

W1 Legal Regulation of Banking in Australia

- Generally there are two main types of legal systems: **civil law and common law**.
- Key differences: in common law countries, case law (judge-made law)—is of primary importance, while in civil law systems, codified statutes predominate.
- As Australia inherited its legal system from England, we have a **common law system** which has two main sources of law:
 - Legislation made by parliament;
 - Common law made by judges.

Purpose of Banking Act 1959 (Cth)

Aims: According to the preamble, **the Banking Act's** primary purposes:

- Protect the interests of depositors in ways that are consistent with the continued development of a viable, competitive, and innovative banking industry; and
- Promote financial system stability in Australia.

Means: Banking Act achieves these aims by way of:

- Australian Prudential Regulation Authority's (APRA) prudential supervision and monitoring of banks;
- APRA exercises powers to protect depositors
- Reserve Bank of Australia is authorized to regulate control of interest rates.

Focus of the semester: **Authorized Deposit-taking Institutions (ADI)**

Three types: Banks, Building societies, and Credit unions

Licenses for "Business of Banking"

The Banking Act restricts entry into the market as a “**bank**” must:

- be a body corporate: s 7;
- be an Authorised Deposit-Taking Institution (ADI): s 8;
- receive authorization by Australian Prudential Regulation Authority (APRA) to carry on the ‘**business of banking**’: s 8;
- receive approval from APRA to use the word "Bank" in its corporate name: s 66.
- More details in Week 2.

Australian Credit License (ACL)

To engage in credit activities, one should lodge applications with ASIC for ACL (unless exemptions apply):

- Credit activity: e.g.,
 - providing credit under a credit contract or consumer lease
 - suggesting or assisting with a particular credit contract or consumer lease
- National Consumer Credit Protection Act 2009

Regulators- Compliance and Enforcement

Regulatory Bodies

§ **Treasury:** Treasury is responsible for broad policy & regulation affecting banking/finance.

Six policy groups:

- Fiscal, Macroeconomic, Revenue, Markets and Corporate Services, and Business Strategy
- Funding and policy direction to regulators

Financial System Inquiry

– Campbell Inquiry (1981): deregulation

– Wallis Inquiry (1997): sharpened the current regulatory structure and philosophy by focusing on the type of activities, rather than on the legal nature/type of institutions.

§ **Reserve Bank of Australia (RBA):** control inflation, money currency

§ **Australian Prudential Regulation Authority (APRA):** ensure banks are not taking too much risks

§ **Australian Securities and Investments (ASIC):** administrator enforcing the Corporations Act, market regulator, consumer protection

^**Council of Financial Regulation (CFR), a non-statutory body coordinating these agencies, now chaired by RSB.**

§ Australian Competition and Consumer Commission (ACCC)

§ Australian Transaction Reports and Analysis Centre (ASUTRAC)

§ Office of the Australian Information Commissioner (OAIC)

§ Financial Ombudsman Service

Private regulators

§ Self-regulation (industry)

§ Private litigators

§ Independent consumer groups e.g.. Choice

Reserve Bank of Australia

RBA is established by the *Reserve Bank Act 1959* (Cth). Overall Policy Role of RBA

- Set monetary policy;
- Maintain a strong financial system; and
- Issue national currency:
 - Monitor payments system.
 - Manages gold and foreign exchange reserves.

The Financial Sector Reform (Amendments and Transitional Provisions) Act set two boards

- Payment System Board: responsible for the payment system policy.
- Reserve Bank Board: all matters other than payment system policy.

Australian Prudential Regulatory Authority (APRA)

- Recommended by the Wallis Committee, APRA was established as a single **prudential regulator** for all institutions involved taking deposits, insurance or superannuation.
- **Prudential regulation**: ensure risks taken by these institutions within reasonable limits so that they are able to meet their obligations to their customers so as to protect the stability of the Australian financial system and economy as a whole (s 11 Banking Act).
 - **Basel I** (1988): focused on capital adequacy ratio (e.g., banks maintain capital equal to at least 8% of their risk-weighted assets; divided assets into five categories based on their risks).
 - **Basel II** (2004): improved via three pillars: (1) more sophisticated capital adequacy requirements; (2) assessment of capital adequacy and enhanced supervision of capital management; (3) transparency through substantially increased disclosure requirements.
 - **Basel III** (2010): reforms after the Global Financial Crisis (GFC), focus also on the liquidity issues: ADIs must manage both their capital reserves and liquidity.
 - APRA, Prudential Standard APS 210 Liquidity (2018)

Australian Securities & Investment Commission

 - ASIC regulates banks
 - – Companies
 - – Financial services & products
 - – Financial markets
 - – Consumer credit
 - ASIC's Money Smart Website provides excellent banking/finance consumer protection

W2 Tutorial

Australia banking sector

1. The treasury: responsible for broad policy & regulation affecting banking/ finance
2. **RBA**: Main roles are set monetary policy, maintain a strong financial system and issue national currency
3. **APRA**: governs ADIs, superannuation, life insurance and general insurance approve ADI and issue licenses
4. FOS: independently resolve disputes **between consumers and financial services providers**
5. **ASIC**: regulate Companies, Financial Services & Products, Financial Markets. They have the power to take licences from financial advisors who breached their duties.
6. **ACCC**: consumer protection

Legal issues for *banking bad* video:

1. Fraud
2. Misconduct
3. Misleading/deceptive conduct: s. 12 DA ASIC, s. 104 48 CA
4. Duty of care/negligence: not acting the best interest of the customers. Breach of fiduciary duties.
5. Breach of trust
6. Unconsciously conduct
7. Breach of compliance with the law (?)RG175.368

Focus of week 1

- The role, functions and other important factors of the financial regulators
- Read textbook chapters

Key regulators/laws in the Australian Banking Industry

1. Reserved Bank of Australia

The Reserve Bank of Australia is Australia's central bank. It conducts monetary policy, works to maintain a strong financial system and issues the nation's currency. As well as being a policy-making body, the Reserve Bank provides selected banking and registry services to a range of Australian government agencies and to a number of overseas central banks and official institutions. It also manages Australia's gold and foreign exchange reserves.

The role and functions of the Reserve Bank are underpinned by various pieces of legislation. The Bank is a statutory authority, established by an Act of Parliament, the Reserve Bank Act 1959, which gives it specific powers and obligations. In terms of the Act, there are two Boards: the Reserve Bank Board and the Payments System Board.

The Reserve Bank Board's obligations with respect to monetary policy are laid out in Sections 10(2) and 11(1) of the Act. Section 10(2) of the Act, which is often referred to as the Bank's 'charter', says:

It is the duty of the Reserve Bank Board, within the limits of its powers, to ensure that the monetary and banking policy of the Bank is directed to the greatest advantage of the people of Australia and that the powers of the Bank ... are exercised in such a manner as, in the opinion of the Reserve Bank Board, will best contribute to:

- a. the stability of the currency of Australia;
- b. the maintenance of full employment in Australia; and
- c. the economic prosperity and welfare of the people of Australia.

The 'charter' of the Payments System Board is defined in section 10B(3) of the Act as follows:

It is the duty of the Payments System Board to ensure, within the limits of its powers, that:

- a. the Bank's payments system policy is directed to the greatest advantage of the people of Australia; and
- b. the powers of the Bank under the Payment Systems (Regulation) Act 1998 and the Payment Systems and Netting Act 1998 are exercised in a way that, in the Board's opinion, will best contribute to:
 - i. controlling risk in the financial system;
 - ii. promoting the efficiency of payments system; and
 - iii. promoting competition in the market for payment services, consistent with the overall stability of the financial system; and
- c. the powers and functions of the Bank under Part 7.3 of the Corporations Act 2001 are exercised in a way that, in the Board's opinion, will best contribute to the overall stability of the financial system.

It is important for RBA to fulfil its duty in stabilising the Australian financial system provided that the whole system affects the economic growth, unemployment rate and the overall banking industry. Failed to ensure and maintain the financial system will result in traumatic consequences such as financial crisis.

2. APRA

The Australian Prudential Regulation Authority (APRA) is an independent statutory authority that supervises institutions across banking, insurance and superannuation, and is accountable to the Australian Parliament. APRA was established by the Australian Government on 1 July 1998 following the recommendations of the Wallis Inquiry into the Australian financial system. Prudential regulation is concerned with maintaining the safety and soundness of financial institutions, such that the community can have confidence that they will meet their financial commitments under all reasonable circumstances.

APRA oversees:

- authorised deposit-taking institutions (such as banks, building societies and credit unions)
- general insurers
- life insurers
- friendly societies
- private health insurers
- reinsurance companies, and
- superannuation funds (other than self-managed funds).

The prudential regulation ensures risks taken by these institutions within reasonable limits so that they are able to meet their obligations to their customers so as to protect the stability of the Australian financial system and economy as a whole under s 11 of Banking Act.

The Basel Accords were developed over a number of years, starting in the 1980s. The BCBS was founded in 1974 as a forum for regular cooperation between its member countries on banking supervisory matters. The BCBS describes its