

EXPLANATORY STATEMENT

Banking Act 1959

Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021

The *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Act 2018* amended the *Banking Act 1959* (the Act) to introduce a new regime, the Banking Executive Accountability Regime (BEAR).

The BEAR imposes a heightened accountability regime on authorised deposit-taking institutions (ADIs) and people, known as accountable persons, with significant influence over the conduct and behaviour of an ADI. It requires these people to conduct themselves with honesty and integrity and to effectively carry out the business activities for which they are responsible.

The obligations set out in the BEAR began to apply to large ADIs from 1 July 2018 and to small and medium ADIs from 1 July 2019.

The BEAR requires ADIs to set out remuneration policies which defer a specified proportion of the variable remuneration of accountable persons for a minimum period. This is intended to create an incentive for these individuals to make decisions taking into account the longer term effects. The proportion of an accountable person's remuneration which must be deferred depends on the size of the ADI where the accountable person works.

The BEAR also includes civil penalties where an ADI fails to meet its obligations under the BEAR. The maximum penalty that may be applied by a court is also determined with reference to the size of the ADI.

Subsection 37G(3) of the Act provides the Treasurer with the power to determine by legislative instrument the kinds of ADIs that are large, medium and small.

The *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021* (the Determination) replaces the *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2018*. It sets out the methodology to determine the size of an ADI as small, medium or large, by considering the total assets of the ADI as reported to APRA. The key changes from the previous Determination are to refer to *Reporting Standard ARS 720.0 ABS/RBA Statement of Financial Position* (ARS 720.0), and to rebase the indexation calculations for the higher threshold amount.

The BEAR applies to subsidiaries of ADIs and their accountable persons. A subsidiary of an ADI takes on the size of the ADI and also the rules applying to an ADI in that size category.

The Determination sets out a methodology for determining the size of an ADI based on total assets reported to APRA in earlier financial years.

An ADI will need to monitor its size every financial year to know how the obligations in the BEAR that depend on whether it is small, medium or large, apply to it.

Consultation with two ADIs that are most likely to be affected by this Determination was conducted. The ADIs understood their obligations if their size designation changes under this Determination and expressed no concerns. No full public consultation was conducted because the changes under this Determination are minor in nature, reflecting an updated Reporting Standard already being used by ADIs. This Reporting Standard is ARS 720.0, which has been consulted on as part of APRA's longstanding public consultation on Economic and Financial Statistics.

A detailed explanation of the Determination, including the Schedule, is at Attachment A.

The Statement of Compatibility with Human Rights is set out in Attachment B.

The Act does not specify any conditions that need to be met before the power to make the Determination may be exercised.

The Determination is a legislative instrument for the purposes of the *Legislation Act 2003*.

The Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021

Section 1 – Name

Section 1 provides that the name of the instrument is the *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021* (the Determination).

Section 2 – Commencement

Section 2 provides that the instrument commences on the day after the instrument is registered.

Section 3 – Authority

Section 3 provides that the instrument is made under subsection 37G(3) of the *Banking Act 1959* (the Act).

Section 4 – Schedules

Section 4 provides that the Schedule to the instrument specifies each instrument that is amended or repealed as set out in each applicable item in the Schedule.

Section 5 – Definitions

Section 5 sets out the definitions that are used in the legislative instrument.

A brief explanation and summary of the terms and definitions included in the instrument are set out below. A full explanation of how these terms are used to calculate an ADI's size is clarified as part of the explanations for sections 6 and 7.

final report means a report submitted by an ADI to APRA under Reporting Standard ARS 320.0 Statement of Financial Position (Domestic Books), Reporting Standard ARS 323.0 Statement of Financial Position (Licensed ADI), or Reporting Standard ARS 720.0 ABS/RBA Statement of Financial Position in relation to the final reporting period for the ADI's final reporting period in a financial year.

financial year, in relation to an ADI, means the ADI's financial year (see section 323D of the *Corporations Act 2001*) and includes financial years that begin before the commencement of this instrument. In most circumstances a financial year for an ADI will be a period of 12 consecutive months, with its first financial year commencing on the day the ADI is registered or incorporated.

Reporting Standard refers to a Reporting Standard determined under section 13 of the *Financial Sector (Collection of Data) Act 2001*. Section 8 sets out what happens when a Reporting Standard with a particular identifier is replaced by a Reporting Standard with a different identifier.

total asset size is the amount used to determine the size of an ADI, and includes an average of total assets reported over two or three years. Section 6 describes how this amount is determined.

total resident assets value is the amount of total assets as reported to APRA in a final report. Section 7 describes how this amount is identified.

Section 6 – Size of an ADI

Section 6 introduces the term ‘total asset size’, which is used to determine the size of an ADI. The total asset size is in turn determined by reference to the ‘total resident assets value’ in a final report (explained in section 7), or several final reports an ADI has submitted to APRA.

If an ADI has submitted:

- a final report for only one financial year, its total asset size is the total resident assets value reported in that final report.
- final reports for only two financial years, its total asset size is the average of the total resident assets value reported in those two final reports.
- final reports for three or more financial years, its total asset size is the average of the total resident assets value in the three most recent reports in three financial years.

A **small ADI** is an ADI that has a total asset size less than or equal to \$10 billion, or a new ADI for which it is not yet possible to work out this amount because they have not yet submitted a final report to APRA (for example a new ADI).

A **medium ADI** is an ADI that has a total asset size greater than \$10 billion but less than \$107 billion.

A **large ADI** is an ADI that has a total asset size greater than or equal to \$107 billion.

Each of these monetary amounts is a threshold demarcating size categories. Each amount is indexed in accordance with section 9.

The reason \$107 billion is used as a threshold in this Determination is because under the *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2018*, the ‘upper threshold’ is \$100 billion, subject to the indexation provision in that instrument. The \$100 billion threshold had been indexed on 1 January 2020, raising it to \$107 billion. This Determination retains this new threshold, and makes \$107 billion the new baseline from which indexation in accordance with section 9 is calculated.

The size of an ADI is calculated on the first day of each financial year. The size category will then apply to that ADI for the duration of that financial year. Due to the fact that a final report is lodged in the year following the year to which the report relates, there is a lag between the financial year that a final report covers, and the financial year to which a designation of size based on that final report, and any previous final reports, applies.

[Subsections 6(2) to (5) – Size of an ADI]

Some ADIs have submitted, or currently submit, reports to APRA under Reporting Standard ARS 720.0 and either Reporting Standard ARS 320.0 or Reporting Standard ARS 323.0 in the same financial year.

If an ADI has submitted final reports for a financial year ending on or before 30 June 2019 under both Reporting Standard ARS 720.0 and Reporting Standard ARS 320.0, the total resident assets value reported under Reporting Standard ARS 320.0 is used. If an ADI has submitted final reports for a financial year ending after 30 June 2019 under both Reporting Standard ARS 720.0 and Reporting Standard ARS 323.0, the total resident assets value reported under Reporting Standard 720.0 is used. For ADIs

that only report under Reporting Standard ARS 323.0 after 30 June 2019, the total resident assets value reported under that Reporting Standard is used.

[Subsection 6(6) – Size of an ADI]

The methodology takes into account the fact that an ADI can have its own financial year under the *Corporations Act 2001* (section 323D), and this could differ from the standard financial year. Being able to use its own financial year minimises the regulatory burden on an ADI and ties in with its existing reporting obligations to APRA.

Example 1 – two-year average

It is currently financial year 2020–2021 for an ADI.

This ADI has submitted a final report for financial year 2018–19, and a final report for financial year 2017–18.

In the final report for financial year 2018–19, the total resident assets value reported is \$22 billion, while in the final report for financial year 2017–18, the total resident assets value reported is \$24 billion.

This ADI’s total asset size is \$23 billion, the average of these two amounts:

$$\frac{\$22 \text{ billion} + \$24 \text{ billion}}{2} = \$23 \text{ billion}$$

This ADI is therefore a medium ADI for the duration of financial year 2020–21.

Once this ADI has submitted a final report for financial year 2019–20, it would be able to recalculate its total asset size by taking the average of the three reported amounts for financial years 2019–20, 2018–19 and 2017–18. This average amount will determine the size of this ADI for financial year 2021–22.

Example 2 – three-year average

It is currently financial year 2020–2021 for an ADI.

This ADI has submitted a final report for financial year 2018–19, a final report for financial year 2017–18 and a final report for financial year 2016–17.

In the final report for financial year 2018–19, the total resident assets value reported is \$8 billion, in the final report for financial year 2017–18, the total resident assets value reported is \$9 billion, and in the final report for financial year 2016–17, the total resident assets value reported is \$10 billion.

This ADI’s total asset size is therefore \$9 billion, the average of these three amounts:

$$\frac{\$8 \text{ billion} + \$9 \text{ billion} + \$10 \text{ billion}}{3} = \$9 \text{ billion}$$

This ADI is therefore a small ADI for the duration of financial year 2020–21.

Once this ADI has submitted a final report for financial year 2019–20, it would be able to recalculate its total asset size by taking the average of the three most recently reported amounts from financial years 2019–20, 2018–19 and 2017–18. This average amount will determine the size of this ADI for financial year 2021–22.

Example 3 – new ADI

It is currently financial year 2020–2021 for an ADI.

This ADI has not yet submitted any final reports because it is a newly formed ADI. It is taken to be a small ADI for the duration of financial year 2020–2021.

Section 7 – Total resident assets value

The total resident assets value is the total assets amount in a final report submitted to APRA.

For ADIs that are required to give information using forms under Reporting Standard ARS 720.0:

- For ADIs submitting Form ARF 720.0A, the total resident assets value is worked out by taking the amount reported in Section A, item 13 Total assets including intra-group assets, and then subtracting assets due from non-residents (items 11.1 and 12.1); and
- For ADIs submitting Form ARF 720.0B, the total resident assets value is the amount reported in Section A, item 13 Total assets including intra-group assets.

ADIs are required to use final reports submitted under Reporting Standard ARS 720.0 for financial years ending after 30 June 2019 for the purpose of the calculations. However, for ADIs that are not required to report under Reporting Standard ARS 720.0, the total resident assets value is found in item 11 in Section A: Assets in Form ARF 323.0.

Final reports submitted under Reporting Standard ARS 320.0 continue to be used to calculate the total resident assets value for financial years ending on or before 30 June 2019. The total resident assets value under Reporting Standard ARS 320.0 is found in item 10 in Section A: Assets in ARF Form 320.0. Reporting Standard ARS 320.0 will not be relevant in the future, once the multi-year calculations no longer apply historical data under Reporting Standard ARS 320.0 (see table below).

The following table summarises how and when each type of form should be used:

Form	Total Resident Assets Value	For reference periods ending
ARF 320.0	Section A: Assets: Item 10 Total assets	Before and including 30 June 2019.
ARF 323.0	Section A: Assets: Item 11 Total assets	Before and including 30 June 2019. After 30 June 2019, only if not submitting reports under Reporting Standard ARS 720.0.
ARF 720.0A	Section A: Assets: Item 13 Total assets including intragroup assets, less: <ul style="list-style-type: none"> • item 11.1 Total assets excluding intra-group assets <i>of which</i>: Due from non-residents; and • item 12.1 : Total intra-group assets <i>of which</i>: Due from non- 	After 30 June 2019.

	residents	
ARF 720.0B	Section A: Assets: item 13 Total assets including intragroup assets	After 30 June 2019.

Section 8 – Reporting Standards

Section 8 provides that where a provision of the Determination (sections 5 and 7) refers to a particular kind of Reporting Standard with a specific identifier in relation to an ADI's final reporting period in a financial year, that provision is known as a referring provision. The referring provision is taken to refer to the version of the Reporting Standard with that identifier that applied to that reporting period because of a determination made under section 13 of the *Financial Sector (Collection of Data) Act 2001*. However, if no version of that Reporting Standard applies to the final reporting period in a financial year because it has been replaced by a different Reporting Standard (with a different identifier and included in a different determination), then a reference to the Reporting Standard that has been replaced is taken to be a reference to the new Reporting Standard. A reference to any material in the Reporting Standard that has been replaced, for example, the reporting form, is taken to be a reference to the corresponding material in the applicable version of the new Reporting Standard.

The intention of this section is to 'future proof' this Determination so that if a new Reporting Standard is determined under the *Financial Sector (Collection of Data) Act 2001*, and ADIs are required to report in accordance with that new Reporting Standard, the referring provisions in this Determination operate to refer to the new Reporting Standard.

Section 9 – Indexation of thresholds

Section 9 provides for indexation on 1 January 2022, and each 1 January after that, of each amount referred to in subsections 6(2), (3) and (4).

An amount is indexed by multiplying the amount by an indexation factor and rounding the result down to the nearest multiple of \$1 billion.

The indexation factor is a fraction calculated by dividing the relevant GDP number by the base GDP number.

The relevant GDP number is the first-published annual estimate of the Gross Domestic Product: Current Prices-Original series for the financial year that ends before the 1 January on which indexation occurs. This can be found in the Australian Bureau of Statistics' 5204.0 series at <https://www.abs.gov.au/ausstats/abs@.nsf/mf/5204.0>. For example, if indexation occurs on 1 January 2022, the relevant financial year is the one ending on 30 June 2021. For the purpose of this calculation, any revisions of that estimate is disregarded.

The base GDP number is the annual estimate of the Gross Domestic Product: Current Prices-Original series, where, if the amount being indexed is \$10 billion, refer to the most recently published series for the financial year ending on 30 June 2018.

For any other amount being indexed, refer to the most recently published series for the financial year ending on 30 June 2019. The reason a different base year is selected for amounts other than \$10 billion is because indexation has already occurred under the *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking*

Institution) Determination 2018, which raised the higher threshold of \$100 billion to \$107 billion on 1 January 2020. The \$107 billion threshold did not change on 1 January 2021. The \$10 billion threshold did not change on 1 January 2020 or 1 January 2021. By rebasing the year from which the GDP number is taken, this Determination preserves the indexation that has occurred, while providing for future indexations. 1 January 2021 will be the first time indexation calculations occur under this Determination.

If the indexation factor calculated is less than 1, then the indexation factor is taken to be 1. This means that the threshold amounts do not change.

Schedule 1—Repeals

Item 1 repeals the *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2018*.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021

This Legislative Instrument 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 of the Legislative Instrument

The *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Act 2018* amended the *Banking Act 1959* (the Act) to introduce a new regime, the Banking Executive Accountability Regime (BEAR).

The BEAR imposes a heightened accountability regime on authorised deposit-taking institutions (ADIs) and people, known as accountable persons, with significant influence over the conduct and behaviour of an ADI. It requires these people to conduct themselves with honesty and integrity and to effectively carry out the business activities for which they are responsible.

The BEAR requires ADIs to set out remuneration policies which defer a specified proportion of the variable remuneration of accountable persons for a minimum period. This is intended to create an incentive for these individuals to make decisions taking account of the longer term effects. The proportion of an accountable person's remuneration which must be deferred depends on the size of the ADI where the accountable person works.

The BEAR also includes civil penalties where an ADI fails to meet its obligations under the BEAR. The maximum penalty that may be applied by a court is also determined with reference to the size of the ADI.

Subsection 37G(3) of the Act provides the Treasurer with the power to determine by legislative instrument the kinds of ADIs that are large, medium and small. The *Banking Executive Accountability Regime (Size of an Authorised Deposit-taking Institution) Determination 2021* sets out the methodology for determining the size of an ADI as small, medium or large.

Human rights implications

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.