporate as the first entity (the entity that is party to the stayed contract). *[Schedule 1, items 31, section 11CAC of the Banking Act; Schedule 2, item 17, section 36C of the Insurance Act; Schedule 3, item 64, section 230AAD of the Life Insurance Act]*

Consequential amendments to the PSN Act to encompass ‘related bodies corporate’

Background

6.17 Amendments are made to the PSN Act to take into account, first, the enhancements to the stay provisions and, secondly, the extension of certain regulatory powers to related bodies of ADIs and insurers. This is because these amendments mean that the stay provisions will apply where regulatory action, including the appointment of a statutory manager, is taken against an entity that is not an ADI or insurer (that is, it may be an authorised NOHC or a subsidiary of an ADI, insurer or authorised NOHC). Secondly, the extension of the stay provisions so that they apply where the contracting party is not the party against which regulatory action was taken (where they are a member of same “relevant group of bodies corporate”) means that amendments are required.

6.18 In broad terms, the PSN Act overrides a range of laws in order to ensure the validity of certain provisions relating to netting and the payments system covered by the PSN Act. For present purposes the protection afforded by existing section 14 (‘Effectiveness of close-out

netting contracts’) to close-out netting contracts, which include over the counter (OTC) derivatives and securities lending contracts, is particularly relevant.

6.19 The PSN Act differentiates between ‘specified provisions’, ‘specified stay provisions’ and ‘direction stay provisions’. Section 14 (‘Effectiveness of close-out netting contracts’), and provisions in the PSN Act relating to other netting and payment systems arrangements, support the effectiveness of close out, netting of obligations, and payments despite any other law, including a ‘specified provision’.

6.20 However, subsection 14(3) of the PSN Act provides an exception by stating that the protections in relation to close-out netting contracts have effect ‘subject to a specified *stay* provision that applies to the contract’. Accordingly, if a stay provision falls within this definition, then the rights to close out and rights in relation to relevant securities in section 14 cannot be exercised if the specified stay provision applies.

6.21 The PSN Act further distinguishes between specified stay provisions that are ‘direction stay provisions’ and those that are not direction stay provisions. If a specified stay provision is a ‘direction stay provision’ then it operates on a permanent and continuing basis; in other words, the action (giving of a direction) that gave rise to the ostensible close-out right cannot itself be relied on as a basis for close-out at any time. If the specified stay provision is *not* a direction stay provision, and the contract in question is a derivative or securities lending contract of a kind covered by section 15A of the PSN Act, the stay will operate temporarily, under Division 2 of Part 4 of the PSN Act (‘Ceasing non-direction stays for derivatives contracts’), although it may be made permanent if the relevant body corporate (e.g. an ADI or insurer) is resolved during the ‘resolution period’ as defined in the PSN Act.

6.22 Having regard to the above, the Bill amends the PSN Act to:

- apply in an appropriate way where resolution actions and directions, to which stay provisions apply, are taken against not only ADIs and insurers, but also authorised NOHCs and subsidiaries of ADIs/insurers and authorised NOHCs. This has implications for Division 2 of Part 4 of the PSN Act (‘Ceasing non-direction stays for derivatives contracts’) where a ‘specified stay provision’ that is not a ‘direction stay provision’ applies in relation to a group entity;
- address the implications of the stay provisions applying on a cross-default basis. This also has implications for Division 2 of Part 4;

- provide for appropriate treatment of the new stay provisions relating to actions under conversion and write-off provisions. As discussed below, these will be defined as both ‘specified stay provisions’ and ‘direction stay provisions’, with the result that they will not be subject to Division 2 of Part 4; and
- ensure that the new moratorium provisions for statutory and judicial management are treated appropriately under the PSN Act. In general terms they will be treated as ‘specified provisions’, with the result that the provisions of the PSN Act in relation to netting arrangements and payment systems will apply despite the moratorium provisions.

Amendments

6.23 A new definition of ‘related body corporate’ is inserted into the PSN Act. For the purposes of the PSN Act, the question of whether a body corporate is related to another body corporate is to be determined in the same way as that question is determined for the purposes of the Corporations Act. The inclusion of this definition is necessary for the purposes of amendments to Part 4 of the PSN Act (‘Close-out netting contracts’) relating to the interaction between stay provisions and the protections given to close-out netting contracts. *[Schedule 5, items 10 and 17, sections 5 and 5AA of the PSN Act]*

6.24 The expansion of the statutory management regime and directions powers to group entities (that is, related bodies corporate of ADIs and insurers - see Chapter 2 and Chapter 3) means that the definition of ‘regulated body’ in the PSN Act had to be expanded beyond ADIs, general insurers, life companies and private health insurers, to include:

- an authorised NOHC of an ADI/insurer; and
- a subsidiary of an authorised NOHC or an ADI/insurer.
- For this purpose it is also necessary to include a definition of ‘subsidiary’ in the PSN Act: *[Schedule 5, items 8 and 17, sections 5 and 5AB of the PSN Act]*

6.25 The existing stay provisions in the Industry Act and the Transfer Act are all listed as ‘specified stay provisions’ under the PSN Act. Since the Bill applies the statutory management regime to the Insurance Act and Life Insurance Act, the following new stay provisions are added to the definition of ‘specified stay provision’ in the PSN Act:

- a recapitalisation facilitated by a statutory manager is not grounds for denial of obligations etc; *[Schedule 2, item 58,*

subsection 62ZOH(2) of the Insurance Act; Schedule 5, item 14, section 5 of the PSN Act]

- a statutory manager being in control is not grounds for denial of obligations etc; *[Schedule 2, item 58, subsection 62ZOX(2) of the Insurance Act; Schedule 5, item 14, section 5 of the PSN Act]*
- a recapitalisation facilitated by a statutory manager is not grounds for denial of obligations etc; *[Schedule 3, item 52, subsection 179AH(2) of the Life Insurance Act; Schedule 5, item 15, section 5 of the PSN Act]* and
- a statutory manager being in control is not grounds for denial of obligations etc. *[Schedule 3, item 52, subsection 179AX(2) of the Life Insurance Act; Schedule 5, item 15, section 5 of the PSN Act]*

6.26 The insertion of the following new conversion and write-off stay provisions into the Industry Acts required relevant changes to the definition of ‘specified stay provision’ and ‘direction stay provision’ in the PSN Act :

- the Banking Act conversion and write-off stay provision (conversion or write-off etc. not grounds for denial of obligations); *[Schedule 1, item 31, subsection 11CAC(2) of the Banking Act; Schedule 5, items 3 and 12, section 5 of the PSN Act]*
- the Insurance Act conversion and write-off stay provision (conversion or write-off etc. not grounds for denial of obligations); *[Schedule 2, item 19, subsection 36C(2) of the Insurance Act; Schedule 5, items 4 and 13, section 5 of the PSN Act]*
- the Life Insurance Act conversion and write-off stay provision (conversion or write-off etc. not grounds for denial of obligations). *[Schedule 3, item 64, section 230AAD(2) of the Life Insurance Act; Schedule 5, items 5 and 15, section 5 of the PSN Act]*

6.27 As explained above this will mean that section 14 of the PSN Act (‘Effectiveness of close-out netting contracts’) applies subject to the stay provisions listed at 6.25 and 6.26. However, those two sets of stay provisions will be treated differently under Division 2 of Part 4 of the PSN Act. The resolution stays regime in Division 2 of Part 4 (‘Ceasing non-direction stays for derivatives contracts’) will apply to the ‘specified stay provisions’ listed at 6.25 as they are not ‘direction stay provisions’ (broadly speaking, they relate to resolution in the context of statutory management, and therefore fall within Division 2 of Part 4, like the corresponding stay provisions in the Banking Act). However, Division 2 of Part 4 will *not* apply to the ‘specified stay provisions’ relating to conversion and write off listed at 6.26 because they will be defined to be

‘direction stay provisions’ (so they will apply permanently in relation to a given trigger for action under a contract).

6.28 The existing sections 15A (‘Ceasing non-direction stays for derivatives contracts’) and 15B (‘When APRA may declare that non-direction stays cease’) in Division 2 of Part 4 of the PSN Act are amended by expanding their application to not only close-out netting contracts to which an ADI or insurer is a party, but to close-out netting contracts to which other group entities are party, and to cater for cross default situations. *[Schedule 5, items 18 to 24, sections 15A and 15B of the PSN Act]*

6.29 The current position is that section 15A of the PSN Act provides for a specified (non-direction) stay provision to apply on a temporary basis to a derivatives or securities lending contract of a kind covered by section 15A of the PSN Act while action is taken to resolve the regulated entity in question. Section 15A and the other provisions in Division 2 of Part 4 are only relevant where the stay provision relates to the appointment of a statutory or judicial manager, or recapitalisation under a statutory or judicial manager, or a compulsory transfer of business (sometimes referred to as ‘resolution stay provisions’). This will continue to be the case.

6.30 The amendments under the Bill will mean that section 15A of the PSN Act applies to keep a stay on foot for at least the resolution period⁵ even where the relevant resolution action (for example, the appointment of a statutory manager) was taken against an authorised NOHC or subsidiary for example, rather than (or as well as) an ADI or insurer. *[Schedule 5, items 18 to 21, section 15A of the PSN Act]*

6.31 Secondly the amendments will ensure that section 15A applies where the contracting party and the trigger body are both members of the same relevant group of bodies corporate (a group comprising an ADI/insurer and its subsidiaries or authorised NOHC and its subsidiaries). As noted above, if the contracting party and the entity against which regulatory action has been taken are related but *not* both members of the same relevant group of bodies corporate, the stay provisions will not apply. *[Schedule 5, items 18 to 21, section 15A of the PSN Act]*

⁵ The ‘resolution period’ where the trigger event for the stay provision is appointment of a statutory or judicial manager, or recapitalisation under a statutory or judicial manager, will continue to be the period from the trigger event to the end of the next business day. If the trigger event relates to a compulsory transfer of business, the resolution period will continue to be the period from the trigger event to just after a certificate of transfer comes into force, unless APRA is satisfied it will not issue a certificate and declares an early end to the resolution period.

6.32 Section 15B of the PSN Act currently gives APRA power to declare, before the end of the resolution period, that the stay is to come to an end, and consequential amendments are made to ensure the section reflects the new application of the stay provisions to related bodies corporate. *[Schedule 5, items 22 to 24, section 15B of the PSN Act]*

6.33 Section 15C of the PSN Act currently sets out what must be done to resolve an ADI or insurer in order for APRA to make the stay provision permanent. The broad policy objectives of this section are unchanged by the Bill but amendments have been made, including by the addition of new provisions, to cater for group resolution, the operation of cross default clauses and the interaction of such clauses with the amended stay provisions. *[Schedule 5, items 25 to 29, sections 15C, 15D and 15E of the PSN Act]*

6.34 In relation to the existing section 15C of the PSN Act (‘When APRA may declare that non-direction stays continue’), the expansion of the statutory management regime to group entities (see Chapters 1 and 2) means the entity to which a trigger event occurs (the ‘trigger body’) may not always be the party to the close-out netting contract (the ‘trigger contract’). For example, APRA could appoint a statutory manager (trigger event) to an ADI (trigger body) where the party to the relevant close-out netting contract is a subsidiary of the ADI.

6.35 To address this issue, section 15C of the PSN Act will continue to cover the simple case where the entity subject to the regulatory action giving rise to the stayed trigger event is party to the contract in question. There will be two new provisions dealing with where the entity subject to the regulatory action is not the same as the contracting entity. *[Schedule 5, items 25 to 29, sections 15C, 15D and 15E of the PSN Act]*

6.36 Accordingly, section 15C of the PSN Act is amended to make it clear that it specifically covers where the regulated body is also the contracting body, which is the simplest scenario and similar to the way section 15C currently works. A number of amendments are required to section 15C to reflect the fact that the regulated body will not necessarily be an ADI or insurer, such as where the trigger is appointment of a statutory manager to a group entity under the new powers discussed in Chapter 2. This is relevant because the test for whether the stay can be made permanent, which broadly requires APRA to make a determination as to whether the body has been resolved, will differ depending on whether it is an ADI or insurer, on the one hand, or a related body corporate that does not have depositors or policyholders. If the regulated body is an ADI or insurer, and it is resolved without a transfer of business, then the resolution test will require APRA to consider (among other things) whether the body has the each material authorisation for its regulated business. If the body is not an ADI or insurer, this requirement

will not apply. Further amendments clarify that it will only be necessary to consider whether minimum capital requirements are met if they actually apply to the party. The amendments also address where the resolution action giving rise to the contractual trigger and stay may be the appointment of a statutory manager to an insurer. *[Schedule 5, items 25 to 28, section 15C of the PSN Act]*

6.37 To address the position where the trigger body and the contracting body are not the same (that is, where they are related bodies corporate), a new provision ('When APRA may declare that non-direction stays continue – related body corporate of regulated body is party to trigger contract') is inserted. Before APRA can make a determination that the stay be made permanent, it will be necessary to apply certain tests set out in subsection 15D(5) to:

- the trigger body (the entity in relation to which the triggering regulatory action has been taken), where resolution occurs without a transfer of business; or
- the receiving body, where resolution occurs through a total transfer of business; or
- either or both of those bodies, where resolution involves a partial transfer of business.

6.38 In each case, APRA will be required to assess whether the matters in subsection 15D(5), which broadly set out a 'resolution test' in similar terms to the one in subsection 15C(3), are satisfied in relation to the trigger body or any receiving body to which relevant business has been transferred. *[Schedule 5, item 29, section 15D of the PSN Act]*

6.39 Other amendments deal with the position where there has been a transfer of business from the trigger entity to a receiving body. If there has been a partial transfer, APRA will have a discretion to apply the 'resolution test' to either or both of the trigger body or the receiving body. In addition, , whether the transfer is total or partial, APRA will only be able to make the stay permanent if APRA is satisfied there will be no detrimental effect on any counterparty to a close out netting contract to which the declaration would apply. *[Schedule 5, item 29, sections 15D and 15E of the PSN Act]*

6.40 Further detail on these amendments, is set out below.

Amended section 15C of the PSN Act: extending the section to authorised NOHCs and subsidiaries, when the trigger body and the contracting body are the same

6.41 To protect the legitimate interests of counterparties to relevant close-out netting contracts, the amendments provide that a specified stay provision may only be declared to continue if the circumstances set out below exist. It should be noted that in these amendments the amended term ‘regulated body’ has the broad meaning discussed at 6.24, namely it includes not only ADIs, insurers and PHIs (as is currently the case), but also authorised NOHCs of ADIs and insurers, and subsidiaries of an ADI/insurer or authorised NOHC. The specified circumstances are:

- a trigger event to which a specified stay provision (other than a direction stay provision) applies is an event that involves a regulated body and the trigger event happens in relation to a close-out netting contract (the ‘trigger contract’) to which that same regulated body is a party;
- APRA is satisfied that all matters set out at 6.44 will be satisfied in relation to the party in respect of which the declaration may be made (which will be either or both of the regulated body or a receiving body if there has been a transfer of business) at the following time:
 - if a certificate of transfer will come into force under the Transfer Act, just after that coming into force; or
 - in all other cases, at the time the declaration will be made;
- the party in respect of which the declaration may be made is not in external administration (as defined in the PSN Act) (other than statutory management or judicial management); and
- APRA has not already made a declaration under section 15B that the specified stay provision ceases to apply in relation to the trigger event. This is to provide certainty, so that APRA cannot make a declaration extending the application of the relevant stay if it has previously made a declaration that the stay ceases to apply. *[Schedule 5, items 25 to 28, heading and subsections 15C(1), 15C(3) and 15C(5) of the PSN Act]*

6.42 If these conditions are satisfied, APRA may declare that the specified stay provision is to continue to apply to:

- if a certificate of transfer for a total transfer will come into force under the Transfer Act, all close out netting contracts to which the regulated body is a party (and to which the receiving body, within the meaning of the Transfer Act, will become a party immediately after the transfer), and all securities given over financial property in respect of obligations under those close-out netting contracts;
- if a certificate of transfer for a partial transfer will come into force under the Transfer Act, either or both of the following:
 - all close out netting contracts to which the regulated body is a party (and to which the regulated body will remain a party immediately after the transfer), and all securities given over financial property in respect of obligations under those close-out netting contracts;
 - all close out netting contracts to which the regulated body is a party (and to which the receiving body, within the meaning of the Transfer Act, will become a party immediately after the transfer), and all securities given over financial property in respect of obligations under those close-out netting contracts; or
- in all other cases, all close out netting contracts to which the regulated body is a party and all securities given over financial property in respect of obligations under those close-out netting contracts. *[Schedule 5, item 26, subsection 15C(2) of the PSN Act]*

6.43 In order for a specified stay provision to continue to apply, APRA must be satisfied that the matters set out at 6.44 will be satisfied in relation to the party (the regulated body and/or receiving body) in respect of which the declaration may be made at the time the declaration will be made or just after the coming into force of a certificate of transfer, if applicable.

6.44 The conditions of which APRA must be satisfied are as follows

- that the party is able to meet all its liabilities under:
 - close out netting contracts to which it is a party as and when they become due and payable (including all payment and delivery obligations); and
 - all securities given over financial property in respect of obligations under those close-out netting contracts;

-
- that the party is solvent (within the meaning of the Corporations Act) (this is a current requirement); and
 - if the party is an ADI, general insurer or life company, that they have the material authorisation (however described) necessary for their regulated business. The term ‘regulated business’ in section 5 of the PSN Act is repealed and replaced with:
 - in relation to an ADI—means the ADI’s banking business (within the meaning of the Banking Act); and
 - in relation to a general insurer—means the general insurer’s insurance business (within the meaning of the Insurance Act); and
 - in relation to a life company—means the life company’s life insurance business (within the meaning of the Life Insurance Act).
 - (If the party is not an ADI, general insurer or life company, then the material authorisation requirement will not need to be satisfied.) *[Schedule 5, item 27, paragraph 15C(3)(c) of the PSN Act]*
 - if minimum capital requirements under the Banking Act, the Insurance Act or the Life Insurance Act apply to the party, that either of the following is satisfied:
 - the party’s level of capital complies with the minimum capital requirements that apply to it under the Banking Act, the Insurance Act or the Life Insurance Act (as the case requires) and the applicable prudential standards made under the relevant Act; or *[Schedule 5, item 27, paragraph 15C(3)(d) of the PSN Act]*
 - arrangements are in place to ensure that the party performs all its obligations under (i) close out netting contracts to which it is a party and (ii) all securities given over financial property in respect of obligations under those close-out netting contracts as and when they are due to be performed. Those arrangements must remain in place until at least the earliest day on which:
 - the party’s level of capital complies with the applicable minimum capital requirements;
-

- if a Banking Act statutory manager is in control of the party's business—APRA makes an ultimate termination of control under existing subsection 13C(3) of the Banking Act;
- if an Insurance Act statutory manager is in control of the party's business—APRA makes an ultimate termination of control under subsection 62ZOC(3) of the Insurance Act;
- if a Life Insurance Act statutory manager is in control of the party's business—APRA makes an ultimate termination of control under subsection 179AC(3) of the Life Insurance Act;
- if the party is under judicial management under the Insurance Act—an order under existing section 62ZF of that Act cancelling the judicial management comes into force; or
- if the party is under judicial management under the Life Insurance Act—an order under existing section 172 of that Act cancelling the judicial management comes into force.
[Schedule 5, item 28, paragraph 15C(5)(b) of the PSN Act]

6.45 The existing subsections 15C(6), 15C(7) and 15C(8) remain unchanged, so that:

- a declaration made under section 15C cannot be varied or revoked;
- a declaration made under section 15C is not a legislative instrument; and
- regulations may do any of the following:
 - prescribe requirements relating to how declarations made by APRA are to be made (including requirements relating to the content or form of declarations);
 - prescribe requirements relating to the notification or publication of declarations;
 - include provisions that apply to determining, either generally or for a particular purpose, the time when declarations are taken to be made.

New section 15D of the PSN Act: Applies where the trigger body and the contracting body are different

6.46 The new section 15D applies when the trigger body and the contracting body are different. This will be relevant where: (a) regulatory

action is taken against one entity in a ‘relevant group of bodies corporate’, where (b) this ostensibly triggers close-out or other relevant rights under a contract between a counterparty and another member of that relevant group of bodies corporate, and (c) those rights are stayed by a ‘specified stay provision’ that is not a ‘direction stay provision’. As with section 15C, for a ‘specified stay provision’ that is not a ‘direction stay provision’ to apply, the regulatory action in question would be appointment of a statutory or judicial manager, recapitalisation under a statutory or judicial manager or a compulsory transfer of business or shares. Section 15D provides that a specified stay provision may only be declared to continue if the following specified circumstances exist:

- a trigger event to which a specified stay provision (other than a direction stay provision) applies is an event that involves a regulated body (the ‘trigger body’) and the trigger event happens in relation to one or more close-out netting contracts (each of which is a ‘trigger contract’) to which a related body corporate of the trigger body (the ‘contracting body’) is a party. The specified stay provisions will apply if the trigger body and contracting body are within the same relevant group of bodies corporate;
- APRA is satisfied that all the matters set out in subsection 15D(5) will be satisfied in relation to each entity covered by subsection 15D(2) (that entity will be the trigger body or a receiving body or both, as explained below) in respect of which the declaration may be made at the following time:
 - if a certificate of transfer will come into force under the Transfer Act, just after that coming into force; or
 - in all other cases, at the time the declaration will be made;
- each entity covered under subsection 15D(2) is not in external administration (as defined in the PSN Act) (other than statutory or judicial management); and
- APRA has not already made a declaration under section 15B that the specified stay provision ceases to apply in relation to the trigger event. This is to provide certainty, so that APRA cannot make a declaration extending the application of the relevant stay if it has previously made a declaration that the stay ceases to apply. *[Schedule 5, item 29, subsection 15D(1) of the PSN Act]*

- 6.47 An entity is covered under subsection 15D(2):
- if section 15E does not apply (in other words, there has been no relevant transfer of business) —the trigger body; or
 - if section 15E applies because a transfer of business has occurred under the Transfer Act from the trigger body to a receiving body:
 - in the case of a total transfer of business—the receiving body; or
 - in the case of a partial transfer of business—an entity specified in a determination under subsection 15E(3), which will either be the trigger body or the receiving body or both. *[Schedule 5, item 29, subsection 15D(2) of the PSN Act]*

6.48 If these conditions are satisfied, APRA may declare that the specified stay provision is to continue to apply to each trigger contract specified in the declaration, and to all securities given over financial property in respect of obligations under each trigger contract specified in the declaration. APRA may specify either or both of the following in such a declaration:

- one or more trigger contracts;
- one or more classes of trigger contracts. *[Schedule 5, item 29, subsections 15D(3) and 15D(4) of the PSN Act]*

6.49 The Bill inserts a note under subsection 15D(4) to refer to subsection 15E(2) for a restriction on when APRA may make a declaration under subsection 15D(2) in the case of a transfer of business from the trigger body to a receiving body. (That restriction is discussed at 6.55). *[Schedule 5, item 29, section 15D of the PSN Act]*

6.50 One of the specified circumstances which must be satisfied in order for a specified stay provision to continue to apply is that APRA must be satisfied that all the matters set out in subsection 15D(5) will be satisfied in relation to the entity covered under subsection 15D(2) in respect of which the declaration may be made. These matters must be satisfied at the time the declaration will be made (or just after the coming into force of a certificate of transfer, if applicable). *[Schedule 5, item 31, paragraph 15D(1)(b) of the PSN Act]*

- 6.51 The conditions of which APRA must be satisfied are as follows:
- that the entity covered under subsection 15D(2) is able to meet all its liabilities under:

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- close out netting contracts to which it is a party as and when they become due and payable; and
 - securities given over financial property in respect of obligations of the entity under those contracts (as they become due and payable); and
 - that the entity covered under subsection 15D(2) is solvent (within the meaning of the Corporations Act); and
 - if the entity covered under subsection 15D(2) is an ADI, general insurer or life company, that it has the material authorisation (however described) necessary for its regulated business. The term ‘regulated business’ in section 5 of the PSN Act is repealed and replaced so that:
 - in relation to an ADI—it means the ADI’s banking business (within the meaning of the Banking Act); and
 - in relation to a general insurer—it means the general insurer’s insurance business (within the meaning of the Insurance Act); and
 - in relation to a life company—it means the life company’s life insurance business (within the meaning of the Life Insurance Act).
 - If the entity covered under subsection 15D(2) is not an ADI, general insurer or life company, then this condition does not apply *[Schedule 5, item 29, paragraph 15D(5)(c) of the PSN Act]*
 - if minimum capital requirements under the Banking Act, the Insurance Act or the Life Insurance Act apply to the entity covered by subsection 15D(2), that either of the following is satisfied:
 - the entity’s level of capital complies with those minimum capital requirements; or
 - arrangements are in place to ensure that the entity performs all its obligations under: (i) close out netting contracts to which it is a party as and when they are due to be performed; and (ii) securities given over financial property in respect of obligations given to the entity under those contracts as and when they are due to be performed. Those arrangements must remain in place until at least the earliest day on which:

- the entity's level of capital complies with the applicable minimum capital requirements;
- if a Banking Act statutory manager is in control of the entity's business—APRA makes an ultimate termination of control under existing subsection 13C(3) of the Banking Act;
- if an Insurance Act statutory manager is in control of the entity's business—APRA makes an ultimate termination of control under subsection 62ZOC(3) of the Insurance Act;
- if a Life Insurance Act statutory manager is in control of the entity's business—APRA makes an ultimate termination of control under subsection 179AC(3) of the Life Insurance Act;
- if the party is under judicial management under the Insurance Act—an order under existing section 62ZF of that Act cancelling the judicial management comes into force; or
- if the party is under judicial management under the Life Insurance Act—an order under existing section 172 of that Act cancelling the judicial management comes into force.
[Schedule 5, item 29, paragraph 15D(5)(d) and subsections 15D(6) and 15D(7) of the PSN Act]

6.52 Subsections 15D(8), (9) and (10) mirror the equivalent existing 15C provisions, so that:

- a declaration made under section 15D cannot be varied or revoked;
- a declaration made under section 15D is not a legislative instrument (this provision is included to assist readers, as the instrument is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*); and
- the regulations may do any of the following:
 - prescribe requirements relating to how declarations made by APRA are to be made (including requirements relating to the content or form of declarations);
 - prescribe requirements relating to the notification or publication of declarations;
 - include provisions that apply to determining, either generally or for a particular purpose, the time when

declarations are taken to be made. *[Schedule 5, item 29, subsections 15D(8), 15D(9) and 15D(10) of the PSN Act]*

New section 15E of the PSN Act: ‘Declaration under subsection 15D(3) – total or partial transfer of business’

6.53 New section 15D refers to new section 15E for determining which entity is covered by subsection 15D(2) when there has been a partial transfer of business. This, and other functions of section 15E, are discussed below. *[Schedule 5, item 29, sections 15D and 15E of the PSN Act]*

6.54 Section 15E applies if:

- paragraph 15D(1)(a) is satisfied in relation to a trigger event (that is a trigger event has happened to a trigger body and this has triggered rights in relation to a close-out netting contract with a related body corporate of that trigger body in the same relevant group of bodies corporate, and a relevant stay provision applies); and
- a certificate of transfer will come into force under the Transfer Act for:
 - a total transfer of business from the trigger body to a receiving body; or
 - a partial transfer of business from the trigger body to a receiving body. *[Schedule 5, item 29 subsection 15E(1) of the PSN Act]*

6.55 Section 15E sets out a general condition on APRA’s ability to declare that a specified stay provision is to continue to apply to a trigger contract where there is a transfer of business, whether that transfer is total or partial. In general terms, it provides that APRA must be satisfied that the declaration will not have a detrimental effect on any counterparty to a close-out netting contract to which the declaration would apply.

[Schedule 5, item 29, subsection 15E(2) of the PSN Act]

6.56 As noted above, subsection 15D(2) specifies the body to which the subsection 15D(5) tests must be applied, depending on how the trigger body has been resolved. If there is no transfer, the tests are applied to the trigger entity. If there is a total transfer from the trigger body, the tests are applied to the receiving body. If there has been a partial transfer of business from a trigger body to a receiving body, paragraph 15D(2)(b)(ii) provides that the subsection 15D(5) tests are to be applied to an entity specified in a determination under subsection 15E(3). Subsection 15E(3) provides that APRA may make a written determination specifying either

or both of the following to be the entity covered by subsection 15D(2), namely the entity to be tested under subsection 15D(5):

- the trigger body;
- the receiving body. *[Schedule 5, item 29, subsection 15E(3) of the PSN Act]*

6.57 The written determination cannot be varied or revoked. *[Schedule 5, item 29, subsection 15E(4) of the PSN Act]*

6.58 A determination under section 15E is not a legislative instrument. The provision is included to assist readers and is merely declaratory of the law, as the instrument is not a legislative instrument within the meaning of section 5 of the Legislative Instruments Act 2003. *[Schedule 5, item 29, subsection 15E(5) of the PSN Act]*

6.59 The Bill allows for regulations to be made. The regulations may do any of the following:

- prescribe requirements relating to how determinations under subsection 15E(3) (that is, written determination specifying which entity or entities are covered by subsection 15D(2) in the case of a partial transfer of business) are to be made by APRA (including requirements relating to the content or form of declarations);
- prescribe requirements relating to the notification or publication of determinations under subsection 15E(3);
- include provisions that apply to determining, either generally or for a particular purpose, the time when determinations under subsection 15E(3) are taken to be made. *[Schedule 5, item 29, subsection 15E(6) of the PSN Act]*

Incorporating the widened moratorium provisions for statutory and judicial management into the PSN Act

6.60 Consequential amendments are made to the PSN Act to ensure that the enhanced moratorium provisions related to statutory and judicial management (see Chapter 2 for further detail) do not disturb the protections afforded to counterparties to relevant close-out netting contracts under the PSN Act.

6.61 In this regard, it is intended that the provisions of the PSN Act relating to RTGS settlement systems, multilateral netting arrangements,

close out netting contracts and market netting arrangements operate despite the new moratorium provisions.

6.62 It should also be noted that the litigation moratorium provisions (section 15B of the Banking Act and its counterparts in the statutory and judicial management provisions in the Insurance and Life Insurance Acts) will operate according to their tenor and will not be subject to any express reference in the amendments to the PSN Act.

6.63 Therefore the Bill inserts a new definition of ‘specified moratorium provision’ to the PSN Act. It lists the following in its definition:

- section 15BA of the Banking Act;
- section 15BB of the Banking Act;
- section 15BC of the Banking Act;
- section 62PA of the Insurance Act;
- section 62PB of the Insurance Act;
- section 62PC of the Insurance Act;
- section 62ZOS of the Insurance Act;
- section 62ZOT of the Insurance Act;
- section 62ZOU of the Insurance Act;
- section 161A of the Life Insurance Act;
- section 161B of the Life Insurance Act;
- section 161C of the Life Insurance Act;
- section 179AS of the Life Insurance Act;
- section 179AT of the Life Insurance Act; and
- section 179AU of the Life Insurance Act. [*Schedule 5, item 10, section 5 of the PSN Act*]

6.64 These moratorium provisions are, as noted above, broadly intended to prevent action being taken in relation to securities given by, and other property of, a body that is under statutory or judicial management.

6.65 The new concept of ‘specified moratorium provision’ is then added in to the definition of ‘specified provisions’ in the PSN Act. This affects the meaning of the existing subsections 6(2), 6A(2), 10(3) and 14(3) of the PSN Act (located in Parts 2 (RTGS Payment systems), Part 3 (approved netting arrangements) and Part 5 (market netting contracts) of the PSN Act) because they refer to ‘specified provisions’. The effect of this is that the existing PSN Act provisions have effect despite these new ‘specified provisions’. *[Schedule 5, item 11, section 5 of the PSN Act (paragraph 5(fc) of the definition of specified provisions’]*

6.66 As noted above, the amended section 15B of the Banking Act (Moratorium-effect of Banking Act statutory management on court and tribunal proceedings), and its equivalents in the Insurance Act (sections 62P and 62ZOR) and Life Insurance Act (sections 161 and 179AR), are not included in the ‘specified provisions’ list in the PSN Act. This preserves the status quo under which the existing section 15B (and its equivalents in the Insurance Acts) are not defined as ‘specified provisions’. This is because the PSN Act is generally designed to ensure the effectiveness of processes, including self-help processes such as close-out, and is not intended to preclude court proceedings that might arise in relation to such processes. *[Schedule 1, item 190, section 15B of the Banking Act; Schedule 2, items 33 and 58, sections 62ZOR and 62P of the Insurance Act; Schedule 3, items 28 and 52, sections 179AR and 161 of the Life Insurance Act]*

6.67 Section 15BD of the Banking Act (‘Moratorium-effect of Banking Act statutory management on supply of essential services’) and 15BE of the Banking Act (‘Moratorium – effect of Banking Act statutory management on annual general meeting’), and their equivalent provisions in the Insurance Act (sections 62ZOV, 62ZOW, 62PD, 62PE) and the Life Insurance Act (sections 179AV, 179AW 161D, 161E), do not relate to financial contracts, or other arrangements supported by the PSN Act. Accordingly, it is not necessary to make consequential amendments in the PSN Act to clarify the relationship between those sections and the PSN Act. *[Schedule 1, item 190, sections 15BD and 15BE of the Banking Act; Schedule 2, items 33 and 58, sections 62PD, 62PE, 62ZOV and 62ZOW of the Insurance Act; Schedule 3, items 28 and 52, sections 161D, 161E, 179AV and 179AW of the Life Insurance Act]*

6.68 Subsection 14(3) of the PSN Act provides, and will continue to provide, that the protection afforded to close-out netting contracts in section 14 of the PSN Act operates despite any ‘specified provision’ (which, as noted above, will include the new ‘specified moratorium provisions’). Therefore the protections in paragraphs 14(1)(ca) and (2)(fa) of the PSN Act in relation to certain securities will apply despite the moratorium provisions relating to enforcement of securities. However, it should be noted that the protections given in paragraphs 14(1)(ca) and (2)(fa) only apply to securities in relation to ‘eligible obligations’ (that is, securities relating to derivatives and securities lending

arrangements). The moratorium provisions relating to enforcement of security will still have scope for operation in relation to close-out netting contracts that do *not* relate to those kinds of obligations, or which otherwise fall outside the scope of paragraphs 14(1)(ca) and 14(2)(fa).

Consequential amendments

6.69 The definition of ‘related’ in the Transfer Act (subsection 4(1)) is repealed and replaced with a new definition of ‘related body corporate’. The new definition (section 4) defines related body corporate to mean, in relation to a body corporate, a body corporate that is related to the first-mentioned body, as determined in accordance with section 4A. *[Schedule 4, items 11, 12 and 15, subsection 4(1) and section 4A of the Transfer Act]*

6.70 As a result of introducing the concept of ‘relevant group of bodies corporate’ into section 36AA of the Transfer Act, a new definition of ‘relevant group of bodies corporate’ was added to the Transfer Act. The new definition defines it as a regulated body and its subsidiaries, or an authorised NOHC (within the meaning of any of the Industry Acts) and its subsidiaries. *[Schedule 4, items 12 and 15, subsection 4(1) and section 4B of the Transfer Act]*

Application and transitional provisions

6.71 The amendments in the Bill relating to stay provisions in the Banking Act (items 43, 102, 143 and 191 of Schedule 1), Insurance Act (43, 49, 110 and 120 of Schedule 2) and Life Insurance Act (items 38, 44, 80 and 89 of Schedule 3) apply in relation to directions and actions taken on or after the Bill receives Royal Assent. *[Schedule 1, items 253 and 263; Schedule 2, items 139 and 145; Schedule 3, items 118 and 127].*

6.72 The amendments to cease non-direction stays for derivatives contracts (items 18 – 29 of Schedule 5) apply in relation to events that occur on or after the Bill receives Royal Assent. *[Schedule 5, item 31]*

Chapter 7

Foreign branches

Outline of chapter

7.1 Schedules 1 to 4 to this Bill amend the Industry Acts and the Transfer Act to expand APRA's crisis management powers with respect to the Australian branches of foreign regulated entities.

Context of amendments

7.2 Foreign ADIs in Australia provide a range of important services, such as corporate lending, trade finance, wholesale lending (including to and from other ADIs), the provision of risk hedging to ADIs and corporate clients (for example, through interest rate and currency swaps and options), and securities trading.⁶

7.3 Foreign insurers also provide important services in the Australian financial services system, including providing a significant amount of reinsurance capacity to the Australian general insurance market.

7.4 Some of APRA's existing crisis resolution powers apply to Australian branches of foreign regulated entities. For example, APRA already has the power to apply to the Court for a judicial manager to be appointed to a foreign insurer. However, some important crisis resolution powers either do not apply to foreign branches or their application is currently unclear. In particular:

- APRA cannot appoint a statutory manager to assume control of the Australian business (or any other business) of a foreign regulated entity;
- it is unclear whether APRA may invoke the voluntary or compulsory transfer of business powers available in the Transfer Act in respect of a foreign regulated entity; and

⁶ Note that foreign ADIs are not permitted to accept retail deposits in Australia, which generally prevents them from accepting initial deposits smaller than \$250,000 from individuals.

- there is some ambiguity as to whether APRA can apply for the winding up of a foreign ADI's Australian business.

7.5 Given the risks that a distressed foreign regulated entity could pose to depositors or policyholders, or to financial system stability in Australia, this Bill enhances APRA's crisis management powers with respect to foreign ADIs and foreign insurers operating in Australia. These enhancements address the gaps in APRA's powers described above at 7.4.

7.6 These enhancements broadly reflect the international standard on resolution powers over branches as set out in the Key Attributes. The Key Attributes note that authorities should have resolution powers over local branches of foreign firms and the capacity to use the powers either to support a resolution carried out by a foreign home authority or, in exceptional cases, to take measures on its own initiative.

7.7 The powers would operate within the context of the challenges that may arise in the resolution of an entity with significant cross-border operations. In these cases, cooperation between the authorities in different jurisdictions will be important in ensuring that relevant powers can be applied in an effective and coordinated manner. Without this, it is possible that powers applied in one jurisdiction will not be recognised in other jurisdictions, leading to uncertainty for relevant stakeholders and a greater risk of disorderly outcomes. APRA will continue to develop its coordination of resolution plans with relevant authorities in other jurisdictions as part of resolution planning where relevant (see 10.5).

7.8 Where appropriate, APRA will be able to give due consideration to using the powers to facilitate the resolution of the relevant entity by its home resolution authority. In other circumstances, APRA may consider using the powers in instances where foreign authorities are unable or unwilling to intervene, or intervene in a manner that is inconsistent with the interests of Australian depositors or policyholders, or with financial system stability in Australia.

Summary of new law

7.9 Schedules 1 to 4 to this Bill amend the Industry Acts and the Transfer Act to:

- provide APRA with powers to appoint a statutory manager to the Australian branch of a foreign regulated entity;
- clarify APRA's powers to apply to wind up the Australian branch of a foreign regulated entity;

- harmonise the power to direct a foreign regulated entity not to transfer assets out of Australia across the Industry Acts;
- clarify APRA's powers to implement a voluntary or compulsory transfer of business of the Australian branch of a foreign regulated entity; and
- provide APRA with an explicit power to revoke the authorisation of a foreign regulated entity in Australia if the entity's authorisation is revoked by a foreign country.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Definition of Australian business assets and liabilities of a foreign regulated entity</i>	
The Australian business assets and liabilities of a foreign regulated entity are defined in the Industry Acts to mean the assets and liabilities of the foreign regulated entity in Australia and other assets and liabilities of the entity related to its operations in Australia that are of a class or kind prescribed in regulations.	Although the Industry Acts refer to 'business carried on in Australia' or 'business carried on outside Australia' in relation to a foreign regulated entity, these concepts are not clearly defined.
<i>Appointing a statutory manager to the Australian business assets and liabilities of a foreign regulated entity</i>	
A statutory manager can be appointed to the Australian business assets and liabilities of a foreign regulated entity where certain pre-conditions are met.	No equivalent.
<i>Clarify APRA's ability to apply to the Court for the winding up of a foreign regulated entity</i>	
APRA may apply for the winding up of a foreign regulated entity on certain grounds.	It is unclear whether APRA may apply for the winding up of a foreign ADI.

<i>New law</i>	<i>Current law</i>
<i>Enable APRA to revoke the authorisation of a foreign regulated entity if the entity's authorisation is revoked in a foreign country</i>	
APRA may revoke the authorisation of a foreign regulated entity in Australia if that entity's authorisation is revoked in a foreign country, including part of a foreign country.	No equivalent.
<i>Harmonise the power to direct a foreign regulated entity to not transfer assets out of Australia across the Industry Acts</i>	
The Insurance and Life Insurance Acts include equivalent provisions to those under the Banking Act that explicitly provide APRA with the power to direct that a foreign regulated entity transfer, or not transfer, assets or liabilities either to or out of Australia.	The Banking Act explicitly provides for APRA to direct a foreign ADI to transfer, or not transfer, assets or liabilities either to or out of Australia.
<i>Implementing a voluntary or compulsory transfer of the Australian business assets and liabilities of a foreign regulated entity</i>	
APRA may implement a voluntary or compulsory transfer of the Australian business assets and liabilities of a foreign regulated entity where certain pre-conditions are met.	It is unclear whether the Transfer Act allows APRA to implement a voluntary or compulsory transfer of business of a foreign regulated entity.

Detailed explanation of new law

General provisions

Definition of Australian business assets and liabilities

7.10 The Bill amends the Industry Acts and the Transfer Act to include a new definition, 'Australian business assets and liabilities', which is defined as:

- the assets and liabilities of the foreign regulated entity in Australia;
- any other assets and liabilities of the foreign regulated entity related to its operations in Australia that are of a kind specified in regulations. *[Schedule 1, items 4 and 59, subsections 5(1) and 11E(3) of the Banking Act; Schedule 2, items 1 and 66,*

subsections 3(1) and 62ZVA(3) of the Insurance Act; Schedule 3, items 6 and 110, subsection 16ZE(6) and Schedule Dictionary of the Life Insurance Act; Schedule 4, item 3, subsection 4(1) of the Transfer Act]

7.11 This definition determines the scope of assets and liabilities of a foreign regulated entity that may be placed under statutory or judicial management, or the subject of voluntary or compulsory transfer under Part 4 of the Transfer Act.

7.12 For the purposes of defining Australian business assets and liabilities, the terms ‘asset’ and ‘liability’ are also defined in each of the Industry Acts by reference to the way these terms are currently defined in section 4 of the Transfer Act. *[Schedule 1, item 59, subsection 11E(3) of the Banking Act; Schedule 2, item 66, subsection 62ZVA(4) of the Insurance Act; Schedule 3, item 6, subsection 16ZE(6) of the Life Insurance Act]*

7.13 The new regulation-making power in these provisions is intended to provide the flexibility to specify additional kinds of assets and liabilities of foreign regulated entities that should be considered part of its Australian business assets and liabilities for the purposes of the relevant provisions in the Industry Acts and the Transfer Act. For example, consideration might be given to using the regulations to prescribe assets and liabilities that are critical to the operation of a foreign regulated entity's activities in Australia, such as offshore servicing facilities or information technology infrastructure controlled by the Australian branch.

7.14 Note that, in the Industry Acts, these terms are defined in this way *only* for the purposes of the definition of ‘Australian business assets and liabilities’. References to ‘asset’ or ‘liability’, or the location of an asset or liability, in other parts of the Industry Acts, whether in respect of domestically incorporated and/or foreign entities (for example, section 11F of the Banking Act, or sections 62ZZC and 116A of the Insurance Act) retain their original meaning.

Application of legislative provisions to foreign regulated entities

7.15 The Bill amends the Industry Acts to extend certain powers to foreign regulated entities.

7.16 The Bill amends the Industry Acts to apply provisions relating to statutory management, judicial management, and certain provisions on external administration, to foreign regulated entities. These provisions include:

- Sections 12, 13BA, 13C and Subdivision B of Division 2 of the Banking Act (relating to statutory management of ADIs and target bodies corporate);

- subsections 13A(1) and 13A(2) of the Banking Act, to the extent that those subsections relate to statutory management;
- sections 62B, 62C, 62D and 62E of the Banking Act (relating to external administration of ADIs);
- Divisions 1, 1A, and 2 of Part VB of the Insurance Act (relating to statutory and judicial management of general insurers and target bodies corporate, as well as to external administration of general insurers); and
- Part 8 of the Life Insurance Act (relating to statutory and judicial management of life insurers and target bodies corporate, as well as to external administration of life insurers). *[Schedule 1, item 59, section 11E of the Banking Act; Schedule 2, item 66, section 62ZVA of the Insurance Act; Schedule 3, item 6, section 16ZE of the Life Insurance Act]*

7.17 To the extent that these powers do apply to foreign ADIs and foreign insurers, the amendments limit the scope of the powers to the ‘Australian business assets and liabilities’ of the foreign regulated entity and, where relevant, to the management of the foreign regulated entity as it relates to its Australian business assets and liabilities. The powers apply to foreign life insurers in a substantially similar way; see 7.19 to 7.22 *[Schedule 1, item 59, subsection 11E(1) of the Banking Act; Schedule 2, item 66, subsection 62ZVA(1) of the Insurance Act]*

7.18 The Insurance Act and Life Insurance Act currently include foreign insurers within the scope of the judicial management regime in each of those Acts. However, the “*insurance* business carried on outside Australia by a foreign general insurer” and the “*life insurance* business carried on outside Australia” by a foreign life company is currently excluded from the scope of judicial management (see existing section 62ZO of the Insurance Act and existing section 16ZE and subsection 165(4) of the Life Insurance Act). The position in relation to ancillary (non-insurance) business is less clear under the existing provisions. Depending on the circumstances, the amendments may expand the scope of assets and liabilities that a judicial manager may be appointed to control.

Scope of application in the Life Insurance Act

7.19 Existing Part 8 of the Life Insurance Act includes provisions relating to judicial management, external administration and winding up. It is amended to include the new statutory management provisions (see Chapter 2). In order to ensure that Part 8 is applied to foreign life insurers appropriately, a number of amendments are made to existing section 16ZE, which currently provides that the Life Insurance Act does not apply

in relation to life insurance business carried on outside Australia by an eligible foreign life insurance company.

7.20 Under the Bill, all of Part 8, except for sections 180, 181, and 182 (which relate to applications for the winding up of life companies), will apply to only the Australian business assets and liabilities and the management of that business of a foreign life company. This covers the majority of provisions in Part 8, including the existing judicial management regime and new statutory management regime. *[Schedule 3, item 6, subsections 16ZE(3) and 16ZE(4) of the Life Insurance Act]*

7.21 Sections 180, 181, and 182 also apply to foreign life insurers. However, the Bill does not confine the application of these sections to the foreign life insurer's business that comprises its Australian business assets and liabilities, or to the management thereof. These sections relate to the winding up of life insurers, and allow APRA to apply for the winding up of a life insurer (including a foreign life insurer). The amendments exclude these sections in order to rely on the existing provisions in Part 5.7 of the Corporations Act that define the Australian courts' powers to wind up a foreign corporation. It will be a matter for the Court to determine the scope of the winding up order. This is particularly important in order to ensure that the scope assets and liabilities of the foreign life insurer that may be subject to such order is appropriate. In relation to provisions outside Part 8, section 16ZE will continue to provide that these do not apply in relation to life insurance business carried on outside Australia by an eligible foreign life insurance company. *[Schedule 3, item 6, subsection 16ZE(2) of the Life Insurance Act]*

7.22 See 7.42 to 7.48 and Chapter 9 generally for more information about how the amendments to this Bill affect APRA's powers to apply for the winding up of regulated entities.

Consequential impact on the existing provisions of the Industry Acts

7.23 The Bill also repeals and replaces certain existing provisions of the Industry Acts that define the way that the Industry Acts apply to foreign regulated entities. This is necessary to provide certainty as to how these powers may be applied to foreign regulated entities. In particular, the Bill repeals section 62ZO of the Insurance Act (which currently excludes insurance business carried on outside Australia by a foreign general insurer from the scope of judicial management), and replaces it with a new section which provides that that the judicial management and new statutory management provisions only apply to the Australian business assets and liabilities, and related management, of a foreign general insurer. The Bill also makes extensive amendments to section 11E of the Banking Act (which sets out how the protection of depositor provisions in Division 2 of Part II of that Act apply in relation to foreign

insurers) and 16ZE of the Life Insurance Act (which explains how the Act applies in relation to foreign life companies). *[Schedule 1, items 58 and 59, section 11E of the Banking Act; Schedule 2, items 57 and 66, sections 62ZO and 62ZVA of the Insurance Act; Schedule 3, item 6, section 16ZE of the Life Insurance Act]*

7.24 With respect to the Banking Act, the Bill preserves the existing position that Division 2 of Part II (except as it relates to statutory management) and Division 2AA of Part II of the Banking Act do not apply to foreign ADIs. Division 2 of Part II includes provisions relating to statutory management and recapitalisation directions. The recapitalisation direction provisions in Division 2 will *not* apply to foreign ADIs, but the statutory management provisions *will* apply in relation to the Australian business assets and liabilities of the foreign ADI and related management functions. Division 2AA relates to the financial claims scheme for protected account holders and it will *not* apply to a foreign ADI. *[Schedule 1, item 58, section 11E(1B) of the Banking Act]*

7.25 The Bill also ensures that the existing requirements in section 11F do not affect APRA's ability to take control of a foreign ADI's Australian business assets and liabilities. Section 11F currently provides that if a foreign ADI (whether in or outside Australia) suspends payment or becomes unable to meet its obligations, the assets of the ADI in Australia are to be available to meet the ADI's liabilities in Australia in priority to all other liabilities of the ADI. The Bill will amend this to ensure that this does not have the unintended effect of requiring a statutory manager to wind up the Australian business of a foreign ADI. (Similar amendments are made to section 13A of the Banking Act – see 2.87, 2.88 and 2.89.) APRA's resolution objectives, and the methods used to achieve those objectives during statutory management, are not intended to be constrained by the existing law that requires, in the event that a foreign ADI suspends payment or becomes unable to meet its obligations, the foreign ADI's assets in Australia to be available to meet its liabilities in Australia in priority to all other liabilities of the ADI. *[Schedule 1, items 61 and 62, subsection 11F(2) of the Banking Act]*

Appointing a statutory manager to the Australian business of a foreign regulated entity

Grounds for taking control of a foreign regulated entity

7.26 The Bill amends the Industry Acts to provide that the statutory management regime applicable to domestically-incorporated entities is also applicable to foreign regulated entities with respect to their Australian business assets and liabilities and the management of the foreign entity to the extent that the management relates to such business. In general, the grounds for such an appointment are the same as those on which a statutory manager may be appointed to a domestically-incorporated

regulated entity, apart from the additional ground discussed at 7.27 and 7.28. *[Schedule 1, item 58 and 59, section 11E of the Banking Act; Schedule 2, item 66, section 62ZVA of the Insurance Act; Schedule 3, item 6, section 16ZE of the Life Insurance Act]*

7.27 The Bill also amends the Industry Acts to add further specific grounds for appointing a statutory or judicial manager to a foreign regulated entity where an external administrator has been appointed to that entity (or other similar appointment) in a foreign country, or there has been an application for the external administration of that entity (or another similar procedure) in a foreign country with respect that entity. this additional basis for appointment is described at 2.56, 2.67, 2.68 and 2.69. *[Schedule 1, item 64, paragraph 13A(1)(e) of the Banking Act; Schedule 2, item 58, paragraph 62ZOA(2)(e) of the Insurance Act; Schedule 3, item 52, paragraph 179AA(2)(e) of the Life Insurance Act]*

7.28 In the case of a foreign regulated entity, the new grounds for appointing a statutory manager or judicial manager also refer to processes similar to external administration, or applications for processes similar to external administration, that may be instituted overseas in respect of that entity. These processes include an action by a resolution authority in another jurisdiction to administer or otherwise take control (whether directly or indirectly) of the business of a foreign regulated entity. In a cross-border context there may be a need for resolution actions to be coordinated between authorities in different jurisdictions. As such, it is important for APRA to have the powers to respond to a foreign resolution authority implementing a resolution action in respect of a foreign regulated entity. APRA could use its power to take control of a foreign regulated entity to support or facilitate action by a foreign resolution authority or to take measures on its own initiative to resolve the entity's operations in Australia.

Effect of statutory management on directors and management of a foreign regulated entity

7.29 The Bill amends the Industry Acts to provide greater certainty about the effects of statutory management on the governance arrangements for a foreign regulated entity. *[Schedule 1, item 174, subsections 15(3A) to 15(3C) of the Banking Act; Schedule 2, item 58, subsections 62ZOP(7) to 62ZOP(9) of the Insurance Act; Schedule 3, item 52, subsections 179AP(7) to 179AP(9) of the Life Insurance Act]*

7.30 While the appointment of a statutory manager to a domestically-incorporated entity causes its directors to cease to hold office, this approach would not be appropriate regarding a foreign regulated entity which will have other operations outside Australia that are not within the scope of statutory management in Australia.

7.31 Instead, the amendments provide that the directors of the foreign regulated entity are prevented from acting in relation to the Australian business assets and liabilities of a foreign regulated entity, or the management of the body corporate to the extent that it relates to such assets and liabilities, once the entity is under statutory management. *[Schedule 1, item 174, subsections 15(3B) and 15(3C) of the Banking Act; Schedule 2, item 58, subsections 62ZOP(7) and 62ZOP(9) of the Insurance Act; Schedule 3, item 52, subsections 179AP(7) and 179AP(9) of the Life Insurance Act]*

7.32 The Bill also provides that the appointment of an agent in Australia of a foreign general insurer, and the Compliance Committee members of a foreign life insurer, ceases to have effect once a statutory manager takes control of the entity's Australian business assets and liabilities. Further, such a person may not be reappointed for the duration of statutory management. It is intended that the statutory manager have the powers and functions of the agent in Australia or Compliance Committee members for the duration of statutory management. As is the case for directors of the foreign insurer, any acts or purported acts by the former agent in Australia or Compliance Committee after the commencement of statutory management are invalid and of no effect. *[Schedule 2, item 58, subsections 62ZOP(3), 62ZOP(4) and 62ZOP(6) of the Insurance Act; Schedule 3, item 52, subsections 179AP(3), 179AP(4) and 179AP(6) of the Life Insurance Act]*

Termination of statutory management of a foreign regulated entity

7.33 The Bill amends the Insurance and Life Insurance Acts to implement specific provisions for the termination of statutory management of foreign insurers. In particular, the amendments change the matters to be addressed by APRA before the ultimate termination of control of a foreign insurer under the Insurance and Life Insurance Acts.

7.34 The harmonised statutory management regime under each of the Industry Acts requires APRA to take certain steps before it can terminate the statutory management of a regulated entity. These steps require APRA to ensure that the regulated entity has directors in place. This can be by ensuring that directors are validly appointed under the entity's constitution or by the statutory manager appointing directors to the entity. Alternatively, APRA is required to ensure that a liquidator has been appointed to the entity.

7.35 The amendments create further requirements where APRA is terminating the statutory management of a foreign insurer under the Insurance or Life Insurance Acts. Before ending the statutory management of a foreign insurer, APRA must ensure that an agent in Australia is appointed in the case of a foreign general insurer, or a Compliance Committee established in the case of a foreign life insurer. Otherwise, APRA must ensure that a liquidator has been appointed to the Australian

business assets and liabilities of the foreign insurer. *[Schedule 2, item 58, subsection 62ZOC(2) of the Insurance Act; Schedule 3, item 52, subsection 179AC(2) of the Life Insurance Act]*

7.36 These amendments are intended to ensure foreign insurers have functional local governance structures to continue operations in Australia after statutory management.

Effect of judicial management on agents in Australia and Compliance Committees of foreign insurers

7.37 The Bill amends the Insurance and Life Insurance Acts to provide that an agent in Australia for a foreign general insurer and the members of a Compliance Committee for a foreign life insurer cease to have their powers and functions upon the appointment of a judicial manager to a foreign insurer, and they lose these powers and functions for the period that the foreign insurer is under judicial management. *[Schedule 2, item 38, subsection 62T(1) of the Insurance Act; Schedule 3, item 33, subsection 165(1) and 165(2) of the Life Insurance Act]*

7.38 The Insurance Act requires all foreign general insurers and subsidiaries of foreign general insurers to have an agent in Australia (see existing section 118 of the Insurance Act). Similarly, the Life Insurance Act requires all foreign life insurers to have a Compliance Committee (see existing section 16ZF of the Life Insurance Act). Agents in Australia and Compliance Committees have a number of powers and functions with respect to the Australian operations of a foreign insurer. However, the current law does not explain the effect of judicial management on the agent in Australia or the members of a Compliance Committee.

7.39 These amendments interact with the amendments to the judicial management provisions in the Insurance and Life Insurance Acts (explained in Chapter 2 – see 2.115 to 2.121) that ensure that persons with the powers and functions of an officer of an insurer cease to have those powers and functions for the duration of judicial management.

7.40 The amendments put beyond doubt that agents in Australia and members of Compliance Committees cannot exercise their powers and functions during the judicial management of a foreign insurer, given that this would conflict with a judicial manager's control of a foreign insurer with respect to its Australian business assets and liabilities.

7.41 The Bill also ensures that, upon the cancellation of judicial management of a foreign insurer, the agent in Australia or members of the Compliance Committee (as appropriate) regain their powers and functions. *[Schedule 2, item 50, paragraph 62ZF(5)(c) of the Insurance Act; Schedule 3, item 45, paragraph 172(5)(c) of the Life Insurance Act]*

Clarify that APRA may apply to the Court for the winding up of a foreign regulated entity

7.42 The Bill amends the Industry Acts to include specific provisions relating to the winding up of a foreign regulated entity. These amendments clarify that APRA may apply to the Federal Court of Australia for the winding up of a foreign regulated entity.

7.43 Regarding foreign ADIs, the Bill provides three grounds on which APRA may apply for the winding up of a foreign ADI;

- where the foreign ADI is unable to meet its liabilities in Australia, or in one or more foreign countries, as and when they become due and payable;
- where application for the winding up or other external administration of the foreign ADI, or for a similar procedure in respect of the foreign ADI, has been made in one or more foreign countries; or
- an external administrator has been appointed to the foreign ADI, or a similar appointment in respect of the foreign ADI has been made, in one or more foreign countries. *[Schedule 1, item 60, section 11EA of the Banking Act]*

7.44 In a cross-border context there may be a need for resolution actions to be coordinated between authorities in different jurisdictions. As such it is important for APRA to have the powers to respond to the application for, or commencement of, procedures in foreign jurisdictions, such as a foreign resolution authority implementing a resolution action in respect of a foreign regulated entity. APRA could use its power to apply for winding up to support or facilitate action by a foreign resolution authority or to take measures on its own initiative to quickly secure the assets of a distressed foreign ADI in order to meet its liabilities in Australia. If APRA's application results in an order for the winding up of a foreign ADI, the winding up is to be conducted in accordance with the Corporations Act.

7.45 The amendments also adapt the existing requirement in subsection 14E(3), providing that APRA must notify the Minister if it has made an application for the winding up of a foreign ADI. *[Schedule 1, item 60, subsection 11EA(3) of the Banking Act]*

7.46 The Bill also includes amendments to existing section 181 of the Life Insurance Act in relation to foreign life insurers to provide that APRA may apply for the winding up of a foreign life insurer where an application for, the appointment of, an external administrator (or similar

procedure) has been commenced or occurred in a foreign country.
[Schedule 3, item 54, subsection 181(2) of the Life Insurance Act]

7.47 The current law already provides that APRA may apply for the winding up of a general insurer, including a foreign general insurer, under the Insurance Act (under section 62ZU) or under the Corporations Act (under section 62ZV). As such, analogous amendments to the Insurance Act of the kind made to the Banking Act are not necessary because APRA may apply for the winding up of a foreign general insurer under the Corporations Act in circumstances set out in that Act.

7.48 As a minor amendment, a note has been added to section 62ZV to explain the relationship between sections 62ZU and 62ZV of the Insurance Act and sections 459P and 462 of the Corporations Act.
[Schedule 2, item 65, section 62ZV of the Insurance Act]

Enable APRA to revoke the authorisation of a foreign-regulated entity if the entity's authorisation is revoked by a foreign country

7.49 The Bill amends the Industry Acts to enable APRA to revoke the authorisation of a foreign regulated entity to carry on banking or insurance business if the entity's authorisation is revoked or otherwise withdrawn in a foreign country.

7.50 The amendments provide APRA with the power to revoke a foreign regulated entity's authorisation in Australia if its authorisation has been revoked or withdrawn in a foreign country, without having to satisfy further grounds for revocation. This may be important where the entity's conduct in a foreign country has been of such prudential concern as to warrant the revocation of its authorisation to conduct banking or insurance business in Australia. It is not intended to be relevant in a situation where an authorisation in a foreign country has been withdrawn for reasons that do not give rise to prudential concerns, for example where the entity has ceased its operations in the foreign country.

7.51 To this end, the Bill includes this new power within the relevant parts of the Industry Acts. *[Schedule 1, item 16, paragraph 9A(2)(j) of the Banking Act; Schedule 2, item 11, paragraph 15(1)(fa) of the Insurance Act; Schedule 3, item 8, paragraph 26(1)(h) of the Life Insurance Act]*

7.52 Note that a reference to a 'foreign country' is intended to include any jurisdictions within a foreign country. For example, where a foreign regulated entity has its licence revoked by an authority within a state of a foreign country.

Harmonise the power to direct that a foreign regulated entity not transfer assets out of Australia across the Industry Acts

7.53 The Bill amends the Insurance and Life Insurance Acts to provide APRA with an explicit power to direct foreign insurers in respect of transfers of assets and liabilities in or out of Australia.

7.54 The Banking Act already includes a specific power for APRA to make a direction to a foreign ADI to require that it transfer, or not transfer, assets or liabilities either to or out of Australia. In general terms existing subsection 11CA(2B) of the Banking Act gives APRA power to direct a foreign ADI to:

- return assets to the control of the Australian business;
- not transfer them out of the control of the Australian business;
- ensure that liabilities ceases to be the responsibility of the Australian business; or
- not act in a way that results in them becoming the responsibility of the Australian business.

7.55 These amendments add equivalent provisions to the Insurance and Life Insurance Acts so that APRA can make a direction of this kind to a foreign insurer. *[Schedule 2, item 118, subsection 104(4A) of the Insurance Act; Schedule 3, item 88, subsection 230B(3A) of the Life Insurance Act]*

7.56 These provisions are not intended to limit the scope of APRA's other directions powers, which are also applicable to foreign regulated entities.

7.57 Minor stylistic amendments have been made to improve the expression of paragraphs 11CA(2B)(a) and 11CA(2B)(b) of the Banking Act, and these amendments have been copied into the new provisions of the Insurance and Life Insurance Acts. *[Schedule 1, items 40 and 41, paragraphs 11CA(2B)(a) and 11CA(2B)(b) of the Banking Act]*

Implementing a voluntary or compulsory transfer of Australian business assets and liabilities of a foreign regulated entity

7.58 The Bill amends the Transfer Act to include specific provisions for the transfer of Australian business assets and liabilities of a foreign regulated entity.

7.59 While the Transfer Act does not explicitly exclude the possibility of voluntary or compulsory transfers of business from foreign regulated entities, it does not address the practicalities of such a transfer.

7.60 In particular, the Transfer Act does not establish the scope of assets and liabilities of a foreign regulated entity that might be transferred under the powers in that Act, and it includes some provisions which might be taken to imply that such transfers are not possible. In particular, existing paragraphs 11(1)(d) and 25(2)(f) currently provide that, in order for APRA to approve or determine a transfer, APRA must be satisfied that complementary State or Territory legislation exists where the transferring and receiving bodies are established. This arguably means that a transfer is only possible where the transferring and receiving bodies are established in Australia.

7.61 The Bill includes new definitions of ‘eligible foreign life insurance company’, ‘foreign ADI’, and ‘foreign general insurer’ that correspond to the equivalent definitions in the Industry Acts, as well as a definition of ‘Australian business assets and liabilities’ which aligns with the equivalent definition added to the Industry Acts under the amendments described at 7.10 to 7.17. *[Schedule 4, items 3 and 6, subsection 4(1) of the Transfer Act]*

7.62 Further, the Bill inserts a new provision that states that, for the purposes of a voluntary or compulsory transfer of business from a foreign regulated entity, the Australian business assets and liabilities of the foreign regulated entity are to be treated as if they comprised the entire business for the purposes of the relevant provisions in the Transfer Act. *[Schedule 4, item 96, section 43A of the Transfer Act]*

7.63 These amendments only relate to transfers under the Transfer Act. They do not affect the existing provisions for the voluntary transfer of business of a general insurer or life insurer (including a foreign insurer) under Part III, Division 3A of the Insurance Act or Part 9 of the Life Insurance Act.

7.64 These amendments are intended to remove any ambiguity in Australian law about which assets and liabilities are covered under a transfer of business from a foreign regulated entity under Part 3 or Part 4 of the Transfer Act.

7.65 The Bill also amends existing paragraphs 11(1)(d) and 25(2)(f) to remove any inference that the transferring and receiving bodies must be established in Australia. Those provisions will now be expressed to apply “where” these bodies are established in Australia. For other changes affecting these provisions, see 4.43. *[Schedule 4, items 28 and 53, paragraphs 11(1)(d) and 25(2)(f) of the Transfer Act]*

Consequential amendments

Foreign insurers may issue policies during judicial management in certain circumstances

7.66 The Bill includes new provisions that explicitly permit the issuing of policies by a foreign insurer that is under judicial management in the course carrying on life insurance business carried on outside Australia. This position reflects the current law in subsection 62T(3) and section 62ZO of the Insurance Act and section 16ZE and subsection 165(4) of the Life Insurance Act. *[Schedule 2, item 66, subsection 62ZVA(2) of the Insurance Act; Schedule 3, item 6, subsection 16ZE(5) of the Life Insurance Act]*

Application and transitional provisions

7.67 Directions given by APRA to insurers (see 7.54) apply to directions given on or after the commencement time. *[Schedule 2, Part 2, item 140; Schedule 3, item 119]*

Chapter 8

Financial Claims Scheme

Outline of chapter

8.1 Schedules 1 and 2 to this Bill amend the Banking and Insurance Acts to make certain enhancements to the efficiency and operation of the FCS.

Context of amendments

8.2 The FCS was established by the Government in 2008 as two separate schemes. One is applicable to locally-incorporated ADIs and the other is applicable to general insurers. The FCS is administered by APRA.

8.3 The FCS provides an important backstop within Australia's resolution regime. While its primary function is to protect retail depositors and policyholders by providing prompt access to their funds, the FCS also contributes to financial stability, for example by limiting the potential for a destabilising 'run' on deposits in the case of ADIs, and more generally by promoting confidence in the financial system.

8.4 The FCS for ADIs provides depositors with a guarantee of their deposits up to a pre-determined limit, which is currently set at \$250,000 per account-holder, per ADI. In the case of general insurers, the FCS provides compensation for most claims up to \$5,000 against a failed general insurer, with claims above \$5,000 also covered for eligible policyholders and certain eligible third parties.

8.5 While the legislative framework for the FCS is broadly consistent with international standards, particularly the IADI Core Principles for Effective Deposit Insurance Schemes, some of the provisions would benefit from further enhancements.

8.6 Some changes to the ADI FCS framework were the subject of the then Government's consultation paper released in May 2011 entitled 'Financial Claims Scheme: Consultation Paper'. The enhancements in this Bill build upon those changes, as well as certain proposals in relation to the FCS for general insurers from the 2012 Consultation Paper.

8.7 To date, the FCS has been declared once in respect of a small general insurer and APRA's experience in administering the FCS for that general insurer also serves as a basis for some of the enhancements in this Bill.

Summary of new law

8.8 Schedules 1 and 2 to this Bill amend the Banking and Insurance Acts to:

- establish an additional payment mechanism to enable FCS entitlements to be satisfied when there has been a transfer of deposits to another ADI or policyholder claims to another general insurer;
- enable APRA to obtain information from third parties in relation to the FCS;
- facilitate the effective payout of FCS entitlements to third party claimants of a policyholder of a failed general insurer where the policyholder is in liquidation;
- enable APRA to make interim payments to claimants under the FCS applicable to general insurers;
- grant the Treasurer the discretion to declare the FCS at an earlier time, upon appointment of a statutory manager; and
- reduce the reporting burden regarding withholding tax in relation to interest on amounts paid under the FCS.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Enable FCS entitlements to be satisfied by transfer of deposits or policyholder claims</i>	
<p>The Banking and Insurance Acts allow FCS funds to be used to support a compulsory transfer of business under the Transfer Act comprising:</p> <ul style="list-style-type: none"> • in the case of a declared ADI, all the protected accounts of the ADI (or all such accounts subject to a limit applied on a per-account-holder basis to reflect the cap that applies per account-holder under section 16AG of the Banking Act); or • in the case of a declared general insurer, at least one protected policy of the general insurer, <p>to meet the entitlements of protected account-holders or relevant policyholders by transferring their accounts or policies to a receiving body.</p>	<p>FCS funds cannot be used to support a compulsory transfer of business under the Transfer Act, in order to meet the entitlements of protected account-holders and policyholders under the FCS by transferring their accounts or policies to a receiving body.</p>
<i>Enable APRA to obtain information from third parties in relation to the FCS</i>	
<p>APRA may obtain information from any other person (in addition to those specified in the current law) relevant to determining and paying amounts under the FCS.</p>	<p>APRA may obtain only from specified persons (for example, a statutory manager of an ADI) information relevant to determining and paying amounts under the FCS.</p>
<i>Ensure the effective payout of FCS entitlements to third-party claimants of the policyholder of a failed general insurer when the policyholder is in liquidation</i>	
<p>If APRA makes payment under the FCS to an insolvent corporate policyholder, it will be clear that a third party claiming against the insolvent policyholder will be accorded priority in liquidation, under section 562 of the Corporations Act, for the amount claimed and paid to the insolvent policyholder.</p>	<p>If APRA makes payment under the FCS to an insolvent corporate policyholder, it uncertain whether a third party claiming against the insolvent policyholder will be accorded priority in liquidation, under section 562 of the Corporations Act, for the amount claimed and paid to the insolvent policyholder.</p>

<i>New law</i>	<i>Current law</i>
<i>Enable APRA to make interim payments to claimants under the FCS</i>	
APRA may determine interim claims as they come in, rather than having to wait for the final claim to come in before making a determination.	It is uncertain whether APRA can make a series of interim determinations allowing additional payments under the insurance FCS. This may be desirable where, for example, the losses insured by a protected policy materialise, and become payable, on multiple occasions over a period of time or where it is expedient to make an initial payment of an undisputed amount and further payments following assessors' reports.
<i>Granting the Treasurer discretion to declare the FCS at an earlier time</i>	
The Treasurer may now declare the FCS in relation to an ADI or general insurer once a statutory manager has taken control of the ADI or general insurer, in addition to the existing preconditions in the law.	The Treasurer may declare the FCS in relation to an ADI only when APRA has applied to wind up the ADI, and in relation to a general insurer only when it is under judicial management or an external administrator has been appointed.
<i>Reducing the reporting burden in relation to withholding tax</i>	
APRA is no longer required to report to the ATO any interest paid and withholding tax applicable on amounts paid out to account-holders or policyholders protected under the FCS.	APRA is required to report to the ATO any interest paid and withholding tax applicable on amounts paid out to account-holders or policyholders protected under the FCS.

Detailed explanation of new law

Enable FCS entitlements to be satisfied by transfer of deposits or policyholder claims

8.9 The Banking and Insurance Acts currently provide APRA with various methods to meet an account-holder's or policyholder's entitlement under the FCS, such as by opening a new account for an account-holder, or paying the amount to the policyholder or applying the amount for the person's benefit.

8.10 The May 2011 Consultation Paper recommended an additional payment mechanism to facilitate the transfer of protected deposit accounts from a failed ADI to a receiving ADI. This new mechanism would enable

the account to be transferred with all direct debit and credit facilities in a way that would allow it to continue to be used seamlessly as if it were still with the failed ADI. APRA would determine whether the transfer option would provide a cost-effective and efficient option based on the circumstances in each case. A similar proposal in respect of the FCS applicable to general insurers was included in the September 2012 Consultation Paper.

8.11 APRA already has extensive powers under the Transfer Act to effect a transfer of business from one ADI to another. This is also the case with a transfer of business from one general insurer to another.

8.12 Transfer of an ADI's protected accounts may have the advantage of preserving arrangements such as direct debit facilities, and therefore be less disruptive than the alternative of APRA making direct FCS payments to the account-holders. In the context of general insurers, a transfer of business, especially long-tail insurance claims, may be either the only practical or the most cost-effective means of maintaining an insured policyholder's protection.

8.13 The Bill therefore amends the Banking and Insurance Acts to create an additional payment mechanism for the FCS by allowing APRA to use FCS funds to facilitate a transfer of business from a declared ADI or from a declared general insurer to a receiving body.

Transferred liabilities determination

8.14 The Bill amends the Banking and Insurance Acts to allow APRA to make a transferred liabilities determination, which will facilitate the transfer of business and the meeting of FCS entitlements.

8.15 APRA may only make a transferred liabilities determination if all of the following apply:

- the Minister has made a declaration under section 16AD of the Banking Act in relation to an ADI (the 'declared ADI'), or a declaration under section 62ZZC of the Insurance Act in relation to a general insurer (the 'declared general insurer');
- APRA has made, or proposes to make, a compulsory transfer determination under section 25 of the Transfer Act that there is to be a total or partial transfer from the declared ADI or general insurer to a receiving body;
- where the transferring body is a declared ADI, the transfer of business will transfer the liabilities in respect of every protected account kept by an account holder with the ADI (or

the liabilities of the declared ADI in respect of every protected account-holder up to their FCS limit – note that if this approach is taken APRA will need to apportion the FCS liability between protected accounts where there are multiple accounts for the account holder which, in aggregate, exceed the FCS limit, as explained below);

- where the transferring body is a declared general insurer, the transfer of business will transfer the liabilities of the general insurer in respect of one or more protected policies issued by the general insurer;
- APRA is satisfied that it will be able to identify those protected accounts or policies;
- APRA has worked out a reasonable estimate of the total amount to which account-holders and policyholders of those protected accounts or policies will be entitled to under the FCS (defined as the FCS amount);
- APRA has worked out a reasonable estimate of the total amount of the costs that would have been incurred by APRA in relation to the exercise of its powers and the performance of its functions if it had administered the FCS in relation to the declared ADI or general insurer instead of making a transferred liabilities determination (defined as the administration amount);
- APRA has worked out a total payment amount being the sum of an FCS payment amount and an administration payment amount (see 8.22 to 8.25 for information about calculating the total payment amount); and
- APRA considers it reasonable in the circumstances to make the determination.

8.16 If APRA makes a transferred liabilities determination in respect of an ADI, it will either transfer *all* of each protected account-holder's balance to the receiving body, or transfer the balance of each protected account-holder up to the FCS limit. In each case the FCS entitlement of each account-holder would be reduced to nil when a certificate of transfer comes into force under the Transfer Act. If the second approach (transfer of accounts up to the FCS limit) is taken, the FCS entitlement of each account-holder would be reduced to nil as outlined in the following two examples:

- Example 1: if an account holder has a single protected account with a balance over the FCS limit of \$250,000 (say \$400,000), then, applying the current limit under section 16AG, only \$250,000 of that account would be transferred to the receiving body with the remainder (\$150,000 in the example) left behind to be claimed by the account-holder in the insolvency of the declared ADI.
- Example 2: if an account-holder has two or more protected accounts with an aggregate balance of over \$250,000, then their balances totalling \$250,000 would be transferred to the receiving ADI with APRA having the discretion to split the accounts to achieve this purpose. The remainder of the balance of the accounts would be left behind to be claimed in the insolvency of the declared ADI *[Schedule 1, item 218, paragraph 16A1A(1)(c)(ii) of the Banking Act]*

8.17 The amendments also require that this determination be made in writing, and that various details (including details of the declared ADI or general insurer, the receiving body, and any other information that APRA considers appropriate) be specified in the determination. *[Schedule 1, item 218, subsection 16A1A(4) of the Banking Act; Schedule 2, item 84, subsection 6ZZMA(4) of the Insurance Act]*

8.18 In order to ensure that transfers of business made under the Transfer Act are certain, the Bill provides that, if APRA has already issued a certificate of transfer under section 33 of the Transfer Act, APRA may not then make a transferred liabilities determination with respect to the protected accounts or protected policies of the declared ADI or general insurer. *[Schedule 1, item 218, subsection 16A1A(2) of the Banking Act; Schedule 2, item 84, subsection 6ZZMA(2) of the Insurance Act]*

8.19 The Bill provides that transferred liabilities determinations are not legislative instruments. The provision is included to assist readers, as such a determination is not a legislative instrument within the meaning of subsection 8(1) of the *Legislation Act 2003*. *[Schedule 1, item 218, section 16A1A of the Banking Act; Schedule 2, item 84, section 6ZZMA of the Insurance Act]*

8.20 The Bill defines a ‘transferred liability determination’ in the Banking and the Insurance Acts to refer to determinations made under sections 16A1A of the Banking Act or 6ZZMA of the Insurance Act (as appropriate). *[Schedule 1, item 10, subsection 5(1) of the Banking Act; Schedule 2, item 7, subsection 3(1) of the Insurance Act]*

8.21 A key difference between the Banking and Insurance Acts regarding transferred liability determinations is that APRA may make a transferred liability determination with respect to a declared general insurer that is only a partial transfer of the protected policies of that

general insurer. The intention is to give APRA the option to make a partial transfer, or multiple partial transfers, to one or more insurers. This will allow APRA to assign protected policies to insurers that are best positioned to accept and manage particular lines of insurance business. It will also be possible to transfer some but not all policies. Policies not transferred would be dealt with by applying the FCS payment processes in the existing provisions. *[Schedule 1, item 218, paragraph 16A1A(1)(c) of the Banking Act; Schedule 2, item 84, paragraph 6ZZMA(1)(c) of the Insurance Act]*

Determining a payment amount

8.22 As part of making a transferred liability determination, the Bill amends the Banking and Insurance Acts to allow APRA to calculate a ‘total payment amount’ that will be paid to the receiving body of the protected accounts or policies. This amount is the sum of two further payment amounts determined by APRA; the ‘FCS payment amount’ and the ‘administration payment amount’. These two amounts should not be confused with the FCS amount and the administration amount. The FCS amount is APRA’s reasonable estimate of the total amount to which protected account-holders would be entitled if the FCS were administered without there being a transferred liabilities determination. The administration amount is APRA’s reasonable estimate of the total amount of administration costs that APRA would incur if it administered the FCS without the transferred liabilities determination. These figures are used to set a ceiling for the purposes of working out the amount to be paid to the receiving body, as described below. *[Schedule 1, item 218, paragraph 16A1B(1)(c) of the Banking Act; Schedule 2, item 84, paragraph 6ZZMB(1)(c) of the Insurance Act]*

8.23 The FCS *payment* amount must be equal to or less than the FCS amount. The FCS payment amount will be an amount APRA considers to be appropriate. It must be deducted from the appropriation in the Financial Claims Scheme Special Account established in Division 2 of Part 5 of the APRA Act. Section 54C of the APRA Act is amended to provide for the debiting of the FCS payment amount from that account. *[Schedule 6, items 3 and 4, section 54C of the APRA Act]*

8.24 When determining an appropriate FCS payment amount and administration payment amount, APRA must consider:

- the total value of the assets that will be transferred from the declared ADI or general insurer to the receiving body in accordance with the transfer of business;
- the total value of the liabilities that will be transferred from the declared ADI or general insurer to the receiving body in accordance with the transfer of business; and

- any other matter that APRA considers appropriate. *[Schedule 1, item 218, and subsection 16A1B(2) of the Banking Act; Schedule 2, item 84, subsection 6ZZMB(2) of the Insurance Act]*

8.25 The administration *payment* amount must be equal to or less than the administration amount. As this amount relates to the cost of administering the FCS, rather than the cost of meeting entitlements under the FCS, the administration payment amount is to be paid out of the APRA Special Account appropriation created by existing section 54 of the APRA Act. In this regard it should be noted that existing section 54 of the APRA Act provides that the APRA Special Account may be debited in making any payments which APRA is authorised or required to make under law of the Commonwealth. This excludes payments that must be deducted from the Financial Claims Scheme Special Account established under section 54C of the APRA Act. As noted above, section 54C of the APRA Act is amended to provide for the debiting of the FCS payment amount from that account, but not the administration payment amount. Accordingly, the administration payment amount may be deducted from the APRA Special Account. This is appropriate because that special account general provides for APRA's administration expenses. *[Schedule 1, item 218, paragraph 16A1B(1)(b) of the Banking Act; Schedule 2, item 84, paragraph 6ZZMB(1)(b) of the Insurance Act; Schedule 6, items 3 and 4, section 54C of the APRA Act]*

8.26 The amendments also allow APRA to specify a nil amount for the FCS payment amount and/or the administration payment amount. This is intended to cover circumstances where APRA has calculated the FCS amount and administration amount but does not consider it appropriate to pay the receiving body any amount with respect to either or both of the FCS amount or administration amount.

8.27 The most likely circumstance in which APRA would consider that both of these amounts should be specified as nil would be that the value of other assets that are also being transferred to the receiving body will be sufficient to cover transferred liabilities, including liabilities in respect of protected accounts.

8.28 The intention of these amendments is to ensure that APRA has discretion to determine an appropriate amount to pay to a receiving body of protected accounts or policies. As a result of these amendments, and reflecting the fact that a transfer of business will usually include assets, APRA may determine that it is to pay a lower amount through a transferred liabilities determination than the amount that it has calculated as the total FCS liability of the transferred accounts/policies. This approach may provide a better financial outcome for the Commonwealth and may also provide continuity for depositors and policyholders.

Effect of a transferred liabilities determination

8.29 The Bill amends the Banking and Insurance Acts to entitle the receiving body, in respect of a transferred liabilities determination, to receive the total payment amount specified in the determination (see 8.22) once APRA has issued the relevant certificate of transfer under section 33 of the Transfer Act.

8.30 These amendments provide that, once APRA has made a transferred liabilities determination, and has issued certificate of transfer, the receiving body is entitled to be paid by APRA an amount equal to the total payment amount. The declared ADI or general insurer is then liable to pay APRA an amount equal to the total payment amount. *[Schedule 1, item 218, section 16AIC(1) of the Banking Act; Schedule 2, item 84, section 62ZZMC(of the Insurance Act)]*

8.31 Note that the Bill also provides that the assets of an insolvent ADI are available to meet an amount owed to APRA under section 16AIC before any other liabilities. *[Schedule 1, item 66, paragraph 13A(3)(a) of the Banking Act]*

8.32 This is because the total payment amount determined by APRA is effectively the entitlement under the FCS of the protected account-holders of the insolvent ADI and should be treated in the same way in the winding up of the insolvent ADI.

8.33 There is no similar provision in the Insurance Act. Subsection 116(3) of the Insurance Act requires that assets in Australia of an insurer be applied first to liabilities in Australia in the winding up of the insurer. Amounts paid by APRA under the FCS, including those paid in connection with a transferred liabilities determination, will (under section 62ZZL) become liabilities of the insurer to APRA. They will be primarily payable in Australia, and will fall within the protection of subsection 116(3).

8.34 The Bill also ensures that the protected account-holder or policyholder is no longer entitled to any amount under the FCS with respect to any protected account in the case of a declared ADI, or with respect to the relevant transferred policy in the case of a declared general insurer. *[Schedule 1, item 218, subsection 16AIC(3) of the Banking Act; Schedule 2, item 84, subsection 62ZZMC(3) of the Insurance Act]*

8.35 This is because, as a result of the transferred liabilities determination, the FCS entitlement of the protected account-holder or policyholder will effectively be provided for by the receiving body following the transfer of their account or policy to the receiving body.

8.36 If APRA has made a transferred liability determination with respect to a declared ADI or general insurer, APRA is not entitled to also rely on the existing FCS provisions that allow APRA to recover the cost of meeting individual entitlements of protected account or policyholders under the FCS from the declared ADI or general insurer. However, the declared ADI or general insurer is then liable to pay APRA an amount equal to the total payment amount (as noted in 8.30). *[Schedule 1, item 218, subsection 16AIC(6) of the Banking Act; Schedule 2, item 84, subsection 62ZZMC(6) of the Insurance Act]*

Enable APRA to obtain information from third parties in relation to the FCS

8.37 APRA may currently under the Banking or Insurance Acts require certain persons to give specified information in relation to the FCS. Those persons are:

- an ADI or general insurer (under section 16AK of the Banking Act and section 62ZZP of the Insurance Act); or
- a statutory manager or liquidator appointed to the ADI (under section 16AK of the Banking Act);
- a judicial manager or liquidator appointed to a general insurer (under section 62ZZP of the Insurance Act); or
- an insurance claimant (under section 62ZZR of the Insurance Act).

8.38 However, these provisions do not enable APRA to require information to be sought from other persons who may hold information that facilitates the administration of the FCS.

8.39 In the ADI context, these persons may include third party service providers to whom APRA may delegate FCS functions under section 16AN of the Banking Act, or any other persons (for example, providers of data warehouse facilities, data processing facilities and IT services) who may have provided or may still be providing certain services to the failed ADI.

8.40 In the general insurance context, one issue that has emerged from experience in administering the FCS is that third parties may hold the relevant information, such as claims files. These third parties may include a co-insurer, insurance broker, claims manager or another general insurer to whom liabilities may have been purportedly transferred by the failed general insurer without complete novation.

8.41 The Bill ensures that, in addition to the persons currently listed, APRA may obtain information from a statutory manager appointed (under the Insurance Act), or any other person (under both the Banking Act and the Insurance Act). The Bill also makes amendments to ensure that the purposes for which APRA may obtain information, as set out in existing subsection 16AK(4) of the Banking Act and subsection 62ZZP(4) of the Insurance Act, cover all relevant FCS-related matters. Currently, as a result of an oversight, two matters are omitted. First, for the purpose of preparing or giving a statement or report required by section 16AHA of the Banking Act or section 62ZZKA of the Insurance Act as the case may be (these require an annual statement of FCS payments to be given to account-holders/claimants). Secondly, for the purpose of complying with an obligation under a law relating to taxation. The amendments will ensure that information can be obtained for these purposes. *[Schedule 1, items 221, 222 and 224, subsection 16AK(1) and paragraph 16AK(4)(g) of the Banking Act; Schedule 2, items 88, 89 and 91, subsection 62ZZP(1) and paragraph 62ZZP(4)(e) of the Insurance Act]*

8.42 These amendments extend the scope of persons that APRA can obtain information from regarding the determination and payment of entitlements under the FCS.

8.43 The Bill also extends the current civil penalty provision, punishable by 200 penalty units, to capture any other person. *[Schedule 1, item 227, subsection 16AL(8) of the Banking Act; Schedule 2, item 94, subsection 62ZZQ(11) of the Insurance Act]*

Ensure the effective payout of FCS entitlements to third party claimants of a policyholder of a failed general insurer where the policyholder is in liquidation

8.44 The Insurance Act currently provides for different types of claimants under the FCS framework. Persons who may claim under the FCS are those entitled to claim under insurance cover provided under a protected policy (for example, the policyholder or someone to whom the policy is expressed to apply), and those permitted to recover an amount from a general insurer under legislation such as the *Insurance Contracts Act 1984* and the Corporations Act. Given the scope of persons who may claim under the FCS, it is possible that a claimant may not be a policyholder of a failed general insurer but, rather, a person claiming against such a policyholder.

8.45 The Bill inserts a regulations-making power into the Insurance Act to enable the specification, for the purposes of section 62ZZJ, of any other law providing cut-through rights for third party insurance claimants in addition to those already specified in section 62ZZJ (that is, section 51 of the *Insurance Contracts Act 1984* and section 601AG of the

Corporations Act). [Schedule 2, items 78 to 80, subsection 62ZZJ(3) and paragraphs 62ZZJ(4)(a) and 62ZZJ(4B)(a) to 62ZZJ(4B)(c) of the Insurance Act]

8.46 The reason for this amendment is to have the flexibility to prescribe other statutory third party rights in relation to insurers, including under State and Territory legislation, in addition to section 51 of the *Insurance Contracts Act 1984* and section 601AG of the Corporations Act.

8.47 The use of the regulation-making power ensures that any current or future legislation that is relevant to cut-through rights for third party insurance claimants can be captured if necessary. This power will be useful if (for example) if legislation prescribing third-party claimant rights is amended or relocated to other legislation. See 8.53 for more detail about payments by APRA to third party claimants.

8.48 Section 562 of the Corporations Act provides that, where a company in liquidation had a policy covering liability to a third party, and the company or its liquidator has ‘received’ from the insurer an amount in respect of that liability, the amount must be paid by the liquidator (after deducting expenses of getting that amount) to the third party in priority to all payments under section 556 of the Corporations Act.

8.49 An example of such a circumstance would be where a company has taken out an insurance policy against the risk of compensation to members of the public, who have suffered loss as a result of negligence of the company, under a public liability policy, and the company is in liquidation with outstanding claims for such compensation at the time that the FCS is declared.

8.50 The existing section 62ZZM of the Insurance Act has the effect of ensuring that in the above scenario (and in relation to FCS payments generally) the FCS payment to the insolvent company (or other claimant) will discharge the liability of the general insurer to company. This means that the company, once it receives the payment under the FCS, cannot ‘double dip’ by claiming against the insurer for the same amount.

8.51 However, there is nothing in the current legislation putting the insolvent company or its liquidator under an obligation to pay the FCS amount to the third party in the same way that it would have to, under section 562, if the payment had been received from the insurer in this scenario. Upon receiving the FCS payment, the liquidator may feel obliged to treat the circumstances as falling outside section 562, because the money was not ‘received’ from the insurer. In that event the third party may have no section 562 rights and their claim against the insolvent company which would rank under section 556 of the Corporations Act with general creditors.

8.52 To overcome this, the Bill amends the Insurance Act to provide, for the avoidance of doubt, that for the purposes of subsection 562(1) of the Corporations Act, the FCS amount will be taken to have been 'received' by the person (that is, by the insolvent company) from the general insurer, and therefore the liquidator will be obliged to deal with the payment in accordance with section 562 as if it had been received from the insurer. *[Schedule 2, item 83, subsection 62ZZM(1A) of the Insurance Act]*

8.53 To provide further certainty that third party claimants are able to access the entitlements under the FCS in appropriate situations, further amendments have been made to the existing section 62ZZK. These are intended to ensure that if, APRA makes a payment directly to a person (a third party claimant), that payment will be taken to be made for the benefit of the protected policy holder. *[Schedule 2, item 81, subsection 62ZZK(1A) of the Insurance Act]*

Enable APRA to make interim payments to claimants under the FCS

8.54 Currently, under the FCS, where APRA becomes aware that a person has made a claim under insurance cover provided under a protected policy, section 62ZZI of the Insurance Act places an obligation upon APRA to determine whether a general insurer is liable to the person in respect of the claim and the amount of that liability. Once a determination is made, APRA may make payments to the person, subject to the person meeting the eligibility requirements for claims of \$5,000 or more.

8.55 APRA has encountered difficulties in administering these provisions where personal injury claims have been litigated. While the legal obligation to pay out under a claim may not arise until the quantum of the claim is determined, payments for personal injury claims are often made by general insurers to meet medical and legal costs arising in the interim. It is arguable that APRA has the ability to make such interim payments under the FCS, however it is not clear under the current legislation.

8.56 The Bill addresses this issue by amending the Insurance Act to allow APRA to determine, in accordance with any regulations, interim claims for payment of part or parts of that liability. These provisions apply to claims made by protected policy holders and to claims made by third party claimants with respect to a protected policy. *[Schedule 2, items 71 and 75, sections 62ZZFA and 62ZZGA of the Insurance Act]*

8.57 If APRA determines that an interim claim or claims ought to be accepted, the claimant is entitled to be paid in respect of the interim claim or claims. These payments reduce the person's total entitlement under the

FCS in relation to the protected policy. *[Schedule 2, items 71 and 75, subsections 62ZZFA(4), 62ZZFA(5), 62ZZGA(5) and 62ZZGA(6) of the Insurance Act]*

8.58 For the avoidance of doubt, it should be noted that a claimant may make more than one interim claim.

8.59 Any regulations made under these provisions may prescribe conditions that must be met before a payment of an interim claim is made. This regulations-making power is intended to allow the Government to establish rules and criteria that APRA must apply and consider when making a determination about the eligibility of an interim claim and the amount to be paid by APRA in respect of that interim claim. It is anticipated that the regulations will ensure that the eligibility requirements currently applicable to claims above \$5,000 will apply where cumulative interim claims will exceed that amount. *[Schedule 2, items 71 and 75, subsections 62ZZFA(3) and 62ZZGA(3) of the Insurance Act]*

Granting the Treasurer the discretion to declare the FCS at an earlier time

8.60 The FCS is currently activated at the discretion of the Treasurer once APRA has formed the view that the ADI or general insurer is insolvent and, in the case of an ADI, has applied to the Federal Court for an ADI to be wound up, or in the case of a general insurer, is under judicial management or an external administrator has been appointed.

8.61 The May 2011 Consultation Paper noted the CFR's recommendation that it should be possible for the FCS to be activated earlier in the resolution process, where there is no prospect of the failing ADI being restored to a sound financial condition or being transferred to another ADI. Under the CFR proposal, rather than having to wait until an application has been made by APRA to windup a distressed ADI, the Treasurer would have discretion to activate the FCS as soon as APRA has appointed a statutory manager.

8.62 To this end, the Bill amends the Banking and Insurance Acts to include the statutory management of an ADI or a general insurer as preconditions that allow the Minister to declare the FCS. *[Schedule 1, item 215, subsection 16AD(1) of the Banking Act; Schedule 2, item 69, subsection 62ZZC(1) of the Insurance Act]*

8.63 The existing preconditions for the Minister to declare the FCS (that is, on APRA's application to wind up the ADI or where an external administrator or judicial manager has been appointed to the general insurer) has not changed. It is noted that a separate amendment in the Bill will enable APRA to apply for the winding-up of an ADI without first having to appoint a statutory manager (see Chapter 9).

8.64 These amendments will assist in managing the resolution of a distressed ADI or general insurer. In particular, in the case that a statutory manager is appointed, it would enable the nature of the intended resolution (if this is clear) to be announced, including the declaration of the FCS, at the same time as the statutory manager is appointed. This would provide depositors and policyholders with greater certainty as to the status of their deposits and ability to claim on their policies, and the intended arrangements with respect to accessing their deposits or making claims.

Reducing the reporting burden in relation to withholding tax

8.65 Under existing section 16AHA of the Banking Act, APRA is required to report to the ATO any interest paid (and withholding tax applicable) on amounts paid to account-holders protected under the ADI FCS. A similar provision exists in section 6ZZKA of the Insurance Act with respect to the FCS for general insurers. APRA's previous experience of administering the FCS identified these requirements as unnecessary and inefficient.

8.66 This reporting obligation imposes costs for ADIs and general insurers, which may have to pre-position to report these amounts to APRA under the FCS. Further, APRA's obligation to collect information on these amounts and report to the ATO duplicates the ATO's existing business processes in the annual investment income report (AIIR). This means that the FCS amounts can be reported to the ATO by the liquidator in due course using the AIIR, rather than by a separate report from APRA.

8.67 The Bill therefore amends the Banking and Insurance Acts to remove the obligation that APRA report to the ATO the amounts paid to and withheld from account-holders or policyholders protected under the FCS. *[Schedule 1, item 217, subsection 16AHA(3) of the Banking Act; Schedule 2, item 82, subsection 6ZZKA(3) of the Insurance Act]*

8.68 These amendments will improve the efficiency of administering the FCS.

8.69 The Bill also makes consequential amendments to the Banking and Insurance Acts to remove references to the reports. *[Schedule 1, item 223, paragraph 16AK(4)(ea) of the Banking Act; Schedule 2, item 90, paragraph 6ZZP(4)(da) of the Insurance Act]*

Consequential amendments

Objectives of the FCS

8.70 The Bill makes consequential amendments to the Banking and Insurance Acts to include statutory management of an ADI or general insurer (as appropriate; see 8.60 to 8.64) as one of the potential preconditions to the declaration of the FCS; as well as including the additional payment mechanism (see 8.9 to 8.35) as part of the objectives of the FCS. *[Schedule 1, items 213 and 214, section 16AB of the Banking Act; Schedule 2, items 67 and 68, section 62ZW of the Insurance Act]*

Clarifying effect of a transferred liabilities determination under the Insurance Act

8.71 The Bill makes consequential amendments to the Insurance Act to ensure that, where a transferred liabilities determination results in a receiving body receiving a total payment amount (see 8.9 to 8.35), sections 62ZZK, 62ZZKA, 62ZZL, and 62ZZM (which relate to the method of paying entitlements) do not apply in relation to the entitlement of the receiving body. *[Schedule 2, item 84, section 62ZZMD of the Insurance Act]*

8.72 The Bill also amends the *Income Tax Assessment Act 1997* to exclude the additional payment mechanism (see 8.9 to 8.35) from the operation of these provisions. *[Schedule 7, item 7, paragraph 322-30(b) of the Income Tax Assessment Act 1997 and the note to that section]*

Amending notes to the Insurance Act FCS provisions

8.73 The Bill makes consequential amendments to the Insurance Act to reflect the expanded scope of laws that APRA may consider when determining whether to pay an amount under the FCS to a claimant (see 8.44). *[Schedule 2, items 72 and 73, subsections 62ZZG(2) and 62ZZG(3) of the Insurance Act]*

Consequential amendments relating to interim payments

8.74 The insertion of the new provisions enabling interim payments require consequential amendments to be made to section 62ZZH of the Insurance Act and a Note to that section. Section 62ZZH provides for notionally extended insurance cover from the date of the FCS declaration of the insurer to 28 days after that. In simple terms this provisions mean that for FCS purposes the relevant insurance policy is treated as though it continued in force for that period even if it did not. This gives policyholders breathing space to arrange alternate insurance but keeps them covered under the FCS in the interim. The amendments to section 62ZZH ensure that this notionally extended cover protection applies not

only in relation to substantive claims under existing sections 6ZZZF and 6ZZZG, but also to interim claims under the new interim claim provisions.
[Schedule 2, items 76 and 77, section 6ZZZH of the Insurance Act]

APRA requiring assistance from a statutory manager

8.75 The Bill adds administrators appointed to take control of a general insurer's business to the list of individuals that APRA may seek assistance from in the administration of the FCS under the Insurance Act.
[Schedule 2, item 86, paragraph 6ZZZO(d) of the Insurance Act]

Chapter 9

Wind-up and other matters

Outline of chapter

9.1 Schedules 1 to 3 to this Bill amend the Industry Acts to enhance the operation and scope of APRA's powers in the context of wind-up and other external administration. The Bill also enhances APRA's powers to impose conditions on, or revoke, a regulated entity's authorisation.

Context of amendments

9.2 APRA's winding up powers under the Industry Acts are an important part of the crisis management toolkit, enabling it to act in situations where a regulated entity is insolvent or about to become insolvent. The ability to initiate the winding up of a regulated entity in a timely manner may assist to prevent further financial deterioration, improve outcomes for depositors and policyholders, and minimise impacts on the financial system more broadly.

9.3 In many cases, proceeding straight to the wind-up of a regulated entity will not be an appropriate way of protecting beneficiaries and minimising impacts on the financial system, even if the entity is or is likely to become insolvent. APRA will usually need to use its other crisis management powers, such as the appointment of a statutory or judicial manager to stabilise the entity's critical operations and facilitate an orderly resolution such as a recapitalisation or transfer. In some cases, with or without use of other powers such as statutory or judicial management, all or part of the failed entity's business could be put into wind-up, with declaration of the FCS as appropriate.

9.4 Although the external administration and winding up provisions in the Industry Acts generally operate satisfactorily, past experience in the application of some of these powers, for example in the general insurance sector, has identified further areas where the regime could be enhanced.

9.5 There are also gaps and a lack of uniformity in APRA's powers in relation to provisional liquidators and certain external administrators, and in the circumstances in which a person applying for the appointment of an external administrator to a regulated entity must provide APRA with notice.

9.6 Making enhancements to address these issues will create a more consistent and effective legislative basis for APRA's involvement in the winding up or other external administration of regulated entities.

9.7 There are also gaps and a lack of consistency between the Industry Acts in relation to APRA's ability to impose conditions on, or to revoke, an entity's authorisation. The Bill makes amendments to ensure that APRA has appropriate powers to impose conditions and revoke authorisations if certain grounds are met.

Summary of new law

- 9.8 Schedules 1 to 3 to this Bill amend the Industry Acts to:
- harmonise the Industry Acts with regard to APRA's involvement in external administration of regulated entities;
 - ensure that APRA's existing powers in the winding up of a regulated entity extend to where a provisional liquidator is appointed;
 - enable APRA to apply for the winding up of an ADI without the ADI having first been placed in statutory management;
 - provide APRA with notice of proposed applications for external administration of regulated entities;
 - ensure that the institution of offence proceedings is no bar to judicial management or winding up of a regulated entity;
 - enhance APRA's ability to impose, vary and revoke conditions of authorisation in certain circumstances; and
 - enable APRA to revoke authorisations on certain additional grounds under the Industry Acts.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>APRA's involvement in external administration</i>	
APRA's powers in the winding up of a regulated entity are extended to where a provisional liquidator is appointed.	It is uncertain that APRA has standing to apply to the Court in relation to the exercise of a provisional liquidator's powers in the same way that APRA has power to do so in relation to a liquidator in a substantive winding up.

<i>New law</i>	<i>Current law</i>
<p>Under each of the Industry Acts:</p> <ul style="list-style-type: none"> • APRA may apply to the Court for directions regarding any matter arising under the winding up (or proposed winding up, where a provisional liquidator has been appointed) of a regulated entity; • liquidators (including provisional liquidators) are required to notify APRA in writing prior to making an application to the Court in relation to a winding up matter; and • APRA may request information from a liquidator (including provisional liquidators) regarding the winding up of a regulated entity. 	<p>Under the Insurance and Life Insurance Acts:</p> <ul style="list-style-type: none"> • APRA may apply to the Court for directions regarding any matter arising under the winding up of a regulated entity; • liquidators must notify APRA in writing prior to making an application to the Court in relation to a winding up matter; and • APRA may request information from a liquidator regarding the winding up of a regulated entity. <p>Conversely, under the Banking Act, only the second bullet point above applies.</p>
<p>APRA's involvement in external administration is expanded to capture regulated entities, authorised NOHCS, and subsidiaries of regulated entities or authorised NOHCs.</p>	<p>APRA's involvement in external administration is limited to regulated entities only.</p>
<p><i>APRA's ability to apply for winding up of ADI without it having been placed in statutory management</i></p>	
<p>APRA may apply for the winding up of an ADI <i>without</i> the ADI having first been placed in statutory management on certain grounds.</p>	<p>APRA may apply for the winding up of an ADI <i>only</i> if a statutory manager has first been appointed to the ADI.</p>
<p><i>Providing APRA with notice of proposed applications for external administration of regulated entities</i></p>	
<p>A person applying to the Court, or using any other process (such as appointment under a deed or statutory power), for the appointment of an external administrator to a regulated entity or authorised NOHC, must provide APRA with notice prior to making the application.</p>	<p>A person applying to the Court for the appointment of an external administrator to an ADI or insurer must provide APRA with notice prior to making the application.</p>

<i>New law</i>	<i>Current law</i>
<i>Institution of offence proceedings no bar to judicial management or winding up</i>	
The institution of offence proceedings is no bar to judicial management under the Insurance and Life Insurance Acts or winding up of a regulated entity.	There is no equivalent provision of subsection 248(2) of the Life Insurance Act in the Banking or Insurance Acts, which provides that the institution of offence proceedings is no bar to the judicial management or winding up of a life company.
<i>Imposing, varying and revoking conditions of authorisation</i>	
<p>Under each of the Industry Acts, APRA may impose, vary and revoke conditions of authorisation.</p> <p>It is an offence to breach a condition of registration under the Life Insurance Act.</p> <p>Uniform penalties (based on section 14 of the Insurance Act) will apply.</p> <p>The general structure of the provisions relating to conditions on authorisation are brought into line with the Insurance Act model.</p>	<p>The provisions in the Industry Acts differ in relation to APRA's ability to impose, vary and revoke conditions of authorisation.</p> <p>Under the Life Insurance Act, it is not an offence if a condition of registration is breached under that Act.</p> <p>The penalty provisions for breach of authorisation differ significantly between the Industry Acts.</p> <p>The structure of the provisions relating to conditions on authorisation varies between the Industry Acts.</p>
<i>Revoking an authorisation</i>	
Under each of the Industry Acts, APRA may revoke the authorisation of a regulated entity in certain circumstances, including certain breaches of laws and prudential requirements.	The Banking and Insurance Acts allow APRA to revoke authorisations in certain circumstances. Equivalent grounds are not included in the Life Insurance Act, under which APRA may only cancel a life company's registration if a life company has ceased to carry on a life insurance business in Australia or if the life company voluntarily requests for its registration to be cancelled.

Detailed explanation of new law

APRA's involvement in external administration

9.9 APRA currently has the power to apply for a winding up order in respect of a regulated entity. In making such an application, it may be necessary for APRA to seek that the Court appoint a provisional liquidator pending the final hearing of the winding up application.⁷

9.10 APRA may seek to appoint a provisional liquidator where there is a need to protect a regulated entity's assets from dissipation during this period and the entity's assets cannot be preserved by appropriate undertakings. For example, this may be the case where there is not already a statutory or judicial manager in place.

9.11 Further, the Industry Acts currently include provisions enabling APRA to be involved in the liquidation of a regulated entity. These include provisions:

- giving APRA power to apply to the Court for directions regarding any matter arising under the winding up of a regulated entity (under the Insurance and Life Insurance Acts);
- requiring a liquidator of a regulated entity to notify APRA in writing before the liquidator makes an application to the Court regarding the winding up of a regulated entity (under the Industry Acts); and
- giving APRA power to request information from a liquidator regarding the winding up of a regulated entity (under the Insurance and the Life Insurance Acts).

9.12 These existing powers reflect the significance of APRA's role in the liquidation of a regulated entity so as to ensure that the interests of depositors and policyholders, and the stability of the financial system, are protected.

⁷ As noted above, the fact that APRA has the ability to seek the appointment of a liquidator or provisional liquidator does not preclude it from exercising its other crisis management powers, including appointing or seeking the appointment of a statutory or judicial manager, in appropriate circumstances, whether or not the entity is insolvent.

Definitions

9.13 The Bill inserts a new definition of ‘liquidator’ into the Industry Acts to make certain that the definition includes a provisional liquidator. The Bill also amends the definition of ‘external administrator’ to remove the reference to ‘provisional liquidator’ as it will be redundant given its inclusion in the definition of ‘liquidator’. *[Schedule 1, items 5 and 7, subsection 5(1) of the Banking Act; Schedule 2, items 2 and 4, subsection 3(1) of the Insurance Act; Schedule 3, items 111 and 113, the Schedule Dictionary of the Life Insurance Act]*

9.14 These amendments provide the mechanism to extend APRA’s powers in external administration to instances where provisional liquidators are appointed, as detailed in the sections below.

9.15 The Bill also extends the application of these powers by using the term ‘entity’, which covers the following:

- a regulated entity;
- an authorised NOHC; or
- a subsidiary of a regulated entity or authorised NOHC.
[Schedule 1, item 243, subsection 62C(4) of the Banking Act; Schedule 2, item 61, subsection 62ZR(4) of the Insurance Act; Schedule 3, item 57, subsection 183(4) of the Life Insurance Act]

Notice of application

9.16 The Industry Acts currently require a liquidator of a regulated entity to notify APRA in writing before they propose to make an application to the Court regarding the winding up of a regulated entity and APRA has the right to be heard in such an application.

9.17 The Bill amends the Industry Acts to insert ‘or the proposed winding-up’ of an entity in a number of provisions. *[Schedule 1, item 242, subsection 62C(1) of the Banking Act; Schedule 2, item 60, subsection 62ZR(1) of the Insurance Act; Schedule 3, items 56 and 58, subsection 183(1) and paragraph 183B(2)(a) of the Life Insurance Act]*

9.18 These amendments, when read with the new definition of ‘liquidator’, ensure that a provisional liquidator must also give APRA written notice if the provisional liquidator proposes to make an application to the court in relation to a matter regarding the entity.

Directions

9.19 APRA currently has the power under the Insurance and Life Insurance Acts to apply to the Court for directions regarding any matter arising under the winding up of an insurer.

9.20 However, there are no equivalent provisions within the Banking Act. The Bill therefore amends the Banking Act to address this inconsistency and harmonise the position across the Industry Acts. *[Schedule 1, item 244, section 62D of the Banking Act]*

9.21 Further, the Bill also amends the Insurance and Life Insurance Acts to extend APRA's ability to apply to the Court for directions regarding the winding up, or proposed winding up, of an entity. *[Schedule 2, item 62, subsection 62ZS(1) of the Insurance Act; Schedule 3, item 59, subsection 184(1) of the Life Insurance Act]*

9.22 These amendments when read with the new definition of 'liquidator', ensure that APRA may apply to the Court for directions when an entity is under the control of either a liquidator or a provisional liquidator.

Information gathering

9.23 APRA currently has the power under the Insurance and Life Insurance Acts to request information from a liquidator of a regulated entity regarding the winding up of a regulated entity.

9.24 However, there are no equivalent provisions within the Banking Act. The Bill therefore amends the Banking Act to address this inconsistency and harmonise the position across the Industry Acts. *[Schedule 1, item 244, section 62E of the Banking Act]*

9.25 Further, the Bill amends the Insurance and Life Insurance Acts to extend APRA's ability to request specific information from a liquidator regarding the winding up, or proposed winding up, and the other affairs of the entity. *[Schedule 2, item 63, subsection 62ZT(1) of the Insurance Act; Schedule 3, item 60, subsection 185(1) of the Life Insurance Act]*

9.26 These amendments when read with the new definition of 'liquidator', ensure that APRA may request information from a liquidator or a provisional liquidator.

APRA's ability to apply for winding up of an ADI without it having been placed in statutory management

9.27 Section 14F of the Banking Act currently empowers APRA to apply to the Court for an ADI, where it is under statutory management, to be wound up where APRA considers that the ADI is insolvent, and cannot be restored to solvency within a reasonable period.

9.28 It will often be desirable for APRA to first appoint a statutory manager before proceeding to a winding up, given that a statutory

manager may assist APRA to assess the ADI's solvency or to take actions required to facilitate the resolution of the ADI's affairs.

9.29 However, where APRA has already formed the view that the ADI is insolvent, having to appoint a statutory manager first before applying for a winding up order may not always be the optimal course of action, particularly where APRA is satisfied that the entity can be wound-up without other resolution actions being required. The approach taken by APRA will depend on an assessment of the circumstances and options for resolution, even if the ADI is insolvent.

9.30 The Bill repeals section 14F and inserts a new provision to provide for APRA to apply for the winding up of a locally-incorporated ADI. This section does not apply to a foreign ADI as, under the Bill, there is a separate section applying to the winding up of a foreign ADI (see 7.43).

9.31 The only ground that must be satisfied before APRA applies for a winding up order is that APRA considers the ADI is insolvent and could not be restored to solvency within a reasonable period. This amendment clarifies APRA's existing power to apply for the winding up of a locally-incorporated ADI, without the ADI first having been placed under statutory management.

9.32 The amendments preserve the existing requirements in subsections 14F(2) and (3) that the winding up of the ADI is to be conducted in accordance with the Corporations Act, and that APRA must inform the Minister as soon as possible if it makes an application for the ADI to be wound up. *[Schedule 1, item 212, subsections 16AAA(4) and 16AAA(5) of the Banking Act]*

9.33 The Bill also clarifies that the application is to be made under existing section 459P of the Corporations Act which provides for certain persons, including APRA, to apply for a company to be wound up in insolvency. *[Schedule 1, item 212, subsection 16AAA(3) of the Banking Act]*

Providing APRA with notice of proposed applications for external administration of regulated entities and authorised NOHCs

9.34 Sections 62ZQ of the Insurance Act and 179C of the Life Insurance Act were amended by the *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Act 2010* to compel a person applying to a Court for the appointment of an external administrator to an insurer to provide APRA with notice of the proposed application. This amendment aligned the Insurance and Life Insurance Acts with existing section 62B of the Banking Act.

9.35 These provisions mean that APRA must be given information about any prospective appointment of an external administrator to a regulated entity before the external administrator is appointed. This allows APRA to understand the circumstances giving rise to the proposed appointment and to take appropriate and timely action, if necessary, to protect the interests of depositors and policyholders, and to promote financial system stability.

9.36 However, there are certain circumstances in which an external administrator may be appointed without an application to the Court, for example, the appointment of a receiver or voluntary administrator via a non-court process under a deed or other instrument.

9.37 The rationale behind the current legislative provisions applies equally whether an external administrator is appointed via the court process or outside the court process.

9.38 The Bill amends the Industry Acts to extend the requirement to capture additional modes of appointment outside of a court. For example, where a receiver is appointed under a contractual power or a voluntary administrator is appointed under a statutory power.

9.39 Accordingly, under the Bill a person must give written notice to APRA, at least one week before they make:

- a court application under Chapter 5 of the Corporations Act for the appointment of an external administrator of a regulated entity or an authorised NOHC; or
- another kind of application (whether or not to a court) for the appointment of an external administrator of a regulated entity or an authorised NOHC; or
- an appointment of an external administrator of a regulated entity or an authorised NOHC (otherwise than as the result of an application made by another person). *[Schedule 1, item 240, subsection 62B(1) of the Banking Act; Schedule 2, item 59, subsection 62ZQ(1) of the Insurance Act; Schedule 3, item 53, subsection 179C(1) of the Life Insurance Act]*

9.40 The requirement to give one week's written notice does not apply if APRA gives the person written notice, before the person makes the application or appointment, that APRA consents to the person making the application or appointment. For example, APRA may consent to the application being commenced immediately, with or without consenting to the actual order sought (APRA might still oppose the application, and would still be entitled to be heard on the application). *[Schedule 1, item 240,*

subsection 62B(1A) of the Banking Act; Schedule 2, item 59, subsection 62ZQ(3) of the Insurance Act; Schedule 3, item 53, subsection 179C(3) of the Life Insurance Act]

9.41 Further, the Bill repeals the requirements in section 62ZQ of the Insurance Act and section 179C of the Life Insurance Act that the person to give APRA a copy of the application and all the documents that will be filed in support of the application. The requirement in the amended provisions will be to provide APRA with written notice of the application or appointment. This must be in approved form, if any, and an approved form may require the provision of relevant information or documents. After receiving notice, APRA will have power to request the person to provide details of the application. *[Schedule 2, item 59, subsection 62ZQ(5) of the Insurance Act; Schedule 3, item 53, subsection 179C(4) of the Life Insurance Act]*

9.42 The Bill applies the existing strict liability offence, punishable by 60 penalty units, to appointment breach of the new provisions. A person will commit an offence if (a) they make a relevant application or appointment of an external administrator, and (b) APRA did not consent to the person making the application without providing the required one week's notice and (c) the person failed to give written notice in the approved form or, if not form has been approved, failed to give written notice. *[Schedule 1, item 241, subsection 62B(4) of the Banking Act; Schedule 2, item 59, subsection 62ZQ(6) of the Insurance Act; Schedule 3, item 53, subsections 179C(6) and 179C(7) of the Life Insurance Act]*

9.43 A strict liability offence is considered appropriate in this instance as failure to comply would undermine the integrity of the regulatory regime. If APRA is not given advance notice of the appointment of an external administrator or receiver, APRA will be unable to take appropriate and timely action, if necessary, to protect the interests of depositors and policyholders, and to promote financial stability.

9.44 It is well within the control of the person to whom the offence applies to notify APRA of the appointment as this person will either be making an application, possibly to a court, to appoint the person or making the appointment directly.

9.45 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*. That is, the maximum penalty is no more than 60 units for an individual and does not include a term of imprisonment.

Institution of offence proceedings no bar to judicial management or winding up

9.46 Existing subsection 248(2) of the Life Insurance Act provides that the institution of proceedings against a company for an offence against that Act or the FSCODA does not prevent the institution of proceedings for the judicial management or the winding-up of the company on a ground that relates to the matter that constitutes the offence. There are no equivalent provisions in the Banking and Insurance Acts.

9.47 The Bill amends the Banking and Insurance Acts to replicate the position in the Life Insurance Act with appropriate modifications.
[Schedule 1, item 249, section 69BA of the Banking Act; Schedule 2, item 138, section 129AA of the Insurance Act]

9.48 These amendments are not intended to imply that administrative proceedings not mentioned in those respective sections, or other court proceedings (including for injunctions or disqualification), are prevented by the institution of proceedings for an offence based on the same matter.

Imposing, varying and revoking conditions of authorisation

9.49 Currently, provisions in the Industry Acts allow APRA to impose, vary and revoke conditions of authorisation, or registration (in the case of the Life Insurance Act).

9.50 However, the provisions in the Banking and Life Insurance Acts are not as clearly set out or comprehensive as those in the Insurance Act. For example, it is not an offence if a condition of registration is breached under the Life Insurance Act.

9.51 Existing section 13 of the Insurance Act provides a comprehensive model for imposing, varying and revoking conditions of authorisation. These provisions allow APRA, at any time and by written notice, to impose conditions, or additional conditions, on an insurer's authorisation. They also enable APRA to vary or revoke conditions imposed on a general insurer's authorisation. Other subsections in section 13 provide for a number of ancillary matters, including that conditions are to have effect despite anything in the prudential standards; allowing APRA to make an authorisation conditional on a parent entity of the general insurer being an authorised NOHC; providing for notice of an action under section 13 to be given to the insurer and published in the Gazette (although noting that a failure to give such notice does not invalidate the action); and confirming that relevant decisions under the section are reviewable.

9.52 Existing section 14 of the Insurance Act provides that an insurer commits a strict liability offence if it does, or fails to do, an act that results in a contravention of a condition of the insurer's authorisation. The maximum penalty for the company is 300 penalty units and for the individual the maximum penalty is 60 penalty units.

9.53 The Bill replicates sections 13 and 14 of the Insurance Act into the Banking and Life Insurance Acts with appropriate modifications to harmonise the position across the Industry Acts. *[Schedule 1, items 13 and 14, subsections 9(4) to 9(6) and sections 9AA and 9AB of the Banking Act; Schedule 3, item 7, sections 22 and 23 of the Life Insurance Act]*

9.54 The Bill inserts strict liability offence provisions in the Banking and Life Insurance Acts. Where a company or individual fails to act, or acts in such a way, as to contravene a condition of an authorisation or registration, as the case may be, the company or individual will be subject to a maximum penalty of 300 penalty units and an individual a maximum of 60 penalty units. *[Schedule 1, item 14, section 9AB of the Banking Act; Schedule 3, item 7, section 23 of the Life Insurance Act]*

9.55 A strict liability offence is considered appropriate in this instance as failure to comply would undermine the integrity of the regulatory regime. The circumstances that justify the imposition of conditions reflect a significant prudential concern. Compliance with conditions of an entity's authorisation or registration is a key element of APRA's prudential supervision of regulated entities and are intended to protect the interests of depositors and policy holders and to ensure the stability of the Australian financial system.

9.56 Given the significance of the potential harm to depositors, policy holders and financial stability if the conditions are not met, establishing fault should not be an element of the offence.

9.57 The penalty for the offence complies with the requirements of the Government's Guide to *Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*. That is, the maximum penalty is no more than 60 units for an individual, 300 units for a company does not include a term of imprisonment.

9.58 Currently, sections 9A of the Banking Act and 15 of the Insurance Act allow APRA to revoke an authorisation for various reasons, including a range of prudential reasons and where the regulated entity has failed to comply with the requirements of the respective Acts.

9.59 There are no equivalent grounds in the Life Insurance Act. Currently APRA only has the power to revoke a life company's registration only if:

- it has ceased to carry on a life insurance business in Australia under section 26 of that Act; or
- it has requested that its registration be cancelled and certain conditions are met.

9.60 The absence of a wider range of grounds in the Life Insurance Act is inconsistent with the other two Industry Acts and potentially ineffective for dealing with the resolution of a life insurer.

9.61 The Bill therefore addresses this anomaly by replicating the provisions of sections 15 and 17 of the Insurance Act in the Life Insurance Act with appropriate modifications. This includes adapting the existing subsections 15(3) to 15(7) of the Insurance Act into the Life Insurance Act, which covers the process by which APRA may revoke the registration of a life insurer, including;

- giving written notice to the life insurer that it is revoking or considering revoking its registration;
- requiring APRA to consider any submissions that the life insurer provides within 90 days of the notice;
- allowing APRA to override the requirement to give notice or consider submissions on the revocation if that is in the public interest; and,
- requiring the notice of revocation to be published in the Gazette (though a failure to do so will not invalidate the revocation)
- providing that revocation of registration is merits reviewable, including in the Administrative Appeals Tribunal [*Schedule 3, item 8, subsections 26(2) to 26(7) of the Life Insurance Act; Schedule 3, item 104, paragraph 236(1)(g) of the Life Insurance Act*]

9.62 The amendments ensure that APRA has the power to revoke a life company's registration if APRA is satisfied that: (1) the company has no liabilities in respect of life insurance business carried on by it in Australia; and (2) one of certain other listed conditions is met such as failure to comply with a regulatory requirement, failure to comply with a Commonwealth law specified in the regulations, insolvency or, in the case of a foreign life insurer, revocation of its authorisation in a foreign country.

Direction to transfer liabilities to facilitate revocation of registration

9.63 As provided for in existing section 17 of the Insurance Act in the same context, a new provision in the Life Insurance Act will provide that, if APRA considers that it would, under section 26, revoke a life company's registration if it had no liabilities, APRA may direct the life company to arrange an assignment of those liabilities to one or more other life companies registered under the Act. *[Schedule 3, items 8 and 11, sections 26 and 27A of the Life Insurance Act]*

9.64 If APRA makes the direction, it is the responsibility of the life insurer who receives the direction to arrange for the transfer. APRA may approve and impose conditions on the transfer having considered a number of relevant factors described in the new provisions. *[Schedule 3, items 9, subsection 27A(4) of the Life Insurance Act]*

9.65 By adapting the existing provisions of section 17 of the Insurance Act into the Life Insurance Act, APRA has the power to direct a life insurer to transfer those liabilities to one or more other life companies registered under the Act. The provisions include the following;

- the direction is to effect despite section 190 of the Life Insurance Act (this is because subsection 190(1) provides that no part of the life insurance business of a life company may be transferred or amalgamated except under a scheme approved by the Court under Part 9. The new provision inserted by the Bill will operate as an exception to this. The business of a life company can also be transferred under the Transfer Act.);
- transferred policies to be treated as though the policies were transferred by novation to the transferee;
- the rights of policy owners against the transferor, and the rights of the transferor against policy owners, are to be treated as though they were transferred by novation to the transferee;
- the assignment of liabilities may include the assignment of rights or benefits in connection with policies in respect of the life insurance business carried on in Australia by the transferor; and
- the direction has effect despite anything in the Insurance Acquisitions and Takeovers Act 1991. *[Schedule 3, item 11, subsections 27A(2), 27A(3), 27A(5), 27A(7) and 27A(8) of the Life Insurance Act]*

9.66 Although the intended purpose of this direction-making power is to address circumstances where a life insurer's registration ought to be revoked despite the fact that it continues to have liabilities, APRA may instead (or, in combination) use any of the other available powers that are appropriate to its resolution objectives (for example, effecting a compulsory transfer of business under the Transfer Act, or appointing a statutory manager to take control of the business of the life insurer).

9.67 These provisions also create a new offence in relation to the direction to assign liabilities in order to facilitate the revocation of a life company registration under the Life Insurance Act. The new offence mirrors equivalent provisions in the Insurance Act. The offence is a strict liability offence and applies where a company or individual fails to act as directed by APRA. *[Schedule 3, item 11, subsections 27A(9) to 27A(11) of the Life Insurance Act]*

9.68 A strict liability offence is considered appropriate because significant delays in revoking a registration to carry on life insurance business in Australia may adversely affect policy holders and financial system stability. The circumstances that would justify the revocation of such a registration are sufficiently serious that a significant criminal deterrent is justified to prevent any such delay, and ought not to depend on whether the life company intended for the delay to occur.

9.69 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*. That is, the maximum penalty is no more than 60 units for an individual, 300 units for a body corporate and does not include a term of imprisonment.

9.70 The Bill also makes consequential amendments to the Life Insurance Act to accommodate the new revocation grounds by adding the following decisions as reviewable decisions under section 236:

- a decision to revoke registration under subsection 26(1);
- a refusal to revoke the registration of a company under section 27;
- a decision to give a direction to assign liabilities under subsection 27A(1);
- a refusal to approve a proposed assignment under subsection 27A(4); and

- a decision to impose conditions on an approval under subsection 27A(4). *[Schedule 3, item 104, subsection 236(1) of the Life Insurance Act]*

9.71 Separately, the Bill inserts an additional ground into the Industry Acts to allow APRA to revoke the authorisation of a foreign-regulated entity if the entity's authorisation is revoked by a foreign regulator, including its home regulator (see 7.51). This ground for revocation, like the others, is subject to the notice requirements in the existing subsection 9A(3) of the Banking Act, subsection 15(3) of the Insurance Act and the new Life Insurance Act revocation provision (see 9.61). Those processes apply unless APRA determines that national or public interest considerations mean that they should not apply.

9.72 Further, the Bill inserts a supplementary ground into the Banking Act to allow APRA to revoke the authorisation if a body corporate, that is a foreign corporation within the meaning of paragraph 51(xx) of the Constitution, is unlikely to be able to meet its liabilities in Australia and is unlikely to be able to do so within a reasonable period of time. *[Schedule 1, item 16, paragraph 9A(2)(j)(i) of the Banking Act]*

9.73 Finally, the Bill inserts an additional ground into the Industry Acts to allow APRA to revoke the authorisation of a regulated entity if the entity fails to comply with a requirement of a provision of Commonwealth law that is prescribed in regulations for this purpose. *[Schedule 1, item 16, paragraph 9A(2)(b)(iv) of the Banking Act; Schedule 2, item 10, paragraph 15(1)(a)(iii) of the Insurance Act; Schedule 3, item 8, paragraph 26(1)(a)(iii) of the Life Insurance Act]*

9.74 The Government's intended use for this regulation-making power is to prescribe Commonwealth laws which, if a regulated entity was found to be in breach of those prescribed laws, would raise significant prudential concerns about the entity that may warrant the revocation of its authority to conduct regulated business. Although regulated entities are expected to comply with all relevant Commonwealth laws, the Government may wish to specify certain laws that are considered particularly important, for example, from the perspective of protecting depositors and policy holders or the stability of the Australian financial system, or on other public interest grounds.

Conditions on a NOHC registration under the Life Insurance Act

9.75 The Bill adapts several of the existing provisions in the Banking and Insurance Acts (as amended by this Bill) relating to conditions on NOHC authorisation and breaches of those conditions into the Life Insurance Act. The purpose of these amendments is to harmonise these provisions across the Industry Acts to the extent that it is appropriate and

beneficial to do so. *[Schedule 3, items 12 to 14, sections 28B and 28BA of the Life Insurance Act]*

9.76 These amendments provide that any conditions on the registration of NOHC under the Life Insurance Act must relate to prudential matters. This change is a safeguard on the use of APRA's powers to impose conditions on NOHC registration, and aligns with what is currently the case in the equivalent provisions of the Banking and Insurance Acts. *[Schedule 3, item 12, subsection 28B(1) of the Life Insurance Act]*

9.77 The amendments also provide that, if APRA imposes, varies or revokes the conditions on a NOHC registration, APRA must give written notice to the registered NOHC and ensure that the notice that this action has been taken is published in the Gazette. In doing so, the amendments do not change the existing provisions with respect to notice to the registered NOHC, and align with what is currently the case in the equivalent provisions of the Banking and Insurance Acts. *[Schedule 3, item 13, subsection 28B(3) of the Life Insurance Act]*

9.78 The amendments also create new strict liability offence provisions in the Life Insurance Act regarding the breach of conditions on a NOHC registration. Where a company or individual fails to act, or acts in such a way, as to contravene a condition of an authorisation or registration, as the case may be, the company or individual will be subject to a maximum penalty of 300 penalty units and an individual a maximum of 60 penalty units. *[Schedule 3, item 14, section 28BA of the Life Insurance Act]*

9.79 As is the case for breaches of conditions on an ADI or insurer's authorisation or registration, this is a strict liability offence. Strict liability is considered appropriate in this instance as failure to comply would undermine the integrity of the regulatory regime. The circumstances that justify the imposition of conditions reflect a significant prudential concern. Compliance with conditions on a NOHC's registration is a key element of APRA's prudential supervision of regulated entities that are subsidiaries of the registered NOHC, and important in order to protect the interests of policy holders and ensure the stability of the Australian financial system.

9.80 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*. That is, the maximum penalty is no more than 60 units for an individual, 300 units for a body corporate and does not include a term of imprisonment

9.81 Finally, the Bill inserts an additional ground into the Life Insurance Act to allow APRA to revoke the authorisation of a registered NOHC if it fails to comply with a requirement of a provision of

Commonwealth law that is prescribed in regulations for this purpose.
[Schedule 3, item 15, paragraph 28C(1)(a)(iia) of the Life Insurance Act]

9.82 This power is equivalent to the new regulations-making power described at 9.73 to 9.74, and its purpose is substantially the same.

Consequential amendments

9.83 Consequential amendments are made to the Banking and Insurance Acts to remove certain existing references to ‘a provisional liquidator’ in light of the new definition of ‘liquidator’. *[Schedule 1, items 219, 220, 225 and 226, paragraph 16AK(1)(c), subsections 16AJ(9)16AL(5) and 16AL(7) of the Banking Act; Schedule 2, item 85, 87, 92 and 93, paragraphs 6ZZO(b) and 6ZZP(1)(b), and subsections 6ZZQ(5) and 6ZZQ(7) of the Insurance Act]*

9.84 The Bill also makes consequential amendments to the Banking Act to update references to the new section 16AAA which gives APRA power to wind up an ADI that is incorporated in Australia (in place of the existing section 14F). *[Schedule 1, items 12, 215 and 216, subsections 5(6), 16AD(1) and 16AD(2) of the Banking Act]*

9.85 In order to minimise ambiguity and use consistent terms throughout the Industry Acts, minor changes have been implemented to harmonise the use of key terms;

- replaced ‘cancel’ with ‘revoke’ regarding the revocation of registration under the Life Insurance Act; *[Schedule 3, items 9, 10 and 16, subsections 27(1) and 27(2), and section 28 of the Life Insurance Act]*

NOHC authorisations and registrations

9.86 The Bill makes changes to the legislative provisions relating to NOHC authorisations and registrations, as well as conditions on those authorisations and registrations.

9.87 Existing section 11AA of the Banking Act serves three functions. First, it gives APRA power to grant a NOHC authority. Secondly, it gives APRA power to impose conditions on such an authority. Thirdly it sets out the consequences of a breach of such a condition. The amendments separate these provisions into three sections. Section 11AA will continue to give APRA power to authorise a NOHC. imposing new section will contain APRA’s power to impose conditions on a NOHC authority. A third section establishes the consequences for a NOHC breaching these conditions. *[Schedule 1, items 17 and 18, sections 11AA, 11AAA and 11AAB of the Banking Act]*

9.88 Existing section 11AA provides for a fault liability offence punishable by a penalty of up to 200 penalty units for a breach of a NOHC authorisation condition. The new penalty provision will provide for a penalty of up to 60 penalty units for an individual and 300 penalty units for a body corporate. It will apply on a strict liability basis. The quantum of the penalty and the strict liability basis of the offence is consistent with other provisions in the Industry Acts (as amended by this Bill) relating to breaches of licence conditions. [*Schedule 1, item 18, section 11AAB of the Banking Act*]

9.89 Strict liability is considered appropriate as failure to comply would undermine the integrity of the regulatory regime. The circumstances that justify the imposition of conditions reflect a significant prudential concern. Compliance with conditions on NOHC authorisation is a key element of the prudential framework for protecting the interests of depositors and the stability of the Australian financial system.

9.90 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers*. That is, the maximum penalty is no more than 60 units for an individual, 300 units for a body corporate and does not include a term of imprisonment.

9.91 The Bill does not replicate existing subsection 11AA(5B) of the Banking Act which provides that a NOHC that commits an offence under subsection 11AA(5) commits that offence on every day during which the conditions of its authority have been breached. This change has been introduced because the repealed section duplicates the effect of section 4K of the *Crimes Act 1914* with respect to the offence in subsection 11AA(5).

Winding up a life insurer

9.92 Existing subsection 181(2) of the Life Insurance Act provides that APRA may only make an application to wind up a life company if, having regard to the conclusions reached by APRA as a result of an investigation under existing Division 3 of Part 7, APRA is satisfied that it is necessary or proper that the application be made. The Bill amends this provision so that APRA can also make an application if satisfied that it is necessary or proper to do so having regard to what APRA has found out as a result of any statutory management of the life company. This will be relevant where, for example, an administrator recommends that APRA make that application, if it is considering whether it is necessary or proper to apply to wind up a life insurer. This is a consequential change as a result of creating a statutory management regime in the Life Insurance Act. [*Schedule 3, item 54, subsection 181(2) of the Life Insurance Act*]

Application and transitional provisions

9.93 A condition in effect under subsection 9(4) of the old Banking Act is taken to be in effect on and after the commencement time under section 9AA of the new Banking Act. A condition in effect under subsection 22(1) of the old Life Insurance Act is taken to be in effect on and after the commencement time under section 22 of the new Life Insurance Act. To avoid doubt, this does not prevent the variation or revocation of a condition on or after the commencement time. *[Schedule 1, item 256 Saving – conditions on section 9 authority; Schedule 3, item 121 Saving – conditions on registration under section 21]*

9.94 The amendments made by the Bill in relation to conditions on an authority or registration apply to the imposition of new conditions on a body corporate's authority under section 9 of the Banking Act or registration under section 21 of the Life Insurance Act on or after the commencement time. The amendments apply to the variation or revocation of conditions on a body corporate's authority under section 9 of the Banking Act or registration under section 21 of the Life Insurance Act on or after the commencement time, even if the conditions were imposed before the commencement time. The amendments also apply to the doing of an act on or after the commencement time, or the failure to do an act on or after the commencement time, resulting in a contravention of such a condition. *[Schedule 1, item 257 Application – conditions on section 9 authority; Schedule 3, item 122 Application – conditions on registration under section 21]*

9.95 A condition in effect under subsection 11AA(3) of the old Banking Act is taken to be in effect on and after the commencement time under section 11AAA of the new Banking Act. A condition in effect under subsection 28B(1) of the old Life Insurance Act is taken to be in effect on and after the commencement time under section 28B of the new Life Insurance Act. To avoid doubt, this does not prevent the variation or revocation of a condition on or after the commencement time. *[Schedule 1, item 259 Saving – conditions on NOHC authority; Schedule 3, item 124 Saving – conditions on NOHC registration]*

9.96 The amendments made by the Bill in relation to conditions on a NOHC authority or NOHC registration apply to the imposition of new conditions on a body corporate's NOHC authority under the Banking Act or NOHC registration under the Life Insurance Act on or after the commencement time. The amendments apply to the variation or revocation of conditions on a body corporate's NOHC authority under the Banking Act or NOHC registration under the Life Insurance Act on or after the commencement time, even if the conditions were imposed before the commencement time. The amendments also apply to the doing of an act on or after the commencement time, or the failure to do an act on or after the commencement time, resulting in a contravention of such a

condition. *[Schedule 1, item 260 Application – conditions on NOHC authority; Schedule 3, item 125 Application – conditions on NOHC registration]*

9.97 As explained above at 9.49 to 9.53 and 9.75 to 9.82, the provisions of the Bill create new offences and amend existing offences in relation to conditions on a regulated entity's authorisation or registration to conduct regulated business and in relation to conditions on a NOHC authority or NOHC registration. As a matter of natural justice, the imposition of strict liability for these offences is intended only to apply in respect of offences committed after the commencement time.

9.98 The provisions of the Bill that amend APRA's powers to revoke an authority or registration apply to an authorisation under section 9 of the Banking Act or section 12 of the Insurance Act, or a registration under section 21 of the Life Insurance Act, whether the authority or registration was granted or made before, on or after the commencement time. The amendments apply in relation to a matter mentioned in a paragraph of subsection 9A(2) of the new Banking Act, subsection 15(1) of the new Insurance Act or subsection 26(1) of the new Life Insurance Act that occurs on or after the commencement time (including such a matter that starts before the commencement time and continues on or after the commencement time). *[Schedule 1, item 258 Application – revocation of section 9 authority; Schedule 2, item 142 Application – revocation of authorisation under section 12; Schedule 3, item 123 Application – revocation of registration under section 21]*

9.99 The provisions of the Bill that amend APRA's powers to revoke a NOHC authority or registration apply to a body corporate's NOHC authority or registration under the Banking Act, the Insurance Act or Life Insurance Act, whether the authority or registration was granted or made before, on or after the commencement time. The amendments apply in relation to a matter mentioned in a paragraph of subsection 11AB(2) of the new Banking Act, subsection 21(1) of the new Insurance Act or subsection 28C(1) of the new Life Insurance Act that occurs on or after the commencement time (including such a matter that starts before the commencement time and continues on or after the commencement time). *[Schedule 1, item 261 Application – revocation of NOHC authority; Schedule 2, item 143 Application – revocation of NOHC authorisation; Schedule 3, item 126 Application – revocation of NOHC registration]*

9.100 The provisions of the Bill that amend APRA's powers to revoke an authority or registration apply to an authorisation under section 9 of the Banking Act or section 12 of the Insurance Act, or a registration under section 21 of the Life Insurance Act, whether the authority or registration was granted or made before, on or after the commencement time. The amendments apply in relation to a matter mentioned in a paragraph of subsection 9A(2) of the new Banking Act, subsection 15(1) of the new Insurance Act or subsection 26(1) of the new Life Insurance Act that occurs on or after the commencement time (including such a matter that

starts before the commencement time and continues on or after the commencement time). *[Schedule 1, item 258 Application – revocation of section 9 authority; Schedule 2, item 142 Application – revocation of authorisation under section 12; Schedule 3, item 123 Application – revocation of registration under section 21]*

9.101 The provisions of the Bill that amend APRA's powers to revoke an regulated entity's authorisation or registration apply to an authorisation under section 9 of the Banking Act or section 12 of the Insurance Act, or a registration under section 21 of the Life Insurance Act, whether the authority or registration was granted or made before, on or after the commencement time to conduct regulated business apply from the commencement of the Bill. The amendments apply in relation to a matter mentioned in a paragraph of subsection 9A(2) of the new Banking Act, subsection 15(1) of the new Insurance Act or subsection 26(1) of the new Life Insurance Act that occurs on or after the commencement time (including such a matter that starts before the commencement time and continues on or after the commencement time). APRA may not revoke an authorisation as a result of a matter that is grounds for revocation under the new provisions if that matter occurred before the commencement of the Bill, unless that matter continues on or after commencement. *[Schedule 1, item 258 Application – revocation of section 9 authority; Schedule 2, item 142 Application – revocation of authorisation under section 12; Schedule 3, item 123 Application – revocation of registration under section 21]*

9.102 A minor amendment has been made to subsection 254(5) of the Life Insurance Act as a result of changes to the provisions that allow APRA to revoke the registration of a life insurer. Section 254 of the Life Insurance Act is a transitional section that makes provisions for life insurers that were registered under a previous version of that Act. The subsection has been amended to ensure that an existing reference in that section to section 26 of the Life Insurance Act remains correct. *[Schedule 3, item 109, subsection 254(5) of the Life Insurance Act]*

Chapter 10

Resolution planning

Outline of chapter

10.1 Schedules 1 to 3 to this Bill amends the Industry Acts to clarify and strengthen APRA's powers in relation to resolution planning.

Context of amendments

10.2 It is important that APRA has the powers it needs, not only to implement an orderly resolution of a failed regulated entity, but to set appropriate prudential requirements for resolution planning and addressing potential barriers to resolution, in advance of any crisis occurring.

10.3 An important lesson from the global financial crisis was that effective resolution requires an advanced level of preparedness through contingency planning, before a failure or crisis event materialises. This has been reflected in the increased international focus on recovery and resolution planning, including in the Key Attributes which provide that authorities should have, at their disposal, a broad range of resolution powers, and to put in place an ongoing process for recovery and resolution planning. Both the BCBS and IAIS have also taken steps to incorporate requirements for recovery and resolution planning into their core principles for supervision.

10.4 APRA's supervision of regulated entities includes working with them to ensure that viable contingency plans are in place for managing a crisis affecting the entity, and to address potential impediments to such plans where necessary. To support amendments in the Bill, APRA will further develop its framework for resolution planning, including where appropriate reflecting this in its prudential framework through standards and guidance, following appropriate consultation.

10.5 In a cross-border context, resolution planning will include working with authorities in other jurisdictions to enable resolution actions to be taken in a coordinated manner where appropriate. This will include consideration of how the application of powers by APRA might be supported by, or itself support, the application of similar powers by other authorities in other jurisdictions. Without this, there is a risk that APRA's resolution powers and other related provisions in the Bill (such as those

relating to immunity and confidentiality in Chapter 3 or the stay provisions referred to in Chapter 6) may have reduced effectiveness in a cross-border context or may conflict with the actions or requirements of authorities in other jurisdictions. Such cross-border coordination is consistent with APRA's current approach of working closely with supervisors in other jurisdictions where relevant.

10.6 The amendments in the Bill clarify the legislative framework for resolution planning, in particular to ensure APRA has clear powers to make and enforce prudential standards on resolution.

10.7 Under the Industry Acts, the term 'prudential matters' is important in determining the scope of the prudential standard-making powers of APRA and the matters for which regulations may be made. However, this term is currently defined differently between the Banking and Insurance Acts, and the Life Insurance Act does not contain a definition (meaning it is not completely clear which matters APRA may make prudential standards on). None of the Industry Acts currently contain any specific reference to resolution, which may lead to uncertainty regarding APRA's ability to make prudential standards relating to a resolution. In addition, although depositor and policyholder protection is a fundamental objective for the prudential supervision of ADIs and insurers, the definition of 'prudential matters' in the Industry Acts does not explicitly reflect this.

10.8 The Bill therefore makes amendments to harmonise the definition of 'prudential matters' across the Industry Acts as applicable, including incorporating a specific reference to resolution and explicitly referring to protecting the interests of depositors or policyholders (as applicable) in each Industry Act.

10.9 The Bill also harmonises the Banking Act and the Life Insurance Act with the Insurance Act by clarifying that entities must comply with prudential standards applicable to them.

10.10 As noted above, resolution planning includes identifying and addressing barriers to resolution which may arise during the planning process. While addressing such issues would be expected to be part of the normal supervisory process between APRA and a regulated entity (with due account given to the relative costs / benefits and other consequences of the potential measures that could be taken), it is important that APRA has the power to enforce its prudential standards or otherwise require actions to facilitate resolution, through directions where necessary (see 3.34 to 3.39 for further details).

10.11 A specific example of a potential barrier to resolution in a group context would be where certain critical parts of a group are found to be

outside the scope of APRA’s resolution powers. While the various powers available to APRA to implement a resolution (as amended by this Bill) apply to a regulated entity, an authorised NOHC and subsidiaries of the regulated entity or authorised NOHC, they do not generally apply to an unauthorised holding company or its subsidiaries (which are not themselves regulated entities or subsidiaries of a regulated entity or authorised NOHC).

10.12 The Bill ensures that APRA is able to address this situation directly by providing it with the power to require a holding company to ensure that a regulated entity has an authorised NOHC where appropriate. In certain circumstances, this may help minimise prudential risks and make it more credible for APRA to use its powers to ensure an orderly resolution of the regulated entity.

Summary of new law

10.13 Schedules 1 to 3 to this Bill amend the Industry Acts to:

- refine and harmonise the definition of ‘prudential matters’(which includes inserting a definition of this term in the Life Insurance Act for the first time);
- clarify which entities must comply with prudential standards; and
- enable APRA to require a holding company to ensure a regulated entity has an authorised NOHC, where appropriate.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<i>Refinement and harmonisation of prudential standards</i>	
The definition of ‘prudential matters’ is harmonised across the Industry Acts, and includes specific reference to facilitating the resolution of a regulated entity and its group in the definition.	‘Prudential matters’ is defined differently between the Banking and Insurance Acts, and contains no explicit reference to resolution. The Life Insurance Act does not contain a definition of ‘Prudential matters’.

<i>New law</i>	<i>Current law</i>
APRA may determine prudential standards in relation to the subsidiaries of ADIs and subsidiaries of authorised NOHCs of ADIs (and particular classes of these subsidiaries).	Unlike the Insurance and Life Insurance Acts, the Banking Act does not explicitly empower APRA to determine prudential standards in relation to the subsidiaries of ADIs and subsidiaries of authorised NOHCs of ADIs (and particular classes of these subsidiaries).
The definition of ‘prudential matters’ in the Industry Acts explicitly refers to protecting the interests of depositors or policyholders.	The definition of ‘prudential matters’ in the Banking and Insurance Acts implicitly includes, but does not explicitly refer to, protecting the interests of depositors or policyholders.
<i>Harmonise provisions creating obligation for entities to comply with prudential standards</i>	
Each of the Industry Acts states that regulated entities, authorised NOHCs, and subsidiaries of regulated entities or authorised NOHCs are obliged to comply with prudential standards made in relation to them.	Unlike the Insurance Act, the Banking and Life Insurance Acts do not state clearly that regulated entities, authorised NOHCs, and subsidiaries of regulated entities or authorised NOHCs are obliged to comply with prudential standards made in relation to them.
<i>Enabling APRA to require a holding company of a regulated entity to ensure the regulated entity has an authorised NOHC</i>	
APRA can require a holding company of a regulated entity to either become an authorised NOHC or to ensure that one of its subsidiaries becomes an authorised NOHC of the regulated entity in accordance with the conditions set by APRA. (APRA will still be able to require, as a condition of initial authorisation or registration of an ADI or insurer, that it be a subsidiary of an authorised NOHC, and be able to impose a condition on an ADI’s or insurer’s authority/registration to this effect.)	APRA can authorise or register a holding company as an authorised NOHC upon their application, but APRA cannot require a holding company that is not authorised, to be authorised. APRA can also require, as a condition of initial authorisation or registration of an ADI or insurer, that it be a subsidiary of an authorised NOHC, and can impose a condition on an ADI or insurer’s authority/registration to this effect.

Detailed explanation of new law

Refinement and harmonisation of prudential standards

Refined and harmonised definition of ‘prudential matters’

10.14 The Bill harmonises the definition of ‘prudential matters’ in the Banking Act and Insurance Act (as applicable), and adds an equivalent definition to the Life Insurance Act, subject to appropriate industry-specific amendments. [*Schedule 1, item 8, subsection 5(1) of the Banking Act; Schedule 2, item 5, subsection 3(1) of the Insurance Act; Schedule 3, item 113, Schedule Dictionary of the Life Insurance Act*]

10.15 The Bill also harmonises the Insurance and Life Insurance Acts with the existing position under the Banking Act by referring in the new definitions of ‘prudential matters’ to a ‘group of bodies corporate’ (as well as to the regulated entity, its authorised NOHC and subsidiaries). Given that prudential matters may relate to groups as a whole, as well as to the regulated entity, its authorised NOHC and subsidiaries, it is important that the definition of ‘prudential matters’ refers to ‘relevant group(s) of bodies corporate’ under all the Industry Acts.

10.16 The Bill further amends the definition of ‘prudential matters’ to clarify that it refers to not just the ‘conduct’ of a regulated entity and its group, but to the ‘structure or organisation’ of a regulated entity and its group. This would include how a regulated entity, its group or members of the group are structured in a legal ownership sense or organised from a business or operational perspective.

10.17 The Bill further amends the definition of ‘prudential matters’ to clarify that it includes matters that facilitate the resolution of the regulated entity and its group. This amendment clarifies that APRA can make prudential standards that relate to planning for resolution, and addressing barriers to resolution whether during normal times or in a time of emerging stress. For this purpose, the Bill inserts a new definition of ‘resolution’ into the Industry Acts. This definition refers to the process by which APRA and other relevant persons – which includes, for example the agencies in the CFR, other State/Territory or Commonwealth agencies, and foreign regulators – may manage or respond to an entity: being, or being considered likely to be or to become unable to meet its obligations; or suspending or being considered likely to suspend payment. This includes managing or responding through the exercise of functions and powers under the relevant Industry Act, or a State/Territory or Commonwealth law or the law in a foreign jurisdiction. This would include any actions by APRA and other relevant persons to manage or respond to such a situation in order to achieve an orderly resolution, including in APRA’s case the use of any of its powers and its role in

administering the FCS. *[Schedule 1, item 10, subsection 5(1) of the Banking Act; Schedule 2, item 7, subsection 3(1) of the Insurance Act; Schedule 3, item 117, Schedule Dictionary of the Life Insurance Act]*

10.18 The references to being considered likely to be or to become unable to meet obligations or being considered likely to suspend payment in the definition of resolution are intended to refer broadly to situations in which the on-going viability of an entity is in jeopardy, which may be prior to the point at which the entity is insolvent as normally defined. This reflects that to achieve an orderly resolution of a distressed entity, it may be necessary for APRA and other relevant persons to intervene as early as possible, and before insolvency. *[Schedule 1, item 10, subsection 5(1) of the Banking Act; Schedule 2, item 7, subsection 3(1) of the Insurance Act; Schedule 3, item 117, Schedule Dictionary of the Life Insurance Act]*

Harmonise provisions creating obligation for entities to comply with prudential standards

10.19 The Bill amends the Banking Act to enable APRA to determine prudential standards in relation to prudential matters to be complied with by the subsidiaries of ADIs, and subsidiaries of authorised NOHCs (and particular classes of ADIs, authorised NOHCs, or subsidiaries of ADIs or authorised NOHCs). *[Schedule 1, items 23, 24, 27, 28 and 30, sections 11AF and 11A of the Banking Act]*

10.20 The Bill also amends the Insurance Act and Life Insurance Act to clarify explicitly that APRA can require a subsidiary of an insurer or of an authorised NOHC (and particular classes of the subsidiaries) (Subsidiary A) to ensure that its subsidiaries, or Subsidiary A and its subsidiaries, satisfy the particular requirements in relation to prudential matters. Corresponding amendments are also made to the Banking Act. These amendments harmonise the Industry Acts. *[Schedule 1, items 25 and 26, subsection 11AF(1AA) of the Banking Act; Schedule 2, items 15 and 16, subsection 32(3) of the Insurance Act; Schedule 3, item 62, subsection, 230A(3A) of the Life Insurance Act]*

10.21 The Bill inserts provisions corresponding to section 35 of the Insurance Act (obligation to comply with prudential standards) in the Banking Act and Life Insurance Act. This clarifies that an ADI, life company, authorised NOHC, or subsidiaries of the ADI or life company or authorised NOHC must comply with the prudential standards applying to them. This amendment harmonises the Industry Acts and is for clarification purposes. It is not intended to substantively change the impact or consequences of an entity failing to comply with a prudential standard that is applicable to it. *[Schedule 1, item 29, section 11AG of the Banking Act; Schedule 3, item 63, section 230AAA of the Life Insurance Act.]*

10.22 Failure to comply with a prudential standard may result in certain consequences under the respective Industry Acts, including the following (existing) consequences:

- *Banking Act*: APRA giving a direction under section 11CA, or the Federal Court granting an injunction under section 65A. In the case of an ADI, such a failure may result in APRA revoking its section 9 authority under subsection 9A(2). In the case of an authorised NOHC, such a failure may result in APRA revoking its NOHC authority under subsection 11AB(2).
- *Insurance Act*: APRA giving a direction under section 104, or the Federal Court making an order for judicial management under Part VB or granting an injunction under section 129D. In the case of a general insurer, such a failure may result in APRA revoking the section 12 authorisation under subsection 15(1). In the case of an authorised NOHC, such a failure may result in APRA revoking its NOHC authorisation under subsection 21(1).
- *Life Insurance Act*: APRA giving a direction under section 230B, or the Federal Court making an order for judicial management under Part 8 or granting an injunction under section 235. In the case of a life company, such a failure may result in APRA revoking its registration under section 26. In the case of an authorised NOHC, such a failure may result in APRA revoking its NOHC registration under subsection 28C(1).

Enabling APRA to require a holding company of a regulated entity to ensure the regulated entity has an authorised NOHC

10.23 The Bill amends the Industry Acts to enable APRA to give a notice to a body corporate that is a holding company of a regulated entity, to require it to ensure, in accordance with the conditions (if any) specified by APRA in the notice, either of the following occurs:

- the body corporate becomes an authorised NOHC of the regulated entity, or
- one of its subsidiaries becomes an authorised NOHC of the regulated entity.

10.24 The notice may deal with the time by which, or period during which, it is to be complied with. APRA may vary the notice if APRA

considers that necessary or appropriate, or revoke the notice if APRA considers that the notice is no longer necessary or appropriate. *[Schedule 1, item 21, section 11AE of the Banking Act; Schedule 2, item 14, section 23A of the Insurance Act; Schedule 3, item 17, section 28AA of the Life Insurance Act]*

10.25 The decision by APRA to give such a notice is reviewable internally and upon application to the Administrative Appeals Tribunal if the person disagrees with the internal review outcome. *[Schedule 1, item 21, subsection 11AE(7); Schedule 2, item 14, subsection 23A(7) of the Insurance Act; Schedule 3, item 105, paragraph 236(1)(gf) of the Life Insurance Act]*

10.26 The amendments in the Industry Acts provide that, in accordance with any conditions set out by APRA, the body corporate has power to comply with APRA's notice despite anything in its constitution or any contract or arrangement to which it is a party. The existing Part 4A of the Transfer Act already provides for a mechanism that may be used to comply with such a notice given by APRA. *[Schedule 1, item 21, subsection 11AE(4) of the Banking Act; Schedule 2, item 14, subsection 23A(4) of the Insurance Act; Schedule 3, item 17, subsection 28AA(4) of the Life Insurance Act]*

10.27 Part 4A of the Transfer Act was enacted in 2007 to address certain identified impediments to the adoption of a NOHC structure by financial groups. The enactment of Part 4A removes these impediments arising under particular requirements of the Corporations Act. When Part 4A was enacted in 2007, related amendments were also made to the *Income Tax Assessment Act 1997*.

10.28 Failing to comply with APRA's notice would attract the application of the existing sections 11CG of the Banking Act, 108 of the Insurance Act and 230F of the Life Insurance Act, which set out the consequences of non-compliance with a direction (an offence with a maximum penalty of 50 penalty units). However, these non-compliance sections do not apply if the contravention of a requirement in an APRA notice happens merely because APRA refuses to grant the body corporate (or its subsidiary) an authority to become an authorised NOHC, and APRA's reasons for that refusal do not include the reason that one or more conditions specified in the notice are not satisfied. *[Schedule 1, item 21, subsections 11AE(8) and 11AE (9) of the Banking Act; Schedule 2, item 14, subsections 23A(8) and 23A (9) of the Insurance Act; Schedule 3, item 17, subsections 28AA(7) and 28AA(8) of the Life Insurance Act]*

10.29 The severance clauses in the Industry Acts are amended for the purposes of the NOHC notice provisions. These provisions are intended to create a constitutional safety net for the avoidance of doubt by providing that each Act has effect as if references to a holding company of an ADI or insurer (as the case may be) has effect as if it were limited to a holding company that is a corporation to which paragraph 51(xx) of the

Constitution applies or a holding company that carries on banking business. *[Schedule 1, item 250, subsection 69F(4A) of the Banking Act; Schedule 2, item 136, subsection 127(5) of the Insurance Act; Schedule 3, item 1, subsection 4(4) of the Life Insurance Act]*

Consequential amendments

10.30 The Bill amends the Banking Act to enable APRA to determine prudential standards in relation to prudential matters to be complied with by the subsidiaries of ADIs, and subsidiaries of authorised NOHCs (and particular classes of ADIs, authorised NOHCs, or subsidiaries of ADIs or authorised NOHCs). As a result, the Bill amends the Banking Act to explicitly state that prudential standards may impose different requirements to be complied with by different classes of ADIs, authorised NOHCs or subsidiaries of ADIs or authorised NOHCs, in different situations or in respect of different activities. This harmonises the Banking Act with the Insurance Act and Life Insurance Act. *[Schedule 1, items 23 and 24, subsections 11AF(1) and 11AF(1A) of the Banking Act]*

10.31 The Bill amends the Banking Act to enable APRA to determine prudential standards to be complied with by, and to issue directions to, the subsidiaries of ADIs and subsidiaries of authorised NOHCs. As a result the Bill makes consequential amendments to the provisions of the Banking Act relating to Auditors of ADIs and authorised NOHCs and their subsidiaries to incorporate appropriate reference to subsidiaries to whom prudential standards may apply and to subsidiaries to which a direction is given. *[Schedule 1, items 228 and 229, sections 16AV and 16BA of the Banking Act]*

10.32 To be consistent with the existing section 35 of the Insurance Act, the Bill amends the Life Insurance Act by adding an obligation to comply with prudential standards. The existing section 7A of the Life Insurance Act sets out that APRA may determine that certain provisions of the Life Insurance Act do not apply to a person while the determination is in force. To be consistent with the existing section 7 of the Insurance Act, the new section 230AAA is added to the list of provisions that APRA may determine to not apply to a person while the determination is in force. *[Schedule 3, item 3, paragraph 7A(1)(j) of the Life Insurance Act]*

Application and transitional provisions

10.33 For the avoidance of doubt, the amendments made by Schedule 1 of the Bill will not affect the validity of a prudential standard made under section 11AF of the Banking Act in force immediately before the Bill receives Royal Assent. *[Schedule 1, items 253 and item 255 Continuation of prudential standards]*

10.34 For the avoidance of doubt, the amendments made by Schedule 2 of the Bill will not affect the validity of a prudential standard made under section 32 of the Insurance Act in force immediately before the Bill receives Royal Assent. *[Schedule 2, items 139 and item 141 Continuation of prudential standards]*

10.35 For the avoidance of doubt, the amendments made by Schedule 3 of the Bill will not affect the validity of a prudential standard made under section 230A of the Life Insurance Act in force immediately before the Bill receives Royal Assent. *[Schedule 3, items 118 and 120 Continuation of prudential standards]*

Chapter 11

Regulation impact statement

11.1 On 20 October 2015, as part of its response to the Financial System Inquiry (Murray Inquiry), the Government agreed with the recommendation that regulatory settings should provide regulators with clear powers in the event a prudentially regulated financial entity fails.

11.2 In line with this response, the Government has developed a streamlined package of reforms to the existing crisis management toolkit which provide the Australian Prudential Regulation Authority (APRA) with an enhanced suite of crisis management powers applicable to prudentially regulated authorised deposit-taking institutions (ADIs), general insurers and life insurance companies (insurers), and certain group entities.

11.3 As part of this process, the Government was informed of the regulatory impacts of various reform options by the findings of three papers as well as through extensive consultations with industry stakeholders. The papers relied upon are:

- The Murray Inquiry Final Report;
- The 2012 consultation paper ‘Strengthening APRA’s Crisis Management Powers’ (Crisis Management Consultation Paper); and
- The 2011 consultation paper ‘Financial Claims Scheme’ (FCS Consultation Paper).

11.4 These papers examine gaps in the existing regulatory crisis management toolkit and other regulatory frameworks relevant to the resolution of a distressed entity, and make recommendations to address these gaps. The package of reforms is based on proposals in the Crisis Management Consultation Paper.

11.5 Treasury has certified that the papers and consultations constitute a process and analysis equivalent to a Regulation Impact Statement (RIS).

11.6 The Australian government Guide to Regulation identifies seven questions that a RIS should address. Following is a summary of the analysis of these questions that occurred as part of the independent reviews and stakeholder consultation process.

The problem and why government action is needed

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

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

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

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

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

Policy options, and the costs and benefits of each option

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

- Strengthening regulators' resolution powers for financial institutions: While many of the gaps identified are relatively minor in isolation, the cumulative effect of addressing them in full would enhance APRA's crisis management powers and more closely align Australia with international standards

and best practice. It was noted that many of the proposed powers would have limited regulatory burden in normal times.

- Investing more in pre-planning and pre-positioning for financial failure: Pre-planning is necessary to support viable crisis management options and increase the consistency of Government approaches to crises. It was noted that pre-planning could be resource intensive for regulators and impose a burden on industry, but compared to other options, would likely be relatively low cost.
- No change to current arrangements for either or both of the above options: The Murray Inquiry noted that there are high costs associated with the disorderly failure of an institution, particularly where this creates financial system instability or the need for Government support. These costs would be exacerbated should the above policy options not proceed.

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

Consultation

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

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

11.16 Consultation was also undertaken on the Government's 2014 Consultation Paper 'Providing Certainty for Contractual Loss Absorption Provisions in Regulatory Capital' which received 4 submissions from industry.

11.17 Prior to the release of the exposure draft legislation, Treasury conducted targeted consultation with key industry representative bodies and law firms. During this period, Treasury also consulted with a number of financial institutions, including the major four banks. Following the

release of the draft Bill for consultation on 18 August 2017, Treasury continued to engage with key industry stakeholders on the main issues.

Agreed option

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

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

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

- enhance APRA’s statutory and judicial management regimes to ensure their effectiveness in a crisis;
- enhance the scope and efficacy of APRA’s existing directions powers;
- improve APRA’s ability to implement a transfer of business;
- ensure the effective conversion and write-off of capital instruments to which the conversion and write-off provisions in APRA’s prudential standards apply;
- enhance stay provisions and ensure that the exercise of APRA’s powers does not trigger certain rights in the contracts of entities within the same group;

- provide APRA with powers to resolve branches of foreign banks;
- enhance the efficiency and operation of the FCS and ensure that it supports the crisis resolution framework;
- strengthen APRA's ability to wind up an entity and monitor external administration processes; and
- provide APRA with clear resolution planning powers, to ensure banks and insurers are better prepared for a crisis.

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

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

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

Table 1: Regulatory burden estimate (RBE) table

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

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

Implementation and evaluation

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

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

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

Chapter 12

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

Financial Sector Legislation Amendment (Crisis Resolution Powers and Other Measures) Bill 2017

12.1 This Bill is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview

12.2 The Bill amends the *Banking Act 1959* (Banking Act), *Insurance Act 1973* (Insurance Act), *Life Insurance Act 1995* (Life Insurance Act), *Australian Prudential Regulation Authority Act 1998* (APRA Act), *Payment Systems and Netting Act 1998* (PSN Act), *Financial Sector (Business Transfer and Group Restructure) Act 1999* (Transfer Act), *Corporations Act 2001* (Corporations Act) and *Income Tax Assessment Act 1997*.

12.3 For the purposes of this Bill, the Banking Act, Insurance Act and Life Insurance Act are collectively referred to as the Industry Acts.

12.4 The Schedules to this Bill make amendments in relation to crisis resolution to:

- enhance APRA’s statutory and judicial management regimes to ensure their effective operation in a crisis;
- enhance the scope and efficacy of APRA’s existing directions powers;
- improve APRA’s ability to implement a transfer under the Transfer Act;

- ensure the effective conversion and write-off of capital instruments to which the conversion and write-off provisions in APRA's prudential standards apply;
- enhance stay provisions and ensure that the exercise of APRA's powers does not trigger certain rights in the contracts of relevant entities within the same group;
- enhance APRA's ability to respond when an Australian branch of a foreign regulated entity (foreign branch) may be in distress;
- enhance the efficiency and operation of the Financial Claims Scheme and ensure that it supports the crisis resolution framework; and
- enhance and simplify APRA's powers in relation to the wind-up or external administration of regulated entities under the Industry Acts, and other related matters.

12.5 Schedules 1 to 3 to this Bill also make amendments to the Industry Acts to ensure that APRA has clear powers to make appropriate prudential standards on resolution planning and ensure that regulated entities and their groups put in place measures to improve their preparedness for resolution.

Human rights implications

12.6 The Bill engages the following human rights:

- the imposition of strict liability in relation to some criminal offences;
- the right against self-incrimination under article 14(3)(g) of the International Covenant on Civil and Political Rights (ICCPR);
- the right to protection from arbitrary or unlawful interference with privacy under article 17 of the ICCPR; and
- the right to freedom of expression and to seek information under article 19(2) of the ICCPR.

Strict liability offences

12.7 The Bill imposes strict liability for offences relating to:

- a failure to comply with a direction by APRA to assign a life insurance business' liabilities to another entity (see paragraphs 9.63 to 9.69 and 12.9 to 12.12);
- a failure to notify APRA where a receiver is appointed under a contractual power or a voluntary administrator is appointed under a statutory power (see paragraphs 9.34 to 9.45 and 12.13 to 12.18); and
- breaches of a condition of authorisation or registration under the Banking and Life Insurance Acts (see paragraphs 9.49 to 9.57 (conditions on regulated entity authorisations), 9.75 to 9.80 (NOHC conditions), 9.86 to 9.91 (NOHC conditions) and 12.19 to 12.24).

12.8 The Bill also extends the application of existing strict liability offences relating to directions given under the Insurance Act and the Life Insurance Act to cover where the direction is given to a subsidiary of an insurer or subsidiary of an authorised NOHC of an insurer (see paragraphs 3.19 to 3.26 for a general discussion of these amendments and 12.25 to 12.28 for consideration of the strict liability offence).

Failures to comply with a direction by APRA

12.9 The Bill amends the Life Insurance Act to allow APRA to direct a life company to arrange an assignment of its liabilities to one or more other life companies registered under the Act (to facilitate APRA's ability to revoke a life company's registration).

12.10 There is a strict liability offence that applies to failures to comply with a direction that is given by APRA. By providing for a strict liability offence, the Bill provides that it will not be necessary for the prosecution to prove fault as part of the offence. This approach is appropriate in this instance as an entity's failure to, or delay in complying with a direction, would undermine the integrity of the regulatory regime and adversely affect policy holders and financial system stability.

12.11 It is appropriate to have strict liability for this offence because there would otherwise be potential for significant delays in APRA's ability to revoke an entity's registration to carry on a life insurance business in Australia which could adversely affect policy holders and financial system stability. The circumstances that would justify the revocation of a registration are so sufficiently serious that a significant criminal deterrent is justified to prevent any delay in compliance with a direction from APRA, and ought not to depend on whether the life company intended for the delay to occur or not.

12.12 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* as:

- the offence is not punishable by imprisonment;
- the maximum penalty is at the maximum allowable for strict liability offences (60 penalty units for individuals and 300 penalty units for companies); and
- the harm to policy holders and financial stability is so significant that fault should not be an element of the offence; and
- an entity subject to a direction should be on notice to guard against the possibility of any contraventions of the direction.

Failures to notify APRA where certain receivers are appointed

12.13 The Bill amends the Industry Acts to require relevant entities to notify APRA when a receiver is appointed under a contractual power or a voluntary administrator is appointed under a statutory power. The provisions extend the existing requirement for entities to notify APRA of proposed applications for the appointment of an external administrator.

12.14 The existing strict liability offences that apply under the Industry Acts to failures to notify APRA about proposed applications for the appointment of an external administrator are extended to also apply in relation to the new provisions requiring disclosure of the appointment of a receiver under a contractual power or a voluntary administrator under a statutory power. A failure to provide the required notification to APRA is punishable by 60 penalty units.

12.15 By providing for a strict liability offence, the Bill provides that it will not be necessary for the prosecution to prove fault as part of the offence. This is appropriate in this instance as a failure to provide notification would undermine the integrity of the regulatory regime.

12.16 If APRA is not given advance notice of the appointment of an external administrator or receiver, APRA will be unable to take appropriate and timely action, if necessary, to protect the interests of depositors and policyholders and to promote financial stability. As such, the imposition of the penalty for contraventions of this notification requirement should not depend on whether the relevant entity intended to appoint the receiver or administrator without notifying APRA.

12.17 Furthermore, requiring fault as a particular element of these offences would undermine deterrence and increase the likelihood of breaches that could impact on policy holders and depositors and financial stability more generally.

12.18 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infraction Notices and Enforcement Powers* as:

- the offence is not punishable by imprisonment;
- the maximum penalty of 60 penalty units is at the maximum allowable for strict liability offences (60 penalty units for individuals and 300 penalty units for companies); and
- the harm to depositors, policy holders and financial stability is so significant that fault should not be an element of the offence; and
- an entity should be on notice to guard against the possibility of appointing a receiver or administrator without notifying APRA.

Breaches of a condition of authorisation or registration

12.19 The Bill amends the Banking and Life Insurance Acts to provide a comprehensive model to allow APRA to impose, vary and revoke a relevant entity's conditions of authorisation or registration. The changes to these provisions replicate the existing effective approach provided for in the Insurance Act with appropriate modifications and they extend to both regulated entities (ADIs and insurers) and authorised NOHCs.

12.20 The amendments to the Banking and Life Insurance Acts provide that a contravention of a condition of authorisation or registration is a strict liability offence with a maximum penalty of 300 penalty units for a company and 60 penalty units for an individual. These offence provisions replicate the existing offence provisions that apply as part of the Insurance Act.

12.21 By making a contravention of a condition of authorisation or registration a strict liability offence, the amendments to the Banking and Life Insurance Acts provide that it will not be necessary for the prosecution to prove fault as part of the offence.

12.22 The imposition of strict liability for these offences is appropriate because the circumstances that would justify APRA's imposition of the conditions would be of significant importance to the protection of an

entity's policy holders and depositors and to financial stability in Australia. Contraventions of the conditions therefore reflect such a significant prudential concern about the risks arising from that regulated entity's operations that the imposition of the criminal penalty should not depend on whether the entity intended to breach the conditions or not.

12.23 Furthermore, requiring fault as a particular element of these offences would undermine deterrence and increase the likelihood of breaches that could impact on policy holders and depositors and financial stability more generally.

12.24 The penalty for the offence complies with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* as:

- the offence is not punishable by imprisonment;
- the maximum penalty is at the maximum allowable for strict liability offences (60 penalty units for individuals and 300 penalty units for companies);
- the harm to depositors, policy holders and financial stability is so significant that fault should not be an element of the offence; and
- an entity subject to a condition should be on notice to guard against the possibility of any contraventions of the condition.

Failures to comply with a direction

12.25 The Bill amends the Industry Acts to extend the power to give directions to cover directions to subsidiaries of authorised NOHCs and regulated entities (see 3.19 to 3.26).

12.26 The existing offence provisions in subsections 108(1) and 108(2) of the Insurance Act and 230F(1) and 230F(2) of the Life Insurance Act currently apply where a general insurer or life insurer (as the case may be) or authorised NOHC fails to comply with a direction, and are strict liability offences with a penalty of 50 penalty units for an individual and 250 penalty units for a corporation. The Bill will amend the direction powers in sections 104 of the Insurance Act and 230B of the Life Insurance Act so that they give APRA power to give a direction to a subsidiary of a regulated entity or NOHC. As a result, the offence provisions are amended so that a subsidiary will commit an offence if it fails to comply with the direction.

12.27 Separate strict liability offence provisions in subsection 108(4) of the Insurance Act and subsection 230F(4) of the Life Insurance Act will also be extended to where a direction is given to a subsidiary of an insurer or authorised NOHC under the amended directions provisions. The existing offences in those subsections apply where a direction is given to an insurer or authorised NOHC and an officer of the entity fails to take reasonable steps to ensure compliance. For the offence to be committed the officer's duties must include ensuring that the company or NOHC complies with the direction, or with a class of directions that includes the direction. This will now extend to officers of relevant subsidiaries that receive a direction under the amendments in the Bill. The penalty for an individual for failure to comply is 50 penalty units.

12.28 The imposition of strict liability for contraventions of directions given by APRA to other entities within a regulated entity's corporate group is necessary because and appropriate because when dealing with complex groups, it is often not sufficient to apply powers to the regulated entity alone. Critical services (such as information technology, financial positions or essential staff) may be located in other group entities and contagion effects can occur within groups. APRA needs to be able to move swiftly to safeguard the critical operation of entities where the need arises. Strong compliance with the directions is necessary to ensure that APRA can effectively resolve entities that enter distress in an orderly fashion.

12.29 Contraventions of these APRA directions could have such significant consequences for financial stability in Australia that the imposition of the criminal penalty should not depend on whether an entity intended to breach the conditions or not.

12.30 Furthermore, requiring fault as a particular element of these offences would undermine deterrence and increase the likelihood of breaches.

12.31 The penalties for these offences comply with the requirements of the *Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* as:

- the offences are not punishable by imprisonment;
- the maximum penalty in each case is below the maximum allowable for strict liability offences (60 penalty units for individuals and 300 penalty units for companies);
- directions are an essential tool for ensuring the prudential safety of insurers and the harm to policy holders and

financial stability is so significant that fault should not be an element of the offence.

Right against self-incrimination under article 14(3)(g) of the ICCPR

12.32 The Bill provides for additional information gathering powers that allow APRA and other statutory managers of an insurer to obtain information from the current and past officers of an insurer and a life company that is under statutory management (see paragraphs 2.159 to 2.161).

12.33 These new information gathering powers replicate the existing powers in the Banking Act that apply in relation to authorised deposit taking institutions and extend them to apply to relevant insurance and life insurance entities.

12.34 The information gathering powers allow APRA and other statutory managers to require current and past officers of insurance and life insurance entities to provide information and documents relating to a relevant entity's affairs if the entity is under statutory management. A failure to provide the requested information or documents is an offence that is punishable with:

- imprisonment of up to 12 months in cases where the information or documents are required by a statutory manager; or
- imprisonment of up to 12 months or 50 penalty units or both where the information or documents are required by APRA.

12.35 The new information gathering provisions engage the right against self-incrimination under article 14(3)(g) of the ICCPR because they provide that an officer (past or current) cannot refuse to provide information or documents on the basis that doing so would incriminate the officer or make the officer liable to a penalty.

12.36 Engaging the right against self-incrimination in this way is necessary and justified as only the key personnel of a relevant entity will have access to information and documents relating to that entity's financial condition. It is essential for APRA or a statutory manager to be able to obtain this information quickly to assist with the management and crisis resolution of an insurance or life insurance entity that is financially distressed.

12.37 By compelling relevant officers to provide the required information and documents, APRA and other statutory managers will be able to maximise their ability to rehabilitate a distressed insurance or life

insurance entity. This will benefit the entity's customers, creditors and other suppliers. In the event of a significant crisis, APRA would also be able to use the information gathering powers to support decision making and prevent contagion in the financial system.

12.38 The Bill balances APRA's need to access information with a person's right against self-incrimination by ensuring that incriminating information or documents provided (and identified as such) cannot be used against a person in criminal proceedings or in proceedings where the person may be liable to a penalty. The protection does not apply in relation to proceedings relating to the falsity of the information or documents provided.

12.39 The amendments therefore effectively ensure that APRA and other statutory managers can access information and documents from relevant officers of insurance and life insurance entities but preserves the officers' rights against self-incrimination by ensuring that the information and documents cannot be used as evidence in criminal proceedings or proceedings where a penalty may be imposed.

12.40 To the extent that criminal and other proceedings can be brought because the information or documents provided are false, this is justified as it is necessary to ensure the accuracy of the material provided to APRA and other statutory managers. Furthermore, any proceedings that are brought would relate to the provision of false information or documents as opposed to proceedings concerning matters the information or documents relate to.

12.41 The new information gathering powers in the Bill are therefore consistent with the right against self-incrimination under article 14(3)(g) of the ICCPR.

Right to the protection against arbitrary or unlawful interference with privacy under article 17 of the ICCPR

12.42 The Bill engages the right to the protection against arbitrary or unlawful interference with privacy under article 17 of the ICCPR as a result of:

- the new information gathering powers outlined above in paragraphs 12.29 to 12.38 of this Statement of Compatibility with Human Rights; and
- the extension of section 42 of the Transfer Act to allow APRA to provide information to a body that receives the shares of another body as part of a compulsory transfer of business.

Information gathering powers

12.43 The information gathering provisions allow for APRA and other statutory managers to obtain information about a relevant entity. While this information must relate to the business of a relevant entity (for example, a distressed insurance entity), it is possible that the information required may include personal information.

12.44 The provision of this information is justified and necessary as it allows APRA and other statutory managers to maximise their ability to rehabilitate a distressed entity. This will benefit the relevant entity's customers, employees, creditors and other suppliers. In the event of a significant crisis, APRA would also be able to use the information obtained to support decision making and prevent contagion in the financial system.

12.45 Where personal information (for example documents relating to an entity's personnel) is provided it would be as part of efforts to rehabilitate a distressed entity. This would be to the benefit of the specific individuals whose personal information is transferred and the general public. The individuals whose information is shared would benefit as the distressed entity would have better prospects for recovery meaning a higher likelihood that jobs would be maintained. There would also be a broader benefit to the general public as a distressed entity would have better prospects of success, reducing possible losses amongst customers, suppliers and other creditors.

Sharing information to support the compulsory transfers of shares

12.46 The amendment to section 42 of the Transfer Act allows APRA to provide information (including personal or confidential commercial information) to the receiving body in connection with the transfer of shares (in addition to the existing power to share information where there is a transfer of business).

12.47 The provision is necessary because under the compulsory transfer provisions a receiving body's board must consent to the transfer. In order to facilitate this it will be necessary and appropriate for APRA to provide information to the receiving body about the business, including confidential information and information relating to staff and executives of the body being transferred. It will also be necessary for APRA to share such information in the process of settling the detail of the transfer, including the schedule of assets and liabilities, and in documentation relating to transferred staff.

Information sharing is consistent with the ICCPR

12.48 The sharing of information under the provisions in the Bill would be subject to express legislative provisions and would therefore be lawful. The information transferred would also still be subject to appropriate protections. The *Privacy Act 1998* would apply to the information as appropriate. Where information is provided to APRA, the existing strong APRA confidentiality provisions would apply and where information is provided to other statutory managers, the statutory manager would be responsible for the relevant entity and as such their access to the information would be no different to the previous manager's access to the information.

12.49 The provisions in the Bill relating to the sharing of information are therefore consistent with the right to the protection against arbitrary or unlawful interference with privacy under article 17 of the ICCPR as they explicitly provide for the lawful sharing of relevant information in appropriate circumstances.

Right to freedom of expression and to seek information under article 19(2) of the ICCPR

12.50 The Bill engages the right to freedom of expression and to seek information under article 19(2) of the ICCPR as a result of new secrecy provisions to be included in the Industry Acts (see 3.78 to 3.106).

12.51 These provisions allow for APRA to indicate in writing that directions it has provided to a relevant banking, insurance or life insurance entity cannot be publically disclosed. APRA can make such secrecy determinations if it believes that disclosure of a direction it has made would have an adverse effect on a relevant entity's deposit or policy holders or if APRA believes that it is necessary to promote financial stability in Australia. A breach of these secrecy provisions could result in imprisonment of two years.

12.52 These secrecy provisions engage article 19(2) of the ICCPR because they prevent individuals from disclosing details about directions given by APRA and also restrict the public's access to information relating to the directions.

12.53 The secrecy powers are intended to resolve crisis situations where APRA will require time to obtain information and take urgent action to prevent significant losses to customers of a distressed entity and ensure that there is no contagion within the financial system. The secrecy powers are necessary and appropriate because they enable APRA to take appropriate steps in a time of crisis to prevent significant public detriment.

12.54 While the secrecy provisions in the Bill do restrict the right to freedom of expression and to seek information under article 19(2) of the ICCPR, this is permitted under article 19(3) as the provisions allow APRA to protect an entity's customers and the public more generally by preventing contagion in the financial system during crisis situations.

12.55 The secrecy provisions have been balanced with exemptions which allow for the disclosure of information in appropriate circumstances. Disclosure is allowed where information subject to a direction is already public or authorised by APRA. There is also an exemption that allows a person affected by a secrecy provision to disclose the information to a legal representative for the purpose of obtaining legal advice. A regulation making power also ensures the Government can create additional exemptions quickly to balance the rights of individuals who may be affected by the secrecy provisions.

12.56 The exemptions to allow disclosure ensure that the secrecy provisions are proportionate by not preventing disclosure where it would be unfair to do so (for example, when seeking legal advice).

12.57 As such, the secrecy provisions in the Bill are consistent with the right to freedom of expression and to seek information under article 19(3) of the ICCPR.

Conclusion

12.58 The Bill is compatible with human rights as:

- the strict liability offences are appropriate and consistent with the requirements of the Government's Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers;
- the information gathering powers are consistent with the right against self-incrimination under article 14(3)(g) of the ICCPR; and
- the information gathering powers are consistent with the right to privacy under article 17 of the ICCPR.

12.59 To the extent that the secrecy provisions in the Bill restrict the right to freedom of expression and to seek information, this is appropriate, justified and consistent with the article 19 of the ICCPR.

